



**HARRINGTON RE LTD.**

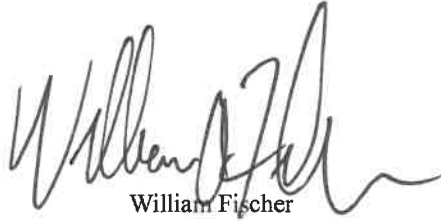
**Financial Condition Report**

**For the twelve months ended December 31, 2018**

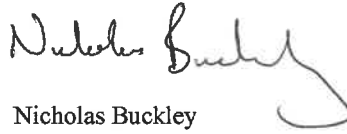
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**Declaration on Financial Condition Report**

To the best of our knowledge and belief, the financial condition report represents the financial condition of Harrington Re Ltd. (the “Company” or “Harrington Re”) in all material respects.



Name: William Fischer  
Title: Chief Executive Officer  
          (“CEO”) and President  
Date: April 30, 2019



Name: Nicholas Buckley  
Title: Chief Risk and Actuarial Officer  
Date: April 30, 2019

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**HARRINGTON RE LTD.  
FINANCIAL CONDITION REPORT  
For the twelve month period ending December 31, 2018**

Harrington Re Ltd. was incorporated under the laws of Bermuda on March 16, 2016. The Company is licensed as a Class 4 multi-line insurer under the Insurance Act 1978, amendments thereto and Related Regulations of Bermuda (the "Insurance Act") and is licensed to underwrite general business on an insurance and reinsurance basis. The Company was licensed by the Bermuda Monetary Authority (the "BMA") effective June 22, 2016, and commenced its operations subsequently. The Company provides a broad range of reinsurance products on a worldwide basis.

Harrington Re has engaged AXIS Reinsurance Managers Limited ("ARM" or the "Liability Manager"), a company incorporated in Bermuda and a wholly-owned subsidiary of AXIS Capital Holdings Limited ("AXIS Capital"), to act as its liability manager pursuant to a Services Agreement dated July 1, 2016 (the "Services Agreement"). The Liability Manager manages the day-to-day underwriting activities of the Company subject to the provisions of the Services Agreement and the oversight of the Company's management and Board of Directors (the "Board").

Pursuant to an Investment Management Agreement dated July 1, 2016 (the "Investment Management Agreement") between Blackstone Harrington Partners L.P., a Cayman Islands exempted limited partnership (the "Fund") and Blackstone Multi-Asset Advisors L.L.C., a Delaware limited liability company and an affiliate of the Blackstone Group ("BMAA"), which was assigned by BMAA to Blackstone ISG-II Advisors L.L.C., a Delaware limited liability company and an affiliate of the Blackstone Group ("BISA-II" or the "Investment Manager"), as of October 1, 2017, BISA-II serves as the investment manager of the assets of Harrington that are invested in the Fund. Harrington is the sole limited partner of the Fund. The Fund seeks to achieve attractive risk-adjusted returns through a portfolio of diversified, primarily alternative, investments.

## **Section 1 - Business and Performance**

### **a) Name of the Insurer**

Harrington Re Ltd.

### **b) Supervisors**

#### *Insurance Supervisor*

Bermuda Monetary Authority  
BMA House  
43 Victoria Street, Hamilton  
HM 12, Bermuda

### **c) Approved Auditor**

Deloitte Ltd.  
Corner House  
Church & Parliament Streets  
Hamilton HM FX, Bermuda

**d) Ownership Details**

The Company is a wholly-owned subsidiary of Harrington Reinsurance Holdings Limited (the "Parent", and together with the Company and the Fund, the "Group"). The Parent was incorporated under the laws of Bermuda on March 15, 2016.

Significant shareholders of the Parent include:

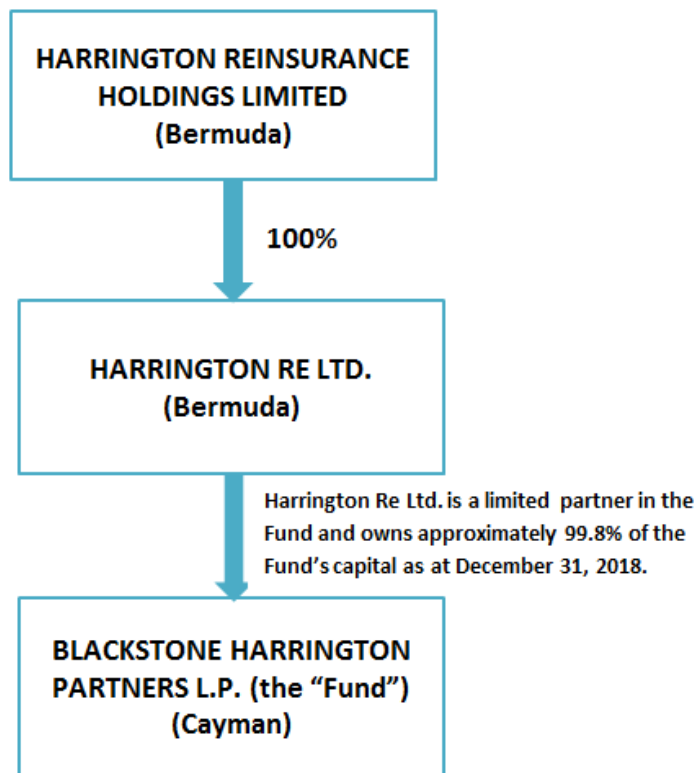
- AXIS Ventures Limited, a wholly-owned subsidiary of AXIS Capital, holds 19% of the Parent's common equity.
- The Blackstone Group L.P. ("Blackstone Group"), through a wholly-owned subsidiary, together with investment entities formed for certain senior professionals and employees of the Blackstone Group, hold in total 9.9% of the Parent's common equity.

**e) Group Structure Chart**

The following diagram provides details of the Company in the Group Structure:

**HARRINGTON REINSURANCE HOLDINGS LIMITED**

**GROUP ORGANIZATIONAL CHART**



## **f) Insurance Business Written by Business Segment and by Geographical Region**

The Company's strategy is to couple a multi-line reinsurance portfolio with a diversified alternative investment strategy in order to earn attractive risk-adjusted returns over the reinsurance cycle. The Company writes multiple lines of reinsurance business, with a focus on medium to longer tailed liabilities where the liability payout is expected to be medium to long term duration. This provides a 'premium float' which is invested in assets managed by the Investment Manager. The lines of business that the Company expects to write include motor, liability, professional lines, accident and health, credit and surety, and property lines with limited property catastrophe exposures.

The Company's consolidated financial statements, from which the financial results within this document have been derived, have been prepared in accordance with generally accepted accounting principles in the United States ("U.S. GAAP").

### **Gross Premiums Written**

The following is a summary of the Company's gross premiums written by line of business and by geographical region, for the twelve months ended December 31, 2018 and December 31, 2017 (in US\$ 000s):

<b><u>Line of Business</u></b>		<b><u>2018</u></b>		<b><u>2017</u></b>
Motor	\$	94,857	\$	5,779
Liability		66,293		92,534
Accident & Health		37,902		-
Credit & Surety		25,042		25,470
Professional		19,138		64,856
Property		7,657		10,410
Catastrophe		4,794		4,171
Agriculture		107		1,191
Other		(450)		9,805
<b>Total Gross Premiums Written</b>	<b>\$</b>	<b><u>255,340</u></b>	<b>\$</b>	<b><u>214,217</u></b>

<b><u>Region<sup>1</sup></u></b>		<b><u>2018</u></b>		<b><u>2017</u></b>
Europe	\$	129,853	\$	50,043
USA		116,737		154,550
Bermuda		6,012		4,032
Other		2,738		5,592
<b>Total Gross Premiums Written</b>	<b>\$</b>	<b><u>255,340</u></b>	<b>\$</b>	<b><u>214,217</u></b>

<sup>1</sup> Geographical region split is based on the location of the cedant and its affiliates.

## **g) Performance of Investments & Material Income & Expenses for the Reporting Period**

### **Performance of Investments for the Reporting Period**

The Company's investments are comprised of fixed maturities, investments in funds, and other securities managed by BISA-II in the Fund. The Fund is a Cayman Islands exempted limited partnership that was formed on August 20, 2015 and commenced operations on July 5, 2016. Blackstone Harrington Associates L.L.C., a Delaware limited liability company serves as the general partner of the Fund (the "General Partner"). The Company is the sole limited partner of the Fund. The Investment Manager provides certain administrative and investment management services to the Fund, including the investigation, evaluation, selection, allocation, negotiation, structuring, commitment to, monitoring of and disposition of the Fund's investments (including allocation of the Fund's assets among investment strategies). The General Partner and the Investment Manager are affiliates of the Blackstone Group.

The Fund seeks to achieve attractive risk-adjusted returns through investing in a portfolio of diversified, primarily alternative, investments.

The following table summarizes the fair value of the Fund's securities grouped by investment strategy held by the Fund as at December 31, 2018 and 2017 (in US\$ 000s):

<b>Strategy</b>	<b>2018</b>	<b>2017</b>
Investment Grade	\$ 100,986	\$ -
Liquid Multi-Strategy Funds	141,830	328,856
Long Credit	105,375	105,370
Liquid Credit Alternative	191,450	180,028
Private Credit Alternative	35,971	15,999
Real Estate Liquid Credit	107,723	16,136
Private Equity	42,902	19,041
Private Real Estate	119,180	30,252
Tactical Opportunities	30,981	18,196
<b>Total Invested Assets</b>	<b>876,398</b>	<b>713,878</b>
Senior Secured Facility Borrowings	(55,000)	(55,000)
Other Balances	12,274	(2,104)
<b>Limited Partner Net Asset Value at Year End</b>	<b>\$ 833,672</b>	<b>\$ 656,774</b>

For the year ending December 31, 2018 the Fund generated a net investment return of \$9.6 million, or a net investment return on total invested assets of 1.5%<sup>2</sup>. The Fund's net investment return during the year primarily resulted from positive performance in Private Equity and Private Real Estate (which contributed 0.72%<sup>3</sup> and 0.86%, respectively, to the Fund's total net investment gain).

For the year ending December 31, 2017 the Fund generated a net investment return of \$35.4 million, or a net investment return on total invested assets of 5.6%. The Fund's net investment return during the year primarily resulted from positive performance in the Credit Alternatives and Liquid Multi-Strategy Funds asset classes (which contributed 2.38% and 1.32%, respectively, to the Fund's total net investment gain).

<sup>2</sup> The net investment return reflects the total investment return generated by the Fund less the Fund's expenses and fees excluding the interest expense related to the Fund's senior borrowing facilities, divided by the period's average invested assets of the Fund that are attributable to Harrington Re as the Limited Partner of the Fund.

<sup>3</sup> The net return contribution from individual asset classes includes unrealized and realized appreciation / (depreciation), expenses, and management and performance fees.

### Material Income & Expenses for the Reporting Period

The Company's main revenue source is reinsurance premiums and, in line with the Harrington Re accounting policy, reinsurance premiums are recorded at the inception of the contract and are estimated based upon information received from ceding companies. Harrington Re sources reinsurance premiums through quota-share and facultative cessions from companies in the AXIS Capital group, as well as from other third-party cedants as recommended by its Liability Manager. For the period from inception to December 31, 2018, the Company wrote business solely through reinsurance treaties with entities in the AXIS Capital group.

The Company's major expense arises from claims losses, and the reserve for losses and loss expenses is reviewed on a quarterly basis. Case reserves (reported claims) are primarily established based on amounts reported by the ceding companies. During the period from inception through December 31, 2018 the Company received a limited quantum of actual losses reported with the reserve for loss and loss expenses primarily representing an estimate of losses incurred but not yet reported ("IBNR"). Management determines booked IBNR loss reserves after reviewing detailed actuarial analyses and applying informed judgment regarding qualitative factors that may not be fully captured in the actuarial estimates.

The reinsurance industry was exposed to a number of severe natural catastrophe events in the second half of 2018 that, in general, made it a very challenging year for many market participants. The Company's decision to limit natural catastrophe exposures as part of its strategy served it well during 2018 with aggregate natural catastrophe losses equating to \$5.3m, which is less than 1% of shareholder's equity.

The following presents the Company's financial performance for the years ended December 31, 2018 and 2017 (all in US\$ 000s):

	<u>For the Year Ended</u> <u>December 31, 2018</u>	<u>For the Year Ended</u> <u>December 31, 2017</u>
<b>Gross Premiums Written</b>	<b>\$ 255,340</b>	<b>\$ 214,217</b>
Net Premium Earned	285,675	162,067
Losses and Loss Expenses	(223,511)	(120,408)
Acquisition Costs	(66,824)	(57,777)
Underwriting-related General and Administrative Expenses	(11,898)	(9,028)
Underwriting Loss	<u>(16,558)</u>	<u>(25,146)</u>
Net Investment Income	9,827	35,432
Other Items	3,012	(54)
<b>Net Income (Loss)</b>	<b>\$ <u>(3,719)</u></b>	<b>\$ <u>10,232</u></b>

### **h) Other Material Information**

No other material information to report.

## Section 2 - Governance Structure

The Company's governance structure is established to:

- Maximize shareholder value over the long-term through diligent oversight of policies, processes and decisions taken by the Company's executive management and Board of Directors;
- Ensure high standards of enterprise risk management are implemented and maintained;
- Ensure the business is operating in an efficient and effective manner; and
- Align control procedures within the organization based on identified risks.

### a) **Board and Senior Executives**

#### **Directors:**

*The Board of Directors is comprised of the following individuals:*

<b>Name</b>	<b>Board Position</b>
Robert Friedman	Chairman of the Board /Chair of the Audit and Risk Committee
Peter Durhager	Board Member/Chair of the Compensation Committee
Martin Alderson Smith	Board Member/Chair of the Investment Committee
Ben Rubin	Board Member/Chair of the Underwriting Committee
William Fischer	Board Member

#### **Senior Officers:**

*The Executive Team is comprised of the following individuals:*

<b>Name</b>	<b>Board Position</b>
William Fischer	CEO and President
Greg Rymon-Lipinski	Chief Financial Officer
Nicholas Buckley	Chief Risk Officer and Chief Actuary

#### *i) Board and Senior Executive Structure, role, responsibilities and segregation of responsibilities.*

The Board of Directors of Harrington Re Ltd. provides oversight of the Company through Board committees and involvement of the executive team, and comprises individuals who meet the Fit and Proper criteria set out in the Schedule to the Insurance Act 1978. The Board comprises five directors and includes the Company's Chief Executive Officer (the "CEO"), a representative from each of the Company's sponsors, AXIS Capital and Blackstone Group (the "Sponsors"), as well as two independent directors. Board members must understand (i) the Company's Bye-Laws, the Code of Business Conduct, the Corporate Governance Principles and all other relevant company policies concerning corporate governance; and (ii) how the policies are enforced to help protect against illegal or unethical conduct.



The annual duties of the Board include the following:

- Setting and overseeing the implementation of business objectives and strategies;
- Approving corporate policies and procedures;
- Oversight of the integrity and effectiveness of the Risk Management Function;
- Oversight of risk funding and ensuring the adequacy of the Company's financing facilities;
- Approving financial results and statutory filings;
- Approving external audit fees;
- Ensuring that the Company is compliant with the BMA's Insurance Code of Conduct;
- Appointment of internal auditors;
- Electing Officers, the Principal Representative and Committee members;
- Review of Board Committee charters;
- Review of Directors' and Officers' insurance coverage; and
- Approving the remuneration of non-executive directors.

The Board also selects and evaluates the performance of the CEO and other senior executive officers.

Committee Governance and Oversight:

The following committees have been established by the Board as part of its overall responsibility for corporate governance:

1. *Audit and Risk Committee:* The purpose of this committee is to assist the Board in its oversight of (i) the integrity of the Company's financial statements, (ii) the Company's internal controls, including the internal controls that exist at the Company's liability and asset managers, to the extent they affect the adequacy and effectiveness of the Company's respective financial, operating, compliance and risk management controls, (iii) to assist the Board in overseeing the integrity and effectiveness of the Company's risk management framework and to ensure that the Company's risk assumption and risk mitigation activities are consistent with that framework. (iv) the Company's compliance with legal and regulatory requirements, (v) the independent auditors' qualifications and independence, and (vi) the Company's internal audit function. In fulfilling its purpose, the committee shall maintain free and open communication with the Company's independent auditors, the Company's internal auditors and management.
2. *Underwriting Committee:* The purpose of this committee is to assist the Board in overseeing the Company's underwriting strategy and activities.
3. *Investment Committee:* The purpose of this committee is to assist the Board in overseeing the Company's investment strategy and activities.
4. *Compensation Committee:* The purpose of this committee shall be to: (i) determine the compensation of the Chief Executive Officer, (ii) to make recommendations to the Board with respect to employee compensation, incentive compensation plans and equity-based compensation plans, and (iii) take a leadership role in shaping the Company's compensation policies.

Each committee shall consist of no fewer than three directors, as determined by the Board, except that AXIS Capital and Blackstone Group shall each have the right to appoint one committee member to each committee. Each committee shall meet at least once per calendar quarter or more frequently as circumstances dictate. All committee reports are presented to the Board.

## Executive Team

The Company's executive team consists of the following individuals:

1. William Fischer – President and Chief Executive Officer, who also serves as the chief underwriting officer for the Company
2. Greg Rymon-Lipinski – Chief Financial Officer and Principal Representative
3. Nicholas Buckley – Chief Risk Officer and Chief Actuary

Each of the members of the executive team is responsible for the resource and information needs that are required to support their respective functions, including the management of services provided by the Liability Manager and the Investment Manager, as well as the functions performed by the outsourced service providers that are discussed further below.

### *ii) Remuneration Policy*

The Company believes that the retention of its key members of management is critical to the success of the Company and the achievement of its strategic objectives. The Company's executive compensation policy was designed to retain and reward management who create long-term value for our shareholders. The remuneration policy provides a fixed base salary along with an annual performance-based bonus which varies in accordance with both the Company's and individual's performance. Additionally, senior executives receive stock options accompanied by long term incentives to align with the Company's goal of sustained success. Such amounts are approved by the Board's Compensation Committee. The Company may also provide reimbursements for a certain amount of personal travel, and in some cases for housing allowances to help defray the costs of maintaining a second residence for executives who are working away from their home countries. The Company also provides certain other perquisites and benefits, such as a general health plan, which the Company believes will give the executives security and convenience that will allow them to focus their attention on carrying out their responsibilities for Harrington Re.

Compensation for our independent directors consists of cash compensation in the form of annual retainers for Board and Committee service. Directors who are also employees of Harrington Re, AXIS Capital or the Blackstone Group do not receive compensation for their service as directors. The Company's Chairman of the Board, who is an independent director, receives an additional retainer.

### *iii) Pension or Early Retirement Schemes for Members, Board and Senior Employees*

For purposes of providing employees with retirement benefits, the Company maintains self-directed defined contribution retirement plans in Bermuda. Contributions are based on the participants' eligible compensation. The contributed funds are invested in one of the Company's pension investment portfolios based on the employee's preference, which is administered by a third party advisor. The Company does not have any early retirement schemes.

### *iv) Shareholder Controllers, Persons who Exercise Significant Influence, the Board or Senior Executive Material Transactions*

Certain directors and executive officers of the Company acquired common shares of the Parent, as part of the Parent's capital raising initiatives completed during 2016.

AXIS Capital also participated in the capital raising activities of the Parent, acquiring 19% of the Parent's common stock. An entity in the AXIS Capital group serves as the exclusive liability manager for the Company. All reinsurance business written since inception through December 31, 2018 was entered into with companies in the AXIS Capital group.

The Blackstone Group through a wholly-owned subsidiary, together with investment entities formed for certain senior professionals and employees of the Blackstone Group, purchased in total 9.9% of the Parent's common equity. An affiliate of the Blackstone Group serves as the Company's exclusive investment manager.

**b) Fitness and Propriety Requirements**

*i) Fit and Proper Process in assessing the Board and Senior Executives*

Harrington Re Ltd. places a high value on appointing fit and proper persons and seeks to ensure that each person hired is suitably qualified to do the job for which he or she is being recruited and that he or she is honest and trustworthy.

The Company's Board has adopted a Fit and Proper Policy and Procedures to provide guidance to ensure appropriate processes are undertaken to assess and document the fitness and propriety of the Company's Board and senior executives.

As part of the Fit and Proper Policy and Procedures, each candidate for a Board or senior executive position is assessed to determine whether he or she is fit for the particular role; specifically with reference to competency and capability. Each candidate is assessed to determine whether he or she meets Harrington Re's standards for probity; specifically with reference to honesty, integrity, fairness, ethical behavior and financial soundness.

This recruitment process includes the following:

- A written job description setting forth the duties and responsibilities of the role,
- A process (i.e. number and diversity of interviews) that matches the person with the requirements of the role, and
- Verification of qualifications, experience, references and professional memberships.

The annual performance review process for each director and senior executive includes continuing consideration of fitness and probity.

Executive management is authorized to hire middle management and other staff to ensure there is sufficient expertise to achieve the Company's objectives. The Human Resources function arranges background screening and other support for all hires to ensure appropriate alignment with Harrington Re's values and culture.

*ii) Board and Senior Executives Professional Qualifications, Skills and Expertise*

**Board of Directors:**

1. Robert Friedman (Chairman of the Board and Director) – Robert Friedman is the Chairman of the Harrington Re Board of Directors. Mr. Friedman is a former Senior Managing Director of the Blackstone Group. Mr. Friedman joined the Blackstone Group in 1999 and served as Chief Legal Officer of the firm from January 2003 through July 2010 and was also the firm's Chief Administrative Officer during most of that period. He retired as a Senior Managing Director in June 2012 and has served as a Senior Advisor of the Blackstone Group since that date. Before joining the Blackstone Group, Mr. Friedman was a partner with Simpson Thacher & Bartlett for 25 years, where he was a senior member of that law firm's mergers and acquisitions practice. Mr. Friedman graduated from Columbia College and the University of Pennsylvania Law School. He currently serves as a Director of AXIS Capital Holdings Limited and YRC Worldwide Inc. He is also a member of the Boards of Directors of United Way of New York City, New Alternatives for Children, the Nantucket Land Council and the Institute for Law and Economics of the University of Pennsylvania.
2. Peter Durhager (Director) – Peter Durhager is a member of the Harrington Re Board of Directors. Mr. Durhager is the former President of Renaissance Services Ltd. and a former Chief Administrative Officer of Renaissance Re

Holdings Ltd. Mr. Durhager was the President at Renaissance Services Ltd. from March 2004 until December 2014 and the Chief Administrative Officer of the global reinsurer, Renaissance Re Holdings Ltd., from June 2003 until December 2014 and its Executive Vice President from February 2010 until December 2014. He served as the Chief Administrative Officer of Renaissance Services Ltd. from June 2003 until his retirement in December 2014. Mr. Durhager served as Deputy Chairman at Ascendant Group Ltd. from June 1, 2012 until his election as Chairman in 2014. He currently serves as Chairman of the Board of Ascendant Group Ltd. Peter co-founded Promisant Holdings Ltd. and served as its President and Chief Operating Officer from January 2000 to February 2003. He served as Vice Chairman of Promisant Holdings Ltd. from 1999 to 2003. Mr. Durhager also served as Chief Executive Officer of Logic Communications Ltd. from January 1996 to December 1999 and Chairman from 1995 to 1999. From 1997 to 1999, he served as President and Chief Executive Officer of Millennium International Limited. From July 1991 to December 1995, Peter served as Head of Electronic Banking & Card Services at the Bank of Butterfield. Mr. Durhager has been a Director of Ascendant Group Ltd. since 2003 and was a Director of KeyTech Limited from 2000 to 2014. Mr. Durhager served as Chairman of America's Cup Bermuda from 2015 to 2018 and the Bermuda Community Foundation from 2014 to 2019. He is also a Non-Executive Director of F&G Re Ltd. and F&G Life Re Ltd as well as Somers Limited. He is a Member of the Institute of Directors (IOD), the National Association of Corporate Directors (NACD) and Young Presidents Organization (YPO). Mr. Durhager holds a bachelor's degree in Philosophy from Transylvania University in Lexington, Kentucky.

3. *Martin Alderson Smith (Director)* - Martin Alderson Smith is a member of the Harrington Re Board of Directors. Mr. Alderson Smith is a Senior Managing Director and Chief Operating Officer of Blackstone Insurance Solutions. Mr. Alderson Smith manages the development and distribution of tailored solutions for insurance companies worldwide. Before taking up his current role, Mr. Alderson Smith was Head of Corporate Development working on firm wide strategy and evaluation of new business initiatives. Mr. Alderson Smith was formerly the Managing Partner of Blackstone's M&A advisory business and a Senior Managing Director in the Financial Institutions Group. In that capacity, he worked on a wide array of insurance and asset management projects, including representing the State Regulators of New York, New Jersey, Iowa, Maryland and Washington on the proposed demutualization and conversion of John Hancock, MetLife, Prudential, Principal, Carefirst and Premera Blue Cross. He also was retained by the Commonwealth of Pennsylvania Insurance Department to review a number of corporate transactions including the affiliation of Highmark with West Penn Allegheny Health System, and Highmark's acquisition of Blue Cross of Northeastern Pennsylvania. In addition, he has advised clients including Aviva, State Street, AIG and Ullico on a spectrum of acquisitions, divestitures and partnership transactions. He is a Blackstone designated Director of Patria Inverimentos S.A. Before joining Blackstone in 1991, Mr. Alderson Smith was with First Boston in London and New York for eight years. Mr. Alderson Smith holds an MA from Oxford University and an MBA from Harvard Business School.
  
4. *Ben Rubin (Vice-Chairman and Director)* - Ben Rubin is the Vice-Chairman of the Harrington Re Board of Directors. Mr. Rubin was appointed Executive Vice President at AXIS Re to lead the company's third party capital business in 2013. Prior to joining AXIS, Mr. Rubin worked at Merrill Lynch in insurance investment banking where his experience encompassed capital raising, mergers and acquisitions and risk transfer solutions globally. Responsible for originating, structuring and executing financing and capital solutions across the insurance sector, Mr. Rubin has significant experience introducing alternative sources of capital into the insurance and reinsurance market. Mr. Rubin earned his bachelor's degree in history from Cornell University and his Master of Business Administration from Columbia Business School.

5. William Fischer (Director) – see biography below.

The Executive Team:

1. William Fischer (CEO, President and Director) – William Fischer is the Chief Executive Officer of Harrington Re and has over 32 years of reinsurance industry experience. Prior to joining Harrington Re, Mr. Fischer served as the Chief Underwriting Officer for the global Reinsurance operations of AXIS Capital, and had worked at AXIS Capital since the company's inception in 2001, helping to found the company. Mr. Fischer played an integral role in building AXIS Capital's global reinsurance business to over \$20 billion in cumulative gross written premium across 14 lines of business with experience leading and managing all aspects of the business including underwriting, risk and capital management. Mr. Fischer moved to Bermuda in 2001 to build the reinsurance business and served as President and Chief Executive Officer of AXIS Reinsurance. Mr. Fischer returned to the United States from Bermuda in June 2011 to assume the role of Chief Underwriting Officer for AXIS Reinsurance globally. Prior to joining AXIS, Mr. Fischer was Executive Vice President at Everest Re Group and had responsibilities for a variety of reinsurance product lines including property, accident and health and financial products. Mr. Fischer previously worked at Transatlantic Reinsurance in both the London and New York offices and began his reinsurance career at Skandia America Group in 1987. Prior to reinsurance Mr. Fischer was a design engineer with Honeywell. Mr. Fischer has both a Bachelor of Science in Engineering and a Master of Business Administration from Columbia University as well as graduating from the prestigious Challenge of Leadership program at Insead.
2. Greg Rymon-Lipinski (Chief Financial Officer and Principal Representative) – Greg Rymon-Lipinski is the Chief Financial Officer at Harrington Re. Mr. Rymon-Lipinski has over 20 years of professional experience in the (re)insurance industry. Prior to joining Harrington Re, Mr. Rymon-Lipinski led the external financial reporting function at AXIS Capital. As part of his role at AXIS Capital, Greg was primarily responsible for meeting the internal and external financial reporting requirements, providing corporate finance and accounting expertise to other AXIS Capital group functions, including investor relations, treasury and corporate development teams, as well as the oversight of the group accounting policies. Prior to joining AXIS Capital in 2013, Mr. Rymon-Lipinski was employed at the global reinsurer, PartnerRe Ltd. as the Head of External Reporting. Between 1997 and 2010, Mr. Rymon-Lipinski was employed by the global accounting firm PricewaterhouseCoopers ("PwC"), most recently as a Director, with a focus on the insurance and reinsurance industry. At PwC, his primary responsibilities included the management of audits of large listed (re)insurance clients, leading local regulatory compliance audits, and the management of consulting engagements such as due diligence reviews, corporate governance analyses, internal controls projects and operational efficiency engagements. Mr. Rymon-Lipinski holds a Bachelor of Commerce Honors degree in Accounting and Auditing from the University of the Witwatersrand and is a member of the Chartered Professional Accountants of Bermuda and the South African Institute of Chartered Accountants.
3. Nicholas Buckley (Chief Risk Officer and Chief Actuary) – Nicholas Buckley is the Chief Risk and Actuarial Officer at Harrington Re. Mr. Buckley has over 20 years of experience in the non-life insurance industry, most recently with AXIS Capital, where he held the roles of Chief Risk Officer for AXIS Re Europe SE and Senior Vice President within the Group Risk Team. Mr. Buckley joined AXIS Capital in 2008, playing an integral role in the development and build out of AXIS Capital's Risk function and Enterprise Risk Management framework. During the years 2001 to 2008 Mr. Buckley was a member of the Remetrics team at reinsurance broker Benfield (now part of Aon Benfield) where he worked on a wide range of reinsurance risk modeling and advisory projects. Mr. Buckley also held the position of Vice President at XL Financial Solutions working on non-traditional reinsurance. He began his career at the actuarial consultancy Tillinghast-Towers Perrin (now part of Willis Towers Watson) where he worked on a variety of reserving and financial modeling assignments. Mr. Buckley graduated from the University of

Manchester with a joint honors degree in Mathematics and Physics and has been a Fellow of the Institute of Actuaries since 2000.

**c) Risk Management and Solvency Self-Assessment**

*i) Risk Management Process & Procedures to Identify, Measure, Manage and Report on Risk Exposures*

The mission of the Enterprise Risk Management (“ERM”) function at Harrington Re is to promptly identify, measure, manage, monitor and report risks that affect the achievement of the Company’s strategic, operational and financial objectives. The Company’s major risk management objectives are to:

- Protect Harrington Re’s capital base and earnings by ensuring that risks are not taken beyond its stated Risk Tolerances;
- Promote a sound risk management culture through disciplined and informed risk taking;
- Enhance value creation and contribute to an optimal risk-return profile by providing the basis for efficient capital deployment;
- Support decision making processes by providing reliable and timely risk information; and
- Safeguard the reputation of Harrington Re and its Sponsors.

The Company’s ERM framework provides a structured approach to ensure that risks are appropriately identified, managed, monitored and controlled with clear ownership and appropriate levels of oversight.

**Risk Identification**

Management have available a range of tools that can be used to identify material foreseeable risks to the Company. Management may use a combination of one or more tools on a regular basis to identify material risks including those indicated by the BMA. In terms of risk identification, the Risk Universe, as set forth below, describes the risk landscape that Harrington Re has determined itself exposed to. It encompasses risks common to the industry, strategic risks, assumed risks (i.e. the underwriting and market risks that Harrington Re is paid to assume), financial risks and the operational risk inherent in running the business.

The following table shows the current categorization of the Company’s Risk Universe:

<b>Harrington Re Risk Universe</b>			
<b>Strategic Risks</b>	<b>Assumed Risks</b>	<b>Financial Risks</b>	<b>Operational Risks</b>
Inappropriate Corporate Governance	Underwriting Risk	Counterparty Credit	Business Interruption
Inappropriate Enterprise Risk Management	Investment Risk	Liquidity	IT – Business Systems and Infrastructure
Risk Funding	Reserve Risk	Tax	IT – Information Security

Strategic Positioning	Claims Handling		Financial Crime
Human Resource	Natural Catastrophe Accumulation		Compliance
	Non-Natural Catastrophe Accumulation		External Financial Reporting
			Third Party Vendor Risk

The Risk Register documents the risks and sub-risks identified by the Company along with the results of the risk assessment process and the status of the Company’s Risk Controls as discussed below.

Risk Measurement/Assessment

The assessment of material risks involves the evaluation of potential risk exposure including the likelihood and severity of each of the material risks. This assessment is then translated into an overall risk assessment rating and reported in the Company’s Risk Register.

The assessment of the Company’s risks will depend upon their nature. For quantifiable risks, risk measurement techniques used may include, but are not limited to, statistical simulation models, deterministic models, stress testing and scenario analysis.

Risk Management

Each of the Company’s risks has an assigned risk owner who has overall accountability for managing the risk and ensuring that appropriate controls are in place to help manage risk exposure in line with the Company’s risk appetite and tolerances.

Harrington Re’s Risk Appetite and Tolerance Framework provides the principles, policies, and governance under which the Company assumes risk and guides the risk taking decisions in pursuit of Harrington Re’s objectives. Through the framework, Harrington Re aims to provide financial security to policyholders, while providing an optimal balance of risk, profitability, and growth for investors.

Harrington Re’s Risk Appetite and Tolerance Framework consists of:

- Qualitative statements of Risk Appetite
- Solvency Standard (policy relating to how the Company measures and holds adequate capital)
- Quantitative Risk Tolerances around risk accumulation and individual risk positions

The framework is reviewed at least annually by executive management and the Board to ensure that it remains relevant to the Company’s strategic goals, external environment and risk profile.

## Risk Reporting

The Company's Risk Register is updated and reported to the Board on a quarterly basis. The Company's key risk positions are also monitored against its Risk Tolerance framework and reported to the Board via a risk dashboard which is updated quarterly.

### *ii) Risk Management and Solvency Self-Assessment Systems Implementation*

The Company's Risk Appetite and Tolerance Framework, which is approved by the Board, includes an overall Solvency Standard and Risk Tolerances for material risks. The framework is aligned with the Company's strategic direction, operating and financial objectives. The framework is reviewed at least annually with the Board and in conjunction with the annual Commercial Insurer's Solvency Self-Assessment ("CISSA") process. The Company, in collaboration with the Liability Manager and Investment Manager, uses the framework as a critical part of the strategic processes to help determine the underwriting and investment portfolios for the Company. Risk positions are monitored against the Risk Tolerances and reviewed with the Board, Management and Sponsors on a quarterly basis. In the event of a breach of a Risk Tolerance it is the responsibility of Management and the Board to develop a risk mitigation plan articulating the actions that will be taken to move the portfolio back into tolerance.

The Company conducts an annual review of its Risk Universe in light of the changing risk environment and to ensure it continues to reflect the most up-to-date view of key risks. In line with the Company's strategy, the risk profile of the Company is dominated by investment risk and reserve risk arising out of our underwriting activities.

The Company assesses solvency requirements through a combination of regulatory and rating agency models. The exercise is conducted at least annually and identifies any deficiencies in solvency requirements. Furthermore, the Company performs stress testing using both internally defined and regulatory required scenarios on at least an annual basis. Any solvency issues noted are brought to the attention of the Board and actioned upon.

### *iii) Relationship Between Solvency Self-Assessment, Solvency Needs & Capital, and Risk Management*

The Company performs a solvency self-assessment as part of the CISSA process. The self-assessment contemplates the achievability of both short and longer term plans in the context of the Company's available resources and the identified risks to which it is exposed.

The self-assessment includes a determination of the capital required by the Company to achieve its goals in relation to external constraints such as regulatory and rating agency capital.

The analysis is performed on a forward looking basis as part of Harrington Re's business planning cycle. The Company analyzes its exposure based upon the potential impact of executing alternative strategies against the Company's Solvency Standard and Risk Tolerances. Where necessary, the Company's business plans and risk mitigation strategies are modified to ensure compliance with the Company's Risk Framework.

Reverse stress testing is also used and provides insights into scenarios that might lead to the Company's business model becoming unviable under proposed business plans.

### *iv) Solvency Self-Assessment Approval Process*

The Company's Chief Risk Officer prepares the annual Solvency Self-Assessment Report. This follows a process of consultation and review with the Harrington Re executive management team and Sponsors. The report is provided to the Board for review and approval.



#### **d) Internal Controls**

##### *i) Internal Control System*

The Company has systems, processes and procedures in place to ensure that data and reporting is reliable, organizational policies are adhered to, and adequate security measures are implemented. The Audit and Risk Committee is responsible for reviewing and evaluating financial information and disclosures, the work of the internal auditors and any significant changes in internal controls over financial reporting.

##### *ii) Compliance Function*

The Company's compliance function is overseen by executive management and is supported by external specialists. The compliance function regularly monitors applicable law, regulation and corporate requirements. The Company has access to legal and regulatory support and training, and access to specialist expertise in particular issues or jurisdictions. Compliance is the responsibility of the directors, senior management and all employees.

The Harrington Re compliance function works to ensure compliance with applicable laws, rules and standards by (i) developing and implementing policies, procedures, and guidelines, such as a Code of Business Conduct; (ii) providing training to Company's employees on compliance; and (iii) working with Company personnel to interpret and apply applicable laws, rules and standards as we conduct our business.

Harrington Re relies on legal support from its sponsor AXIS Capital for legal compliance and monitoring of legal and regulatory changes. AXIS Capital employs and properly utilizes qualified attorneys, paralegals and regulatory, finance and other professionals throughout the Company to monitor regulatory requirements and ensure compliance. Harrington Re also engages external counsel consultants and other external advisors (both in the US and Bermuda), when required to complement the AXIS Capital resources. In addition to ongoing monitoring of new and changing regulation within Bermuda and any applicable jurisdiction (through AXIS Capital legal staff and external legal firms), there is also regular and ongoing engagement by the executive management with the Bermuda regulators, ensuring that regulatory and compliance matters are appropriately reported and discussed.

#### **e) Internal Audit**

The internal audit function is an independent and objective assurance and consulting activity that is guided by a philosophy of adding value to improve the operations of the Company.

The internal audit function is currently outsourced to an independent third party who, along with its internal processes to ensure independence and objectivity from the Company, has direct access to the Audit and Risk Committee of the Board, agrees the audit plans with the Audit and Risk Committee, and provides findings reports from each audit for discussion at the Audit and Risk Committee meetings.

The internal audit function assists the Company in accomplishing its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of the organization's risk management, internal control, and governance processes.

Internal audit procedures are carried out to test adherence of practice to stated frameworks and policies. In addition, the internal audit team is responsible for reporting major internal control findings or issues to the Audit and Risk Committee to help strengthen group-level governance, assist the Board-level committee to exercise its oversight and to provide advice and recommendations to the management of Harrington Re.

## **f) Actuarial Function**

Analysis to produce quarterly actuarial reserve estimates is outsourced to AXIS Capital in their role as Liability Manager. Under this arrangement the Company benefits from the experienced actuarial reserving, pricing and modelling capabilities of AXIS Capital all of which are utilized in developing the actuarial reserve estimates put forward to Harrington Re. The Harrington Re Chief Actuary reviews the reserve estimates prepared by AXIS Capital along with the supporting analysis and information relating to risks and uncertainties present in the reserving process and inherent to the subject business. Following consideration of these analyses and the materials provided, the Harrington Re Chief Actuary prepares the final reserve recommendations for review and approval by the Company's Reserve Committee. The Reserve Committee includes all executive officers of the Company and meets at least once per quarter prior to the reserves being recorded in the Company's financial statements. The Company's reserves estimates are also presented to and reviewed by the Audit and Risk Committee of the Board each quarter.

The Company also retains external actuarial consultants who are responsible for performing an annual independent review of the Company's technical provisions and for providing the annual Statement of Actuarial Opinion required by the BMA.

## **g) Outsourcing**

### *i) Outsourcing Policy and Key Functions that have been outsourced*

The Company outsources a number of key functions and has formal policies in place with respect to contractors, consulting services and outsourcing activities.

The key functions that are outsourced include day to day underwriting activities, risk and actuarial, accounting, legal and compliance, internal audit, investment management, information technology and human resources services, all of which are based on services agreements with various third parties.

A significant portion of the Company's operational activities are outsourced to its Sponsors under long-term agreements and include the following:

#### AXIS Reinsurance Managers Limited (Liability Manager and other operational support)

Harrington Re has engaged AXIS Reinsurance Managers Limited, a wholly-owned subsidiary of AXIS Capital, to act as the Liability Manager pursuant to a long term services agreement. The Liability Manager manages the day-to-day underwriting activities of the Company subject to the provisions of the services agreement and the oversight of management and the Board of Directors of the Company. The services agreement also provides for ARM to provide certain other services to the Company, including claims handling, actuarial, risk management and information technology support as specified in the services agreement.

#### Blackstone ISG-II Advisors L.L.C. (Investment Manager)

Pursuant to an Investment Management Agreement, BISA-II serves as the investment manager of the assets of the Company that are invested in the Fund. The Company is the sole limited partner of the Fund. The Fund seeks to achieve attractive risk-adjusted returns through a portfolio of diversified, primarily alternative, investments. Pursuant to the Investment Management Agreement, the Investment Manager provides certain administrative and investment management services to the Fund, including the investigation, evaluation, selection, allocation, negotiation, structuring, commitment to, monitoring of and disposition of investments (including allocation of the Fund's assets among investment strategies).

The delivery and quality of the performance of the outsourced services is reviewed by the executive management on a periodic basis and discussed with the Harrington Re Board of Directors.

In addition, Internal Audit undertakes independent reviews of the outsourced operations to provide independent assurance that the outsourcing process is being implemented in line with Company policy.

*ii) Material Intra-Group Outsourcing*

There are no material intra-group outsourcing functions utilized by the Company.

**h) Other Material Information**

No other material information to report.

**Section 3 - Risk Profile**

**a) Material Risks the Insurer is Exposed to During the Reporting Period**

The material risks identified by the Company are summarized below according to the material risk categories defined in the Harrington Re Risk Universe:

The four major Risk Categories as identified are:

1. Strategic Risks – This category consists of risks associated with Corporate Governance (i.e. Inadequate or inappropriate board level corporate governance leading to the Company not acting in the best interests of shareholders or policyholders), Enterprise Risk Management (i.e. inappropriate or ineffective ERM framework leading to inappropriate risk culture and risk taking that prevents the Company from achieving its strategic, operational and financial objectives), Risk Funding (i.e. the risk that the Company does not have adequate or appropriate funding in place to execute its strategic objectives), Strategic Positioning (i.e. risk of disconnect between existing strategy and the external environment, thereby threatening the Company’s competitive position and its ability to ensure ongoing profitability and viability), and Human Resources (risks that impair the Company’s ability to employ adequate and appropriate staff. Includes inability to retain, motivate and/or reward staff, thereby preventing the organization from operating at full capacity and/or efficiency).
2. Assumed Risks – This category includes Underwriting (i.e. premium risk and catastrophe risk), Investment market risk (i.e. the risk of adverse movements in the valuation of assets, as well as the income from assets, as a result of movements in equity prices, interest rates, exchange rates and credit spreads.), Reserve risk (i.e. the risk that the loss reserves we have established to cover losses already incurred are insufficient), Natural Catastrophe Accumulation (i.e. the risk that the aggregation of natural catastrophe risk exposure is not understood or managed appropriately), and Non-Natural Catastrophe Accumulation (i.e. the risk that the aggregation of non-natural catastrophe exposure is not understood or managed appropriately).
3. Financial Risks – These consist of Counterparty Credit (i.e. the risk of failed or delayed premiums due to Harrington Re and/or settlements of reinsurance claims recoverable), Liquidity (i.e. the risk that Harrington Re, although solvent, either does not have available sufficient financial resources to enable it to meet its obligations as they fall due, or can secure such resources only at excessive cost), and Tax (i.e. the risk of non-compliance with tax legislation within each jurisdiction as well as the unintended tax exposure from specific transactions or business decisions).

4. Operational Risks – This category includes Business Interruption (i.e. the risk that the business is unable to respond to a major disruption to its operations), Business Systems and IT Infrastructure Risk (i.e. the risk that business systems and IT infrastructure do not meet functional and operational requirements of the business), Information Security Risk (i.e. failure to maintain the confidentiality, integrity and availability of key information assets), and Compliance (i.e. failure to comply with laws, regulations, rules, related self-regulatory standards, and codes of conduct applicable to business activities).

The Company assesses the materiality of the various risks to which it is exposed by considering both the potential likelihood and severity of each risk that is defined in the Risk Register. The assessment process may be quantitative or qualitative or a combination of both depending upon the nature of the risk. The Company also uses proprietary models, vendor models and internal scenario analysis to assist with this process.

Reserve, Investment and Underwriting risks all increased during 2018. This was in line with expectations based upon the Company's strategic objectives and growth objectives since commencing operations in July 2016.

#### **b) Risk Mitigation in the Organization**

Risks are controlled by the Company using a variety of tools and techniques. For each material risk there is a risk owner who has overall responsibility for ensuring that an appropriate control environment is designed and implemented to mitigate the risk to an agreed target risk assessment level. Risks are continuously assessed both before and after consideration of the impact of the Company's various Risk Controls. The status and effectiveness of these Risk Controls are reported to relevant stakeholders using the Risk Register.

The Company also has defined Risk Tolerances which represent the maximum amount of risk that the Board regards as acceptable to bear for certain material risk categories. The Risk Management Function reports actual risk positions against the Risk Tolerances on a quarterly basis to the Board and management via the Risk Dashboard to facilitate effective oversight. In the event of a Risk Tolerance breach the Board and management are responsible for developing an appropriate risk mitigation strategy to bring the reported risk positions back within tolerance.

#### **c) Material Risk Concentrations**

The most material areas of risk concentration relate to underwriting risk, reserve risk and investment risk as described below:

##### Underwriting Risk

The vast majority of the Company's underwriting risk is derived from premium (non-natural catastrophe) risk due to the Company's strategy to focus on medium to longer tailed lines of business. The Company monitors its non-natural catastrophe risk positions using a number of internally defined scenarios.

The Company also has exposure to natural catastrophe risk via the underwriting portfolio although this is small relative to shareholder's equity. Southeast US Hurricane is currently the most material natural catastrophe peril to which the Company is exposed, followed by California Earthquake.

##### Reserve Risk

The Company is exposed to reserve risk since there is uncertainty around the value at which the claims for which it carries loss reserves will finally settle.

In line with the Company's strategy, its reserves have grown since commencing business in 2016. This is a normal consequence of planned underwriting activities and means that reserve risk has become a more material component of the Company's risk profile over this period.

Harrington's management considers the risks and uncertainties inherent in the estimation of its loss reserves through the reserving process discussed in Section 2 (f) of this report. As part of this process the Company also retains external third party actuarial consultants to perform an independent review.

#### Investment Risk

Investment risk is determined to be the most material individual risk category that is currently borne by the Company. Potential exposures to adverse investment events are monitored and quantified to help understand the potential volatility within the portfolio.

The analysis utilizes proprietary Blackstone and third party modelling tools and considers the potential risk exposure to adverse economic scenarios that are defined by Harrington Re. Risks are modelled both by individual investment category and in the aggregate after allowing for correlation across investment types.

The Company has implemented an Investment Risk Tolerance which is designed to limit the maximum risk exposure based upon this analysis.

The Company also has strict Investment Guidelines in place as part of the Investment Management Agreement with Blackstone.

#### Economic Event Risk

The Company recognizes the potential for correlation between its investment exposures and certain underwriting exposures (for example, Credit, Professional Lines and Mortgage Reinsurance) under certain adverse economic scenarios. The Company utilizes scenario analysis to assist with the monitoring of this risk and has implemented an aggregate Economic Event Risk Tolerance for this purpose.

#### **d) Investment in Assets in Accordance With the Prudent Person Principles of the Code of Conduct**

The Company's Investment portfolio is managed by BISA-II in accordance with the Company's Investment Policy and Investment Guidelines.

In considering the prudent investment of the Company's capital, surplus and cash flow from underwriting, the Company's liquidity needs arising from potential claims activity are of primary importance. These are therefore considered in asset class participation and the asset allocation process.

A primary objective of the investment portfolio is to contribute to the positive growth in book value of the Company over time. The Company seeks to balance the investment portfolio objectives of increasing book value with the generation of attractive risk adjusted returns, while maintaining ample liquidity.

To achieve this objective the contractual and operational arrangements with the Fund have been designed to limit liquidity risk. The Company performs analysis of its liquidity profile to ensure that it is in compliance with its internal Liquidity Risk Tolerance and that to ensure that it has sufficient liquidity to meet cash flow requirements even in highly stressed underwriting scenarios.

#### **e) Stress Testing and Sensitivity Analysis to Assess Material Risks**

Harrington Re performs a variety of internal and regulatory stress and sensitivity tests to assist with the assessment of the materiality of the different risk categories to which the Company is exposed.

The results of certain stress scenarios are reported regularly via the Company's risk dashboard as part of its risk reporting. Stress scenarios are also contemplated as part of the Company's solvency self-assessment when evaluating capital adequacy. Key stress tests performed by the Company include the following:

#### Underwriting Risk

For premium risk Harrington Re monitors its exposure to a number of internally defined deterministic Non-Natural Catastrophe related realistic disaster scenarios.

For Natural-Catastrophe risk Probable Maximum Loss estimates are produced by key peril region and monitored on a quarterly basis using proprietary vendor models in conjunction with AXIS Capital.

#### Investment Risk and Economic Risks

The Company's investment portfolio is tested for the impact of sensitivity to adverse economic scenarios. The scenarios are intended to capture the potential impact to the Harrington Re portfolio due to changes in interest rates, credit spreads, equity markets and other factors.

The potential aggregate impacts of these adverse economic scenarios upon both the Underwriting and Investment Portfolios are also monitored and considered as part of the Company's framework.

#### Liquidity Risk

Harrington Re performs analysis of the liquidity profile of the Company and applies stress tests for certain claims events to ensure that it has sufficient liquidity to meet cash flow requirements even in highly stressed underwriting scenarios.

#### Reverse Stress Testing

As part of the Strategic business planning process and forward looking assessment, reverse stress testing is used to help identify scenarios that might lead to the Company's business model becoming unviable.

Based upon the results of the above tests as at December, 31 2018 the Company is compliant with its internal Risk Tolerance framework and has sufficient capital and liquidity to meet its contractual obligations upon experiencing such events.

## **Section 4 - Solvency Valuation**

### **a) Valuation Bases, Assumptions and Methods to Derive the Value of Each Asset Class**

The Company has used the valuation principles outlined by the Bermuda Monetary Authority's "Guidance Note for Statutory Reporting Regime" for the reporting period's statutory filing. The economic valuation principles outlined in this document are to measure assets and liabilities on a fair value basis, which is the value that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between open market participants at the measurement date. The fair value principles used for the assets are as follows:

Cash and cash equivalents - Cash and cash equivalents include cash and investments with original maturities of three months or less. Cash and cash equivalents are recorded at amortized cost, which approximates fair value due to the short-term, liquid nature of these securities.

Investments – The Investment Manager values investments according to U.S. GAAP which defines fair value, establishes a framework for measuring fair value, and requires enhanced disclosures regarding fair value measurements. Fair value is the amount that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date (i.e., the exit price) under current market conditions.

The Investment Manager receives market and investment specific data (“Market Data”), including quotations from market participants and pricing services, that is used to determine investment fair values. The Investment Manager evaluates Market Data received from market participants and pricing services for investments that are publicly traded as well as private assets that are not traded on an exchange and may require significant judgment when determining the valuation.

Investments in open ended registered investment companies and Undertakings for Collective Investment in Transferable Securities (“UCITS”) are valued at the published daily quotation of their net asset value.

When selecting price sources, the Investment Manager generally prioritizes fair value price sources that are most observable for each investment.

#### *Over-the-counter market prices*

Certain investments that trade on over-the-counter markets may also utilize published transaction prices when it is both readily available and representative of fair value.

#### *Market Participant and Pricing Service quotations*

Certain investments that trade on over-the-counter markets, where published transaction prices are not utilized are generally valued with indications of fair value from market participants and pricing services (“Quotations”). To determine the fair value of an investment, market participants and pricing services may consider observable market transactions for identical or similar investments, quotations by other market participants, pricing matrices or pricing relationships between investments with similar characteristics.

When evaluating quotations from a pricing service, the Investment Manager may consider the number of indications of fair value from market participants, the ability to transact at such prices based on recent trading activity, reviews of quotations and prices for similar assets, as well as other Market Data.

#### *Affiliated Investment Funds*

The fair value of investments in affiliated investment funds (“Investee Funds”) is generally determined using the reported Net Asset Value per share of the Investee Fund, or its equivalent, as a practical expedient for fair value.

Accounts and premiums receivable, advances to affiliates and other sundry assets – the carrying value of accounts and premiums receivable, advances to affiliates and other sundry assets has been used to approximate fair value due to the short maturity of these assets.

### **b) Valuation Bases, Assumptions and Methods to Derive the Value of Technical Provisions**

Insurance technical provisions are valued based on best estimate cash flows, adjusted to reflect the time value of money using a risk-free discount rate term structure with an appropriate illiquidity adjustment. In addition, there is a risk margin to reflect the uncertainty contained inherent in the underlying cash flows which is calculated using the cost of capital approach and a risk-free discount rate term structure. The discount rate term structures are prescribed by the Bermuda Monetary Authority for each reporting period.

The best estimate for the loss and loss expense provision is calculated by using U.S. GAAP reserves as the starting point and then performing a series of adjustments:

- Removal of any elements of prudence.
- Incorporation of expected reinsurance counterparty defaults.
- Incorporation of events not in data (“ENID”).

- Other adjustments related to consideration for investment expenses, etc.
- Discounting of cash flows.

The best estimate for the premium provision is calculated by using the unearned premium reserve on a U.S. GAAP basis, adjusting for bound but not incepted business as at December 31, 2018 and applying expected future loss ratios, expense ratios and appropriate claims pay-out patterns to derive cash flows which are then discounted.

As at December 31, 2018 and December 31, 2017 the Company’s technical provisions amounted to \$299.0 million and \$156.7 million, respectively, comprising the following (reported in US\$000s):

	<u>2018</u>	<u>2017</u>
Best Estimate Loss and Loss Expense Provision	268,030	134,268
Best Estimate Premium Provisions	(42,905)	(3,031)
Risk Margin	73,846	25,465

**c) Description of Recoverables from Reinsurance Contracts**

The Company did not enter into any ceded reinsurance contracts in the period from inception through December 31, 2018.

**d) Valuation Bases, Assumptions and Methods to Derive the Value of Other Liabilities**

Similar to the valuation principles for assets, the Company’s liabilities follow the valuations principles outlined by the Bermuda Monetary Authority’s “Guidance Note for Statutory Reporting Regime” which values liabilities at a fair value basis. All other liabilities are valued on a U.S. GAAP basis. The Company measures all derivative instruments at fair value. The carrying value of the remaining other liabilities has been used to approximate fair value due to the short term nature of these liabilities.

**e) Any Other Material Information**

No other material information to report.

**Section 5 - Capital Management**

**a) Eligible Capital**

*i) Capital Management Policy and Process for Capital Needs, How Capital is managed and Material Changes during the Reporting Period*

The capital management objectives of the Company are to maintain a strong capital base to support the development of its business and to meet regulatory and rating agency capital requirements at all times.

To achieve this objective Harrington Re has implemented a formal Board approved Solvency Standard that establishes target levels of capital in relation to regulatory requirements and target rating capital. The Solvency Standard is reviewed at least annually to ensure it remains appropriate in light of any changes in the Company’s business strategy, operations, risk environment or any other factors affecting its risk profile and capital resources.

The Solvency Standard considers the minimum amount of capital required to absorb shock losses and still satisfy the minimum solvency targets in relation to regulatory capital requirements and the Company’s desired rating. Harrington Re’s Solvency Standard is used to set the Company’s overall capital and solvency requirements. It is divided into four components:



1. Target Rating - Capital to support desired financial strength rating under a stress scenario. Target capital is estimated based upon requirements derived from AM Best's model in support of an A- rating. Target rating capital is stressed to reflect the occurrence of internally defined underwriting and investment events.
2. Regulatory Minimum - Capital to maintain the BMA minimum 120% of the Enhanced Capital Requirement ("ECR") under a stress scenario. Regulatory capital is also stressed to reflect the occurrence of internally defined underwriting and investment events.
3. Selected Minimum - Maximum of Target Rating and Regulatory Minimum Capital.
4. Internal Excess - Capital in excess of the Selected Minimum is considered "excess" to current needs and management should consider appropriate capital management actions.

The Chief Financial Officer, with the assistance of the CEO, the Chief Risk Officer and Sponsor resources, continuously evaluates and monitors the most effective management of capital, including issues of share equity or debt issuances to fund new strategic opportunities. Credit facilities are relied upon for provision of additional liquidity (or short-term capital relief) to the Company through credit revolvers and senior secured borrowing facilities, which have been negotiated by the Company and its Sponsors through established bank relationships.

*ii) Eligible Capital Categorized by Tiers in Accordance to the Eligible Capital Rules*

As at December 31, 2018 all of Harrington Re's eligible capital is categorized as Tier 1 capital in accordance with the Eligible Capital Rules. As at December 31, 2018 and December 31, 2017, the amount of Harrington Re's eligible capital was \$557.3 million and \$529.9 million, respectively.

*iii) Eligible Capital Categorized by Tiers in Accordance to the Eligible Capital Rules Used to Meet ECR and Minimum Solvency Margin ("MSM") Requirements of the Insurance Act*

All eligible capital is categorized as Tier 1 capital in accordance with the Eligible Capital Rules and was used to meet ECR and MSM requirements of the Insurance Act.

*iv) Confirmation of Eligible Capital That is Subject to Transitional Arrangements*

Not applicable.

*v) Identification of Any Factors Affecting Encumbrances on the Availability and Transferability of Capital to Meet the ECR*

Not applicable.

*vi) Identification of Ancillary Capital Instruments Approved by the Authority*

Not applicable.

*vii) Identification of Differences in Shareholder's Equity as Stated in the Financial Statements Versus the Available Capital and Surplus*

Other than the impact of employing statutory-based technical provision valuation techniques, the only significant differences between U.S. GAAP shareholder equity and available statutory capital and surplus relate to the reduction in available statutory capital for intangible assets and prepaid expenses.

**b) Regulatory capital requirements**

*i) ECR and MSM Requirements at the End of the Reporting Period*

The Company's target regulatory capital positions as at December 31, 2018 and December 31, 2017 (values in US\$000s) were as follows:

<b>Requirement</b>	<b>2018</b>	<b>2017</b>
Minimum Solvency Margin	127,670	107,109
Enhanced Capital Requirement	278,171	227,834

*ii) Identification of Any Non-Compliance with the MSM and the ECR*

The Company was compliant with the MSM and ECR requirements at the end of the reporting period.

*iii) A Description of the Amount and Circumstances Surrounding the Non-Compliance, the Remedial Measures and Their Effectiveness*

As at December 31, 2018, the Company was in compliance with all requirements of the Insurance Act.

*iv) Where the Non-Compliance is not Resolved, a Description of the Amount of the Non-Compliance*

Not applicable.

**c) Approved Internal Capital Model**

*i) Description of the Purpose and Scope of the Business and Risk Areas Where the Internal Model is Used*

Not applicable.

*ii) Where a Partial Internal Model is Used, Description of the Integration with the BSCR Model*

Not applicable.

*iii) Description of Methods Used in the Internal Model to Calculate the ECR*

Not applicable.

*iv) Description of Aggregation Methodologies and Diversification Effects*

Not applicable.

*v) Description of the Main Differences in the Methods and Assumptions Used for the Risk Areas in the Internal Model Versus the BSCR Model*

Not applicable.

*vi) Description of the Nature & Suitability of the Data Used in the Internal Model*

Not applicable.

*vii) Any Other Material Information*

Not applicable.

## **Section 6 - Subsequent Events**

The Company has completed its subsequent events evaluation for the period subsequent to the balance sheet date of December 31, 2018 through April 30, 2019, the date of the filing of this financial condition report, and concluded that there are no subsequent events requiring disclosure.