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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

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**FORM 10-Q**

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Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

for the period ended September 30, 2013,

or

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number 1-31599

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**ENDURANCE SPECIALTY HOLDINGS LTD.**

(Exact Name of Registrant as Specified in Its Charter)

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**Bermuda**  
(State or other jurisdiction of  
incorporation or organization)

**98-0392908**  
(I.R.S. Employer  
Identification No.)

**Wellesley House  
90 Pitts Bay Road  
Pembroke HM 08, Bermuda**  
(Address of principal executive offices, including postal code)

**Registrant's Telephone Number, Including Area Code: (441) 278-0400**

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

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

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

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Description of Class	Common Shares Outstanding as of November 1, 2013
Ordinary Shares - \$1.00 par value	44,335,250

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**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(In thousands of United States dollars, except share amounts)

	<u>SEPTEMBER 30,</u> <u>2013</u>	<u>DECEMBER 31,</u> <u>2012</u>
	<u>(UNAUDITED)</u>	
<b>ASSETS</b>		
Investments		
Fixed maturity investments, available for sale at fair value (amortized cost: \$4,759,092 and \$4,728,596 at September 30, 2013 and December 31, 2012, respectively)	\$ 4,800,838	\$ 4,868,150
Short-term investments, available for sale at fair value (amortized cost: \$11,600 and \$42,224 at September 30, 2013 and December 31, 2012, respectively)	11,599	42,230
Equity securities, available for sale at fair value (cost: \$246,288 and \$76,997 at September 30, 2013 and December 31, 2012, respectively)	262,866	86,997
Other investments	594,156	517,546
Total investments	5,669,459	5,514,923
Cash and cash equivalents	789,999	1,124,019
Premiums receivable, net	1,006,227	601,952
Insurance and reinsurance balances receivable	123,777	105,663
Deferred acquisition costs	197,048	168,252
Prepaid reinsurance premiums	263,499	166,702
Reinsurance recoverable on unpaid losses	513,080	691,783
Reinsurance recoverable on paid losses	428,300	83,159
Accrued investment income	21,783	27,166
Goodwill and intangible assets	167,000	172,000
Deferred tax asset	50,148	43,501
Net receivable on sales of investments	124,236	9,144
Other assets	192,104	86,708
Total assets	<u>\$ 9,546,660</u>	<u>\$ 8,794,972</u>
<b>LIABILITIES</b>		
Reserve for losses and loss expenses	\$ 4,052,102	\$ 4,240,876
Reserve for unearned premiums	1,314,687	965,244
Deposit liabilities	17,577	22,220
Reinsurance balances payable	347,048	110,843
Debt	527,506	527,339
Net payable on purchases of investments	224,473	81,469
Other liabilities	224,257	136,384
Total liabilities	<u>6,707,650</u>	<u>6,084,375</u>
Commitments and contingent liabilities		
<b>SHAREHOLDERS' EQUITY</b>		
Preferred shares		
Series A and B, total liquidation preference \$430,000 (2012 - \$430,000)	17,200	17,200
Common shares		
Ordinary – 44,249,622 issued and outstanding (2012 – 43,116,394)	44,250	43,116
Additional paid-in capital	560,204	527,915
Accumulated other comprehensive income	69,457	152,463
Retained earnings	2,147,899	1,969,903
Total shareholders' equity	<u>2,839,010</u>	<u>2,710,597</u>
Total liabilities and shareholders' equity	<u>\$ 9,546,660</u>	<u>\$ 8,794,972</u>

See accompanying notes to unaudited condensed consolidated financial statements.

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
**AND COMPREHENSIVE INCOME**

(In thousands of United States dollars, except share and per share amounts)

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2013	2012	2013	2012
<b>Revenues</b>				
Gross premiums written	\$ 544,363	\$ 621,255	\$ 2,294,435	\$ 2,286,980
Ceded premiums written	(149,030)	(107,175)	(525,566)	(445,431)
Net premiums written	395,333	514,080	1,768,869	1,841,549
Change in unearned premiums	158,212	37,792	(251,872)	(358,702)
Net premiums earned	553,545	551,872	1,516,997	1,482,847
Net investment income	38,097	45,882	119,870	134,723
Net realized and unrealized investment (losses) gains	(6,640)	10,097	9,967	30,258
Total other-than-temporary impairment losses	(190)	(126)	(1,575)	(274)
Portion of loss recognized in other comprehensive income (loss)	—	(5)	—	(483)
Net impairment losses recognized in earnings	(190)	(131)	(1,575)	(757)
Other underwriting (loss) income	(943)	(1,347)	694	(1,663)
<b>Total revenues</b>	<b>583,869</b>	<b>606,373</b>	<b>1,645,953</b>	<b>1,645,408</b>
<b>Expenses</b>				
Net losses and loss expenses	339,036	407,523	917,064	1,016,187
Acquisition expenses	78,775	88,782	222,279	229,399
General and administrative expenses	67,470	52,715	215,307	181,365
Amortization of intangibles	1,652	2,434	5,378	7,988
Net foreign exchange losses (gains)	2,201	3,774	8,496	(14,699)
Interest expense	9,048	9,041	27,138	27,132
<b>Total expenses</b>	<b>498,182</b>	<b>564,269</b>	<b>1,395,662</b>	<b>1,447,372</b>
Income before income taxes	85,687	42,104	250,291	198,036
Income tax expense	(2,271)	(1,986)	(5,557)	(2,893)
<b>Net income</b>	<b>83,416</b>	<b>40,118</b>	<b>244,734</b>	<b>195,143</b>
Preferred dividends	(8,188)	(8,188)	(24,564)	(24,564)
<b>Net income available to common and participating common shareholders</b>	<b>\$ 75,228</b>	<b>\$ 31,930</b>	<b>\$ 220,170</b>	<b>\$ 170,579</b>
<b>Comprehensive income</b>				
Net income	\$ 83,416	\$ 40,118	\$ 244,734	\$ 195,143
Other comprehensive income (loss)				
Net unrealized holding gains (losses) on investments arising during the period (net of other-than-temporary impairment losses recognized in other comprehensive income (loss), reclassification adjustment and applicable deferred income taxes of \$8,582 and (\$1,576) for the nine months ended September 30, 2013 and 2012, respectively)	29,079	38,290	(82,016)	60,706
Foreign currency translation adjustments	8,918	4,675	(1,057)	2,075
Reclassification adjustment for net losses on derivative designated as cash flow hedge included in net income	22	22	67	66
Other comprehensive income (loss)	38,019	42,987	(83,006)	62,847
<b>Comprehensive income</b>	<b>\$ 121,435</b>	<b>\$ 83,105</b>	<b>\$ 161,728</b>	<b>\$ 257,990</b>
<b>Per share data</b>				
Basic earnings per common share	\$ 1.70	\$ 0.74	\$ 5.04	\$ 3.94
Diluted earnings per common share	\$ 1.70	\$ 0.74	\$ 5.04	\$ 3.94
Dividend per common share	\$ 0.32	\$ 0.31	\$ 0.96	\$ 0.93

See accompanying notes to unaudited condensed consolidated financial statements.

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN**  
**SHAREHOLDERS' EQUITY**  
(In thousands of United States dollars)

	NINE MONTHS ENDED SEPTEMBER 30,	
	2013	2012
Preferred shares		
Balance, beginning and end of period	\$ 17,200	\$ 17,200
Common shares		
Balance, beginning of period	43,116	43,087
Issuance of common shares, net of forfeitures	1,452	207
Repurchase of common shares	(318)	—
Balance, end of period	44,250	43,294
Additional paid-in capital		
Balance, beginning of period	527,915	526,910
Issuance of common shares, net of forfeitures	29,961	1,182
Repurchase of common shares and share equivalents	(14,266)	—
Settlement of equity awards	(2,975)	(3,234)
Stock-based compensation expense	19,569	8,426
Balance, end of period	560,204	533,284
Accumulated other comprehensive income		
Cumulative foreign currency translation adjustments:		
Balance, beginning of period	12,676	9,609
Foreign currency translation adjustments	(1,057)	2,075
Balance, end of period	11,619	11,684
Unrealized holding gains on investments, net of deferred taxes:		
Balance, beginning of period	141,731	122,815
Net unrealized holding (losses) gains arising during the period, net of other-than-temporary impairment losses and reclassification adjustment	(82,016)	60,706
Balance, end of period	59,715	183,521
Accumulated derivative loss on cash flow hedging instruments:		
Balance, beginning of period	(1,944)	(2,032)
Net change from current period hedging transactions, net of reclassification adjustment	67	66
Balance, end of period	(1,877)	(1,966)
Total accumulated other comprehensive income	69,457	193,239
Retained earnings		
Balance, beginning of period	1,969,903	1,893,576
Net income	244,734	195,143
Dividends on preferred shares	(24,564)	(24,564)
Dividends on common shares	(42,174)	(40,298)
Balance, end of period	2,147,899	2,023,857
Total shareholders' equity	\$ 2,839,010	\$ 2,810,874

See accompanying notes to unaudited condensed consolidated financial statements.

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**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands of United States dollars)

	NINE MONTHS ENDED	
	SEPTEMBER 30,	
	2013	2012
Cash flows (used in) provided by operating activities		
Net income	\$ 244,734	\$ 195,143
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Amortization of net premium on investments	39,933	16,512
Amortization of other intangibles and depreciation	15,131	17,609
Net realized and unrealized investment gains	(9,967)	(30,258)
Net impairment losses recognized in earnings	1,575	757
Deferred taxes	1,935	(6,151)
Stock-based compensation expense	19,569	8,426
Equity in earnings of other investments	(43,083)	(38,101)
Premiums receivable, net	(404,275)	(592,113)
Insurance and reinsurance balances receivable	(18,114)	(20,216)
Deferred acquisition costs	(28,796)	(49,762)
Prepaid reinsurance premiums	(96,797)	(79,184)
Reinsurance recoverable on unpaid losses	178,703	(403,954)
Reinsurance recoverable on paid losses	(345,141)	(5,765)
Accrued investment income	5,383	5,771
Other assets	(6,875)	(2,668)
Reserve for losses and loss expenses	(188,774)	685,218
Reserve for unearned premiums	349,443	438,383
Deposit liabilities	(4,643)	(3,330)
Reinsurance balances payable	236,205	67,186
Other liabilities	37,280	7,946
Net cash (used in) provided by operating activities	<u>(16,574)</u>	<u>211,449</u>
Cash flows used in investing activities		
Proceeds from sales of available for sale investments	2,382,068	2,460,861
Proceeds from maturities and calls on available for sale investments	542,059	654,976
Proceeds from the redemption of other investments	28,485	78,043
Purchases of available for sale investments	(3,094,718)	(3,224,163)
Purchases of other investments	(62,012)	(86,195)
Net settlements of other assets	(38,223)	(18,208)
Purchases of fixed assets	(10,768)	(10,446)
Net cash paid for subsidiary acquisition	(378)	(1,468)
Net cash flows used in investing activities	<u>(253,487)</u>	<u>(146,600)</u>
Cash flows used in financing activities		
Issuance of common shares, net of forfeitures	31,289	1,262
Repurchase of common shares	(14,584)	—
Settlement of equity awards	(2,975)	(3,234)
Proceeds from issuance of debt	640	812
Repayments and repurchases of debt	(624)	(1,806)
Dividends on preferred shares	(24,564)	(24,564)
Dividends on common shares	(42,174)	(40,298)
Net cash flows used in financing activities	<u>(52,992)</u>	<u>(67,828)</u>
Effect of exchange rate changes on cash and cash equivalents	(10,967)	7,841
Net (decrease) increase in cash and cash equivalents	(334,020)	4,862
Cash and cash equivalents, beginning of period	<u>1,124,019</u>	<u>890,914</u>
Cash and cash equivalents, end of period	<u>\$ 789,999</u>	<u>\$ 895,776</u>

See accompanying notes to unaudited condensed consolidated financial statements.

**ENDURANCE SPECIALTY HOLDINGS LTD.  
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS**

(Amounts in tables expressed in thousands of United States dollars, except  
for ratios, share and per share amounts)

1. General

Endurance Specialty Holdings Ltd. (“Endurance Holdings” or the “Company”) was organized as a Bermuda holding company on June 27, 2002. Endurance Holdings writes specialty lines of insurance and reinsurance on a global basis through its wholly-owned operating subsidiaries:

<u>Operating Subsidiaries</u>	<u>Domicile</u>
Endurance Specialty Insurance Ltd.	Bermuda
Endurance Worldwide Insurance Limited	England
Endurance Reinsurance Corporation of America	Delaware
Endurance American Insurance Company	Delaware
Endurance American Specialty Insurance Company	Delaware
Endurance Risk Solutions Assurance Co.	Delaware
American Agri-Business Insurance Company	Texas

2. Summary of significant accounting policies

The accompanying unaudited condensed consolidated financial statements have been prepared on the basis of accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Results for the three and nine months ended September 30, 2013 are not necessarily indicative of the results that may be expected for the year ending December 31, 2013. The unaudited condensed consolidated financial statements include the accounts of Endurance Holdings and its wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated in consolidation. Management is required to make estimates and assumptions that affect the amounts reported in the unaudited condensed consolidated financial statements and accompanying disclosures. Actual results could differ from those estimates. Among other matters, significant estimates and assumptions are used to record premiums written and ceded, to record the fair value of investments and to record reserves for losses and loss expenses and contingencies. Estimates and assumptions are periodically reviewed and the effects of revisions are recorded in the consolidated financial statements in the period that they are determined to be necessary.

The balance sheet at December 31, 2012 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. These unaudited condensed consolidated financial statements and notes thereto should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2012 contained in Endurance Holdings’ Annual Report on Form 10-K for the fiscal year ended December 31, 2012 (the “2012 Form 10-K”).

Certain comparative information has been reclassified to conform to current year presentation.



**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except  
for ratios, share and per share amounts)

2 Summary of significant accounting policies, cont'd.

There were no material changes in the Company's significant accounting and reporting policies subsequent to the 2012 Form 10-K.

In December 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standard Update ("ASU") 2011-11 "Disclosures About Offsetting Assets and Liabilities" ("ASU 2011-11"). ASU 2011-11 requires additional disclosures about financial instruments and derivative instruments relating to netting arrangements.

ASU 2011-11 was effective for interim and annual periods beginning on or after January 1, 2013, with retrospective presentation required. The Company adopted this standard effective January 1, 2013. This standard did not have a material impact on the Company's consolidated financial statements.

In February 2013, the FASB issued ASU 2013-02 "Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income" ("ASU 2013-02"). ASU 2013-02 requires entities to report, in one location, information about reclassifications out of accumulated other comprehensive income ("AOCI"). ASU 2013-02 also requires companies to report changes in AOCI balances. For significant items reclassified out of AOCI into net income in their entirety in the same reporting period, reporting (either on the face of the statement where net income is presented or in the notes to the financial statements) is required about the effect of the reclassifications on the respective line items in the statement where net income is presented. For items that are not reclassified into net income in their entirety in the same reporting period, a cross reference to other disclosures currently required under US GAAP is required in the notes. The above information must be presented in one place (parenthetically on the face of the financial statements by income statement line item or in a note to the financial statements).

ASU 2013-02 was effective for fiscal years and interim periods beginning after December 15, 2012. The Company adopted this standard prospectively on January 1, 2013. This standard resulted in an additional note to the consolidated financial statements (see Note 6).

In July 2013, the FASB issued ASU 2013-11 "Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists" ("ASU 2013-11"). ASU 2013-11 provides guidance on the presentation of unrecognized tax benefits to better reflect the manner in which an entity would settle at the reporting date any additional income taxes that would result from the disallowance of a tax position when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist.

ASU 2013-11 will be effective for annual and interim reporting periods beginning after December 15, 2013, with both early adoption and retrospective application permitted. The Company does not expect this standard to have a material impact on the Company's consolidated financial statements.

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except for ratios, share and per share amounts)

3. Investments

*Composition of Net Investment Income and of Invested Assets*

The components of net investment income for the three and nine months ended September 30, 2013 and 2012 are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Available for sale investments	\$27,889	\$ 33,946	\$ 86,036	\$105,606
Other investments	13,244	15,050	43,083	38,101
Cash and cash equivalents	752	289	2,043	978
	<u>\$ 41,885</u>	<u>\$49,285</u>	<u>\$131,162</u>	<u>\$ 144,685</u>
Investment expenses	(3,788)	(3,403)	(11,292)	(9,962)
Net investment income	<u>\$ 38,097</u>	<u>\$ 45,882</u>	<u>\$119,870</u>	<u>\$ 134,723</u>

The following table summarizes the composition of the investment portfolio by investment type at September 30, 2013 and December 31, 2012:

Type of Investment	September 30, 2013		December 31, 2012	
	Fair Value	Percentage	Fair Value	Percentage
Fixed maturity investments	\$ 4,800,838	75.6%	\$ 4,868,150	74.2%
Cash and cash equivalents <sup>(1)</sup>	689,762	10.8%	1,051,694	16.0%
Other investments <sup>(2)</sup>	594,156	9.3%	517,546	7.9%
Short-term investments	11,599	0.2%	42,230	0.6%
Equity securities	262,866	4.1%	86,997	1.3%
Total	<u>\$6,359,221</u>	<u>100.0%</u>	<u>\$6,566,617</u>	<u>100.0%</u>

- (1) Includes net receivable on sales of investments and net payable on purchases of investments.  
(2) Consists of investments in alternative funds and specialty funds.

The following table summarizes the composition by investment rating of the fixed maturity and short-term investments at September 30, 2013 and December 31, 2012. In some cases, where bonds are unrated, the rating of the issuer has been applied.

Ratings <sup>(1)</sup>	September 30, 2013		December 31, 2012	
	Fair Value	Percentage	Fair Value	Percentage
U.S. government and agencies securities	\$ 823,761	17.1%	\$ 737,535	15.0%
AAA / Aaa	1,031,149	21.4%	993,277	20.2%
AA / Aa	1,781,679	37.0%	1,821,250	37.1%
A / A	807,509	16.8%	993,307	20.2%
BBB	296,489	6.2%	219,017	4.5%
Below BBB	67,269	1.4%	143,198	2.9%
Not rated	4,581	0.1%	2,796	0.1%
Total	<u>\$ 4,812,437</u>	<u>100.0%</u>	<u>\$ 4,910,380</u>	<u>100.0%</u>

- (1) The credit rating for each security reflected above was determined based on the rating assigned to the individual security by Standard & Poor's Financial Services LLC ("Standard & Poor's"). If a rating is not supplied by Standard & Poor's, the equivalent rating supplied by either Moody's Investors Service, Inc. ("Moody's") or Fitch Ratings is used.

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except for ratios, share and per share amounts)

3. Investments, cont'd.

Contractual maturities of the Company's fixed maturity and short-term investments are shown below as of September 30, 2013 and December 31, 2012. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	September 30, 2013		December 31, 2012	
	Amortized	Fair Value	Amortized	Fair Value
	Cost		Cost	
Due within one year	\$ 128,110	\$ 129,417	\$ 136,283	\$ 137,567
Due after one year through five years	1,775,192	1,787,984	1,725,927	1,765,662
Due after five years through ten years	265,740	266,962	410,755	429,099
Due after ten years	27,207	27,847	29,654	33,803
Residential mortgage-backed securities	1,235,668	1,240,222	1,252,468	1,280,579
Commercial mortgage-backed securities	872,259	889,460	741,178	781,379
Asset-backed securities	466,516	470,545	474,555	482,291
Total	\$ 4,770,692	\$ 4,812,437	\$ 4,770,820	\$ 4,910,380

In addition to the Company's fixed maturity, short-term and equity investments, the Company invests in (i) hedge funds and private investment funds that generally invest in senior secured bank debt, high yield credit, distressed debt, distressed real estate, derivatives, equity long/short strategies, currencies and commodities ("alternative funds") and (ii) high yield loan and convertible debt funds ("specialty funds"). The Company's alternative funds and specialty funds are recorded on the Company's balance sheet as "other investments." At September 30, 2013 and December 31, 2012, the Company had invested, net of capital returned, a total of \$438.9 million and \$394.5 million, respectively, in other investments. At September 30, 2013 and December 31, 2012, the carrying value of other investments was \$594.2 million and \$517.5 million, respectively. The following table summarizes the composition and redemption restrictions of other investments as of September 30, 2013 and December 31, 2012:

September 30, 2013	Market Value	Unfunded Commitments	Ineligible for Redemption over next 12 months
Alternative funds			
Hedge funds	\$ 385,913	\$ —	\$ 44,791
Private investment funds	55,531	60,790	55,531
Total alternative funds	441,444	60,790	100,322
Specialty funds			
High yield loan funds	109,171	—	—
Convertible debt funds	43,541	—	—
Total specialty funds	152,712	—	—
Total other investments	\$ 594,156	\$ 60,790	\$ 100,322

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except for ratios, share and per share amounts)

3. Investments, cont'd.

December 31, 2012	Market Value	Unfunded Commitments	Ineligible for Redemption in 2013
<b>Alternative funds</b>			
Hedge funds	\$ 337,200	\$ —	\$ 61,161
Private investment funds	35,219	29,483	35,219
Total alternative funds	<u>372,419</u>	<u>29,483</u>	<u>96,380</u>
<b>Specialty funds</b>			
High yield loan funds	105,886	—	—
Convertible debt funds	39,241	—	—
Total specialty funds	<u>145,127</u>	<u>—</u>	<u>—</u>
Total other investments	<u>\$ 517,546</u>	<u>\$ 29,483</u>	<u>\$ 96,380</u>

Hedge funds – The redemption frequency of the hedge funds range from monthly to biennially with notice periods from 30 to 90 days. Over one year, it is estimated that the Company can liquidate approximately 88.2% of the hedge fund portfolio, with the remainder over the following two years.

Private investment funds – The Company generally has no right to redeem its interest in any private investment funds in advance of dissolution of the applicable partnership. Instead, the nature of these investments is that distributions are received by the Company in connection with the liquidation of the underlying assets of the applicable limited partnership. It is estimated that the majority of the underlying assets of the limited partnerships would liquidate over 5 to 10 years from inception of the limited partnership. A secondary market, with unpredictable liquidity, exists for limited partner interests in private equity funds.

High yield loan funds – There are generally no restrictions on the Company’s right to redeem its interest in high yield loan funds with the exception of certain redemption frequency and notice requirements. The redemption frequency of these funds ranges from monthly to quarterly with notice periods from 30 to 90 days.

Convertible debt funds – There are generally no restrictions on the Company’s right to redeem its interest in convertible debt funds with the exception of certain redemption frequency and notice requirements. The redemption frequency of these funds is monthly with a required notice period of 5 days.

*Net Realized and Unrealized Investment (Losses) Gains*

Realized and unrealized investment gains and losses are recognized in earnings using the first in, first out method. The analysis of net realized and unrealized investment (losses) gains for the three and nine months ended September 30, 2013 and 2012 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Gross realized gains on investment sales	\$ 6,180	\$ 11,976	\$ 30,191	\$ 34,837
Gross realized losses on investment sales	(13,178)	(2,222)	(19,924)	(5,391)
Change in fair value of derivative financial instruments <sup>(1)</sup>	358	343	(300)	812
Net realized and unrealized investment (losses) gains	<u>\$ (6,640)</u>	<u>\$ 10,097</u>	<u>\$ 9,967</u>	<u>\$ 30,258</u>

(1) For additional information on the Company’s derivative financial instruments, see Note 7.

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
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**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except for ratios, share and per share amounts)

3. Investments, cont'd.

*Unrealized Gains and Losses and Other-than-temporary Impairments*

The Company classifies its investments in fixed maturity investments, short-term investments and equities as available for sale. The amortized cost, fair value and related gross unrealized gains and losses and non-credit other-than-temporary impairment (“OTTI”) losses on the Company’s securities classified as available for sale at September 30, 2013 and December 31, 2012 are as follows:

September 30, 2013	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Non-Credit OTTI (2)
<b>Fixed maturity investments</b>					
U.S. government and agencies securities	\$ 819,585	\$ 9,332	\$ (5,156)	\$ 823,761	\$ —
U.S. state and municipal securities	27,731	129	(490)	27,370	—
Foreign government securities	175,280	1,725	(1,496)	175,509	—
Government guaranteed corporate securities	34,244	328	(52)	34,520	—
Corporate securities	1,127,809	18,130	(6,488)	1,139,451	—
Residential mortgage-backed securities	1,235,668	20,278	(15,724)	1,240,222	(4,785)
Commercial mortgage-backed securities (1)	872,259	26,341	(9,140)	889,460	(47)
Asset-backed securities	466,516	5,067	(1,038)	470,545	—
Total fixed maturity investments	<u>\$ 4,759,092</u>	<u>\$ 81,330</u>	<u>\$ (39,584)</u>	<u>\$ 4,800,838</u>	<u>\$ (4,832)</u>
Short-term investments	11,600	—	(1)	11,599	—
Total fixed income investments	<u>\$ 4,770,692</u>	<u>\$ 81,330</u>	<u>\$ (39,585)</u>	<u>\$ 4,812,437</u>	<u>\$ (4,832)</u>
<b>Equity securities</b>					
Equity investments	\$ 152,328	\$ 17,197	\$ (2,697)	\$ 166,828	\$ —
Emerging market debt funds	60,250	255	—	60,505	—
Preferred equity investments	10,184	1,883	(64)	12,003	—
Short-term fixed income fund	23,526	4	—	23,530	—
Total equity securities	<u>\$ 246,288</u>	<u>\$ 19,339</u>	<u>\$ (2,761)</u>	<u>\$ 262,866</u>	<u>\$ —</u>

(1) Balances include amounts related to collateralized debt obligations held with total fair values of \$14.1 million.

(2) Represents total OTTI recognized in accumulated other comprehensive income. It does not include the change in fair value subsequent to the impairment measurement date. At September 30, 2013, the gross unrealized loss related to fixed income investments for which a non-credit OTTI was recognized in accumulated other comprehensive income was \$0.1 million.

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(Amounts in tables expressed in thousands of United States dollars, except for ratios, share and per share amounts)

3. Investments, cont'd.

December 31, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Non-Credit OTTI (2)
<b>Fixed maturity investments</b>					
U.S. government and agencies securities	\$ 718,992	\$ 18,596	\$ (53)	\$ 737,535	\$ —
U.S. state and municipal securities	37,952	1,119	(177)	38,894	—
Foreign government securities	106,218	3,264	(145)	109,337	—
Government guaranteed corporate securities	62,782	1,682	—	64,464	—
Corporate securities	1,334,451	40,555	(1,335)	1,373,671	—
Residential mortgage-backed securities	1,252,468	30,426	(2,315)	1,280,579	(5,884)
Commercial mortgage-backed securities (1)	741,178	41,737	(1,536)	781,379	(53)
Asset-backed securities	474,555	8,435	(699)	482,291	—
Total fixed maturity investments	<u>\$4,728,596</u>	<u>\$145,814</u>	<u>\$ (6,260)</u>	<u>\$4,868,150</u>	<u>\$ (5,937)</u>
Short-term investments	42,224	6	—	42,230	—
Total fixed income investments	<u>\$ 4,770,820</u>	<u>\$145,820</u>	<u>\$ (6,260)</u>	<u>\$ 4,910,380</u>	<u>\$ (5,937)</u>
<b>Equity securities</b>					
Equity investments	\$ 59,736	\$ 7,194	\$ (620)	\$ 66,310	\$ —
Emerging market debt funds	10,000	576	—	10,576	—
Preferred equity investments	7,261	2,851	(1)	10,111	—
Total equity securities	<u>\$ 76,997</u>	<u>\$ 10,621</u>	<u>\$ (621)</u>	<u>\$ 86,997</u>	<u>\$ —</u>

(1) Balances include amounts related to collateralized debt obligations held with total fair values of \$8.5 million.

(2) Represents total OTTI recognized in accumulated other comprehensive income. It does not include the change in fair value subsequent to the impairment measurement date. At December 31, 2012, the gross unrealized loss related to fixed income investments for which a non-credit OTTI was recognized in accumulated other comprehensive income was \$0.4 million.

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(Amounts in tables expressed in thousands of United States dollars, except for ratios, share and per share amounts)

3. Investments, cont'd.

The following tables summarize, for all available for sale securities in an unrealized loss position at September 30, 2013 and December 31, 2012, the aggregate fair value and gross unrealized loss by length of time the security has continuously been in an unrealized loss position.

	Less than 12 months		12 months or greater		Total	
	Unrealized Losses(1)	Fair Value	Unrealized Losses(1)	Fair Value	Unrealized Losses(1)	Fair Value
<b>September 30, 2013</b>						
<b>Fixed maturity investments</b>						
U.S. government and agencies securities	\$ (5,156)	\$ 265,417	\$ —	\$ —	\$ (5,156)	\$ 265,417
U.S. state and municipal securities	(490)	19,711	—	—	(490)	19,711
Foreign government securities	(1,495)	109,722	(1)	4,858	(1,496)	114,580
Government guaranteed corporate securities	(52)	11,301	—	—	(52)	11,301
Corporate securities	(6,488)	422,818	—	—	(6,488)	422,818
Residential mortgage-backed securities	(15,641)	510,138	(83)	1,619	(15,724)	511,757
Commercial mortgage-backed securities	(8,822)	351,269	(318)	4,936	(9,140)	356,205
Asset-backed securities	(853)	184,964	(185)	4,193	(1,038)	189,157
Total fixed maturity investments	<u>\$ (38,997)</u>	<u>\$ 1,875,340</u>	<u>\$ (587)</u>	<u>\$ 15,606</u>	<u>\$ (39,584)</u>	<u>\$ 1,890,946</u>
Short-term investments	(1)	1,246	—	—	(1)	1,246
Total fixed income investments	<u>\$ (38,998)</u>	<u>\$ 1,876,586</u>	<u>\$ (587)</u>	<u>\$ 15,606</u>	<u>\$ (39,585)</u>	<u>\$ 1,892,192</u>
<b>Equity securities</b>						
Equity investments	\$ (2,697)	\$ 43,925	\$ —	\$ —	\$ (2,697)	\$ 43,925
Preferred equity investments	(64)	5,924	—	—	(64)	5,924
Total equity securities	<u>\$ (2,761)</u>	<u>\$ 49,849</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ (2,761)</u>	<u>\$ 49,849</u>

(1) Gross unrealized losses include unrealized losses on non-OTTI and non-credit OTTI securities recognized in accumulated other comprehensive income at September 30, 2013.

As of September 30, 2013, 743 available for sale securities were in an unrealized loss position aggregating \$42.3 million. Of those, 31 securities with aggregated unrealized losses of \$0.6 million at September 30, 2013 had been in a continuous unrealized loss position for twelve months or greater.

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3. Investments, cont'd.

	Less than 12 months		12 months or greater		Total	
	Unrealized Losses(1)	Fair Value	Unrealized Losses(1)	Fair Value	Unrealized Losses(1)	Fair Value
<b>December 31, 2012</b>						
<b>Fixed maturity investments</b>						
U.S. government and agencies securities	\$ (53)	\$ 48,570	\$ —	\$ —	\$ (53)	\$ 48,570
U.S. state and municipal securities	(177)	6,905	—	—	(177)	6,905
Foreign government securities	(139)	23,157	(6)	4,870	(145)	28,027
Corporate securities	(1,305)	245,232	(30)	1,849	(1,335)	247,081
Residential mortgage-backed securities	(1,920)	327,473	(395)	7,511	(2,315)	334,984
Commercial mortgage-backed securities	(474)	79,125	(1,062)	11,625	(1,536)	90,750
Asset-backed securities	(94)	53,471	(605)	8,123	(699)	61,594
<b>Total fixed maturity investments</b>	<b>\$ (4,162)</b>	<b>\$ 783,933</b>	<b>\$ (2,098)</b>	<b>\$ 33,978</b>	<b>\$ (6,260)</b>	<b>\$ 817,911</b>
<b>Equity securities</b>						
Equity investments	\$ (580)	\$ 9,183	\$ (40)	\$ 387	\$ (620)	\$ 9,570
Preferred equity investments	(1)	201	—	—	(1)	201
<b>Total equity securities</b>	<b>\$ (581)</b>	<b>\$ 9,384</b>	<b>\$ (40)</b>	<b>\$ 387</b>	<b>\$ (621)</b>	<b>\$ 9,771</b>

- (1) Gross unrealized losses include unrealized losses on non-OTTI and non-credit OTTI securities recognized in accumulated other comprehensive income at December 31, 2012.

As of December 31, 2012, 403 available for sale securities were in an unrealized loss position aggregating \$6.9 million. Of those, 55 securities with aggregated unrealized losses of \$2.1 million had been in a continuous unrealized loss position for twelve months or greater.

The analysis of OTTI for the three and nine months ended September 30, 2013 and 2012 is as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Total other-than-temporary impairment losses	\$ (190)	\$ (126)	\$ (1,575)	\$ (274)
Portion of loss recognized in other comprehensive income (loss)	—	(5)	—	(483)
<b>Net impairment losses recognized in earnings</b>	<b>\$ (190)</b>	<b>\$ (131)</b>	<b>\$ (1,575)</b>	<b>\$ (757)</b>

Of the \$0.2 million (2012: \$0.1 million) of OTTI losses recognized by the Company in the third quarter of 2013, the majority was related to expected losses following the Company's decision to sell a corporate security. At September 30, 2013, the Company did not have the intent to sell any of the remaining fixed maturity investments in an unrealized loss position and determined that it was unlikely that the Company would be required to sell securities in an unrealized loss position.



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3. Investments, cont'd.

The unrealized losses on the Company's available for sale securities at September 30, 2013 were primarily due to an increase in interest rates and widening of credit spreads, rather than any actual credit losses on these securities. Because the Company has the ability and intent to hold its equity securities until recovery, the Company currently believes it is probable that it will collect all amounts due according to their respective contractual terms. Therefore, the Company does not consider these securities to be other-than-temporarily impaired at September 30, 2013.

The following table provides a roll-forward of the amount related to credit losses for the Company's available for sale investments recognized in earnings for which a portion of an OTTI loss was recognized in accumulated other comprehensive income for the three and nine months ended September 30, 2013:

	<u>Three months ended</u>		<u>Nine months ended</u>	
	<u>September 30,</u>		<u>September 30,</u>	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
Beginning balance	\$(1,769)	\$(2,268)	\$ (2,000)	\$(2,225)
Addition for the amount related to the credit loss for which an other-than-temporary impairment was not previously recognized	—	—	—	(3)
Addition for the amount related to the credit loss for which an other-than-temporary impairment was previously recognized	—	(5)	—	(503)
Reductions for increases in cash flows expected to be collected that are recognized over the remaining life of the security	—	—	—	—
Reductions for securities sold during the period	<u>113</u>	<u>216</u>	<u>344</u>	<u>674</u>
Ending balance	<u>\$(1,656)</u>	<u>\$(2,057)</u>	<u>\$(1,656)</u>	<u>\$(2,057)</u>

*Variable Interest Entities*

Entities that do not have sufficient equity at risk to allow the entity to finance its activities without additional financial support or in which the equity investors, as a group, do not have the characteristics of a controlling financial interest are referred to as variable interest entities ("VIE"). A VIE is consolidated by the variable interest holder that is determined to have the controlling financial interest (primary beneficiary) as a result of having both the power to direct the activities of a VIE that most significantly impact the VIE's economic performance and the obligation to absorb losses or right to receive benefits from the VIE that could potentially be significant to the VIE. The Company determines whether it is the primary beneficiary of an entity subject to consolidation based on a qualitative assessment of the VIE's capital structure, contractual terms, nature of the VIE's operations and purpose and the Company's relative exposure to the related risks of the VIE on the date it becomes initially involved in the VIE. The Company reassesses its VIE determination with respect to an entity on an ongoing basis.

The Company is involved in the normal course of business with VIEs primarily as a passive investor in residential and commercial mortgage-backed securities and through its interests in other investments in alternative and specialty funds that are structured as limited partnerships considered to be third party VIEs. The Company determined that it was not the primary beneficiary for any of these investments as of September 30, 2013. The Company believes its exposure to loss with respect to these investments is generally limited to the investment carrying amounts reported in the Company's Condensed Consolidated Balance Sheets and any unfunded investment commitments.

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4. Fair value measurement

The Company determines the fair value of the fixed maturity investments, short-term investments, equity securities, other investments, debt, and other assets and liabilities in accordance with current accounting guidance, which defines fair value and establishes a fair value hierarchy based on inputs to the various valuation techniques used for each fair value measurement. The Company determines the estimated fair value of each individual security utilizing the highest level inputs available. Valuation inputs by security type may include the following:

- Government and agencies fixed maturity securities – These securities are generally priced by pricing services or index providers. The pricing services or index providers may use current market trades for securities with similar quality, maturity and coupon. If no such trades are available, the pricing service typically uses analytical models which may incorporate option adjusted spreads, daily interest rate data and market/sector news. The Company generally classifies the fair values of government and agencies securities in Level 2. Current issue U.S. government securities are generally valued based on Level 1 inputs, which use the market approach valuation technique.
- Government guaranteed corporate fixed maturity securities – These securities are generally priced by pricing services or index providers. The pricing service or index providers may use current market trades for securities with similar quality, maturity and coupon. If no such trades are available, the pricing service typically uses analytical spread models which may incorporate inputs from the U.S treasury curve or LIBOR. The Company generally classifies the fair values of its government guaranteed corporate securities in Level 2.
- Corporate fixed maturity securities – These securities are generally priced by pricing services or index providers. The pricing services or index providers typically use discounted cash flow models that incorporate benchmark curves for treasury, swap and high issuance credits. Credit spreads are developed from current market observations for like or similar securities. The Company generally classifies the fair values of its corporate securities in Level 2.
- Equity securities – These securities are generally priced by pricing services or index providers. Depending on the type of underlying equity security or equity fund, the securities are priced by pricing services or index providers based on quoted market prices in active markets or through a discounted cash flow model that incorporates benchmark curves for treasury, swap and credits for like or similar securities. The Company generally classifies the fair values of its equity securities in Level 1 or 2.

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4. Fair value measurement, cont'd.

- Other assets and liabilities – These balances include a variety of derivative instruments used to enhance the efficiency of the investment portfolio and economically hedge certain risks. These instruments are generally priced by pricing services, broker/dealers and/or recent trading activity. The market value approach valuation technique is used to estimate the fair value for these derivatives based on significant observable market inputs. Certain derivative instruments are priced by pricing services based on quoted market prices in active markets. These derivative instruments are generally classified in Level 1. Other derivative instruments are priced using industry valuation models and are considered Level 2, as the inputs to the valuation model are based on observable market inputs. Also included in this line item are proprietary, non-exchange traded derivative-based risk management products primarily used to address weather and energy risks. The trading market for these weather derivatives is generally linked to energy and agriculture commodities, weather and other natural phenomena. In instances where market prices are not available, the Company uses industry or internally developed valuation techniques such as spread option, Black Scholes, quanto and simulation modeling to determine fair value and classifies these in Level 3. These models may reference prices for similar instruments.
- Structured securities including agency and non-agency, residential and commercial, mortgage and asset-backed securities – These securities are generally priced by broker/dealers. Broker/dealers may use current market trades for securities with similar qualities. If no such trades are available, inputs such as bid and offer, prepayment speeds, the U.S. treasury curve, swap curve and cash settlement may be used in a discounted cash flow model to determine the fair value of a security. The Company generally classifies the fair values of its structured securities in Level 2.
- Other investments – Other investments, including alternative funds and specialty funds, are generally priced on net asset values (“NAV”) received from the fund managers or administrators. Due to the timing of the delivery of the final NAV by certain of the fund managers, valuations of certain alternative funds and specialty funds are estimated based on the most recently available information, including period end NAVs, period end estimates, or, in some cases, prior month or prior quarter NAVs. As this valuation technique incorporates both observable and significant unobservable inputs, the Company generally classifies the fair value of its other investments in Level 3.
- Debt – Outstanding debt consists of the Company’s 6.15% Senior Notes due October 15, 2015 and the 7.0% Senior Notes due July 15, 2034 (the “Senior Notes”). The fair values of these securities were obtained from a third party pricing service and pricing was based on the spread above the risk-free yield curve. These spreads are generally obtained from the new issue market, secondary trading and broker-dealer quotes. As these spreads and the yields for the risk-free yield curve are observable market inputs, the fair values of the Senior Notes are classified in Level 2.

The carrying values of cash and cash equivalents, accrued investment income, net receivable on sales of investments, net payable on purchases of investments and other financial instruments not described above approximated their fair values at September 30, 2013.

Transfers between levels are assumed to occur at the end of each period.

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4. Fair value measurement, cont'd.

The following table sets forth the Company's available for sale investments, other investments, other assets and liabilities and debt categorized by the level within the hierarchy in which the fair value measurements fall at September 30, 2013:

	<b>Fair Value Measurements at September 30, 2013</b>			
	Total at September 30, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets</b>				
<b>Fixed maturity investments</b>				
U.S. government and agencies securities	\$ 823,761	\$ 17,865	\$ 805,896	\$ —
U.S. state and municipal securities	27,370	—	27,370	—
Foreign government securities	175,509	—	175,509	—
Government guaranteed corporate securities	34,520	—	34,520	—
Corporate securities	1,139,451	—	1,138,692	759
Residential mortgage-backed securities	1,240,222	—	1,240,015	207
Commercial mortgage-backed securities	889,460	—	880,878	8,582
Asset-backed securities	470,545	—	467,635	2,910
<b>Total fixed maturity investments</b>	<b>\$ 4,800,838</b>	<b>\$ 17,865</b>	<b>\$ 4,770,515</b>	<b>\$ 12,458</b>
<b>Equity securities</b>				
Equity investments	166,828	80,596	86,232	—
Emerging market debt funds	60,505	—	60,505	—
Preferred equity investments	12,003	—	12,003	—
Short-term fixed income fund	23,530	23,530	—	—
<b>Total equity securities</b>	<b>\$ 262,866</b>	<b>\$ 104,126</b>	<b>\$ 158,740</b>	<b>\$ —</b>
Short-term investments	11,599	—	11,599	—
Other investments	594,156	—	—	594,156
Other assets (see Note 7)	122,853	—	120,526	2,327
<b>Total assets</b>	<b>\$ 5,792,312</b>	<b>\$ 121,991</b>	<b>\$ 5,061,380</b>	<b>\$ 608,941</b>
<b>Liabilities</b>				
Other liabilities (see Note 7)	\$ 74,237	\$ —	\$ 69,405	\$ 4,832
Debt	582,296	—	582,296	—
<b>Total liabilities</b>	<b>\$ 656,533</b>	<b>\$ —</b>	<b>\$ 651,701</b>	<b>\$ 4,832</b>

During the nine months ended September 30, 2013, there were net transfers into Level 3 from Level 2 of \$9.8 million, excluding other investments. Transfers into Level 3 consisted of corporate securities, mortgage-backed securities and asset-backed securities for which observable inputs were no longer available in the current period.

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4. Fair value measurement, cont'd.

The following table sets forth the Company's available for sale investments, other investments, other assets and liabilities and debt categorized by the level within the hierarchy in which the fair value measurements fall at December 31, 2012:

	<b>Fair Value Measurements at December 31, 2012</b>			
	Total at December 31, 2012	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets</b>				
<b>Fixed maturity investments</b>				
U.S. government and agencies securities	\$ 737,535	\$ 39,889	\$ 697,646	\$ —
U.S. state and municipal securities	38,894	—	38,894	—
Foreign government securities	109,337	—	109,337	—
Government guaranteed corporate securities	64,464	—	64,464	—
Corporate securities	1,373,671	—	1,373,671	—
Residential mortgage-backed securities	1,280,579	—	1,280,223	356
Commercial mortgage-backed securities	781,379	—	777,049	4,330
Asset-backed securities	482,291	—	478,480	3,811
<b>Total fixed maturity investments</b>	<b>\$ 4,868,150</b>	<b>\$ 39,889</b>	<b>\$4,819,764</b>	<b>\$ 8,497</b>
<b>Equity securities</b>				
Equity investments	66,310	66,310	—	—
Emerging market debt funds	10,576	—	10,576	—
Preferred equity investments	10,111	—	10,111	—
<b>Total equity securities</b>	<b>\$ 86,997</b>	<b>\$ 66,310</b>	<b>\$ 20,687</b>	<b>\$ —</b>
Short-term investments	42,230	—	42,230	—
Other investments	517,546	—	—	517,546
Other assets (see Note 7)	23,649	—	20,688	2,961
<b>Total assets</b>	<b>\$5,538,572</b>	<b>\$106,199</b>	<b>\$4,903,369</b>	<b>\$ 529,004</b>
<b>Liabilities</b>				
Other liabilities (see Note 7)	10,660	—	7,699	2,961
Debt	592,677	—	592,677	—
<b>Total liabilities</b>	<b>\$ 603,337</b>	<b>\$ —</b>	<b>\$ 600,376</b>	<b>\$ 2,961</b>

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4. Fair value measurement, cont'd.

Level 3 assets represented 10.5% and 9.6% of the Company's total available for sale investments, other investments and derivative instruments at September 30, 2013 and December 31, 2012, respectively. There were no material changes in the Company's valuation techniques for the nine months ended September 30, 2013. No impairment losses on Level 3 securities were recognized in earnings for the three and nine months ended September 30, 2013 or 2012.

The following tables present a reconciliation of the beginning and ending balances for all assets and liabilities measured at fair value on a recurring basis using Level 3 inputs during the three and nine months ended September 30, 2013 and 2012, respectively:

	<b>Three Months Ended September 30, 2013</b>				
	<u>Fixed maturity</u> <u>investments</u>	<u>Other</u> <u>investments</u>	<u>Other</u> <u>assets</u>	<u>Total assets</u>	<u>Other</u> <u>liabilities</u>
Level 3, beginning of period	\$ 7,546	\$ 569,393	\$ —	\$ 576,939	\$ —
Total net realized gains included in earnings	56	19,108	—	19,164	—
Total net realized and unrealized losses included in earnings	(15)	(5,864)	—	(5,879)	—
Change in unrealized gains included in other comprehensive income (loss)	111	—	—	111	—
Change in unrealized losses included in other comprehensive income (loss)	(62)	—	—	(62)	—
Purchases	—	16,597	—	16,597	—
Sales	(1,879)	(5,078)	—	(6,957)	—
Transfers in to Level 3	7,903	—	—	7,903	—
Transfers out of Level 3	(1,202)	—	—	(1,202)	—
Level 3, end of period	<u>\$ 12,458</u>	<u>\$ 594,156</u>	<u>\$ —</u>	<u>\$ 606,614</u>	<u>\$ —</u>

  

	<b>Nine Months Ended September 30, 2013</b>				
	<u>Fixed maturity</u> <u>investments</u>	<u>Other</u> <u>investments</u>	<u>Other</u> <u>assets</u>	<u>Total assets</u>	<u>Other</u> <u>liabilities</u>
Level 3, beginning of period	\$ 8,497	\$ 517,546	\$ 2,961	\$ 529,004	\$ 2,961
Total net realized gains included in earnings	104	61,010	—	61,114	—
Total net realized and unrealized losses included in earnings	(17)	(17,927)	—	(17,944)	—
Change in unrealized gains included in other comprehensive income (loss)	438	—	—	438	—
Change in unrealized losses included in other comprehensive income (loss)	(270)	—	—	(270)	—
Purchases	—	62,011	6	62,017	12
Sales	(6,081)	(28,484)	(2,967)	(37,532)	(2,973)
Transfers in to Level 3	11,550	—	—	11,550	—
Transfers out of Level 3	(1,763)	—	—	(1,763)	—
Level 3, end of period	<u>\$ 12,458</u>	<u>\$ 594,156</u>	<u>\$ —</u>	<u>\$ 606,614</u>	<u>\$ —</u>

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4. Fair value measurement, cont'd.

	<b>Three Months Ended September 30, 2012</b>				
	<b>Fixed maturity investments</b>	<b>Other investments</b>	<b>Other assets</b>	<b>Total assets</b>	<b>Other liabilities</b>
Level 3, beginning of period	\$ 9,819	\$478,860	\$—	\$488,679	\$ —
Total net realized gains included in earnings	44	18,461	—	18,505	—
Total net realized and unrealized losses included in earnings	—	(3,411)	—	(3,411)	—
Change in unrealized gains included in other comprehensive income (loss)	570	—	—	570	—
Change in unrealized losses included in other comprehensive income (loss)	(14)	—	—	(14)	—
Purchases	2	37,319	—	37,321	—
Sales	(1,536)	(52,319)	—	(53,855)	—
Transfers in to Level 3	5,695	—	—	5,695	—
Transfers out of Level 3	(762)	—	—	(762)	—
Level 3, end of period	<u>\$ 13,818</u>	<u>\$478,910</u>	<u>\$—</u>	<u>\$492,728</u>	<u>\$ —</u>

	<b>Nine Months Ended September 30, 2012</b>				
	<b>Fixed maturity investments</b>	<b>Other investments</b>	<b>Other assets</b>	<b>Total assets</b>	<b>Other liabilities</b>
Level 3, beginning of period	\$ 10,394	\$ —	\$—	\$ 10,394	\$ —
Total net realized gains included in earnings	54	29,286	—	29,340	—
Total net realized and unrealized losses included in earnings	(13)	(14,310)	—	(14,323)	—
Change in unrealized gains included in other comprehensive income (loss)	1,732	—	—	1,732	—
Change in unrealized losses included in other comprehensive income (loss)	(243)	—	—	(243)	—
Purchases	(38)	84,519	—	84,481	—
Sales	(2,568)	(53,013)	—	(55,581)	—
Transfers in to Level 3	7,771	432,428 <sup>(1)</sup>	—	440,199	—
Transfers out of Level 3	(3,271)	—	—	(3,271)	—
Level 3, end of period	<u>\$ 13,818</u>	<u>\$478,910</u>	<u>\$—</u>	<u>\$492,728</u>	<u>\$ —</u>

(1) As required by ASU 2011-04, the fair value of the Company's other investments was transferred into Level 3 at March 31, 2012.

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5. Earnings per share

The two-class method utilized by the Company is an earnings allocation formula that determines earnings per share for the holders of Endurance Holdings' ordinary shares (also referred to as "common shares") and participating common shares, which includes unvested restricted shares that receive cash dividends, according to dividends declared and participation rights in undistributed earnings. Net income available to common and participating common shareholders is reduced by the amount of dividends declared in the current period and by the contractual amount of dividends that must be paid for the current period related to the Company's common and participating common shares. Any remaining undistributed earnings are allocated to the common and participating common shareholders to the extent that each security may share in earnings as if all of the earnings for the period had been distributed. In periods of loss, no losses are allocated to participating common shareholders. Instead, all such losses are allocated solely to the common shareholders.

Basic earnings per common share are calculated by dividing net income available to common shareholders by the weighted average number of common shares outstanding. The weighted average number of common shares excludes any dilutive effect of outstanding options and convertible securities such as unvested restricted shares.

Diluted earnings per common share are based on the weighted average number of common shares and assumes the exercise of all dilutive stock options and the vesting or conversion of all convertible securities such as unvested restricted shares using the two-class method described above.

The following table sets forth the computation of basic and diluted earnings per share for the three and nine months ended September 30, 2013 and 2012:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
<b>Numerator:</b>				
Net income available to common and participating common shareholders	\$ 75,228	\$ 31,930	\$ 220,170	\$ 170,579
Less amount allocated to participating common shareholders <sup>(1)</sup>	(1,997)	(494)	(4,742)	(2,828)
Net income allocated to common shareholders	<u>\$ 73,231</u>	<u>\$ 31,436</u>	<u>\$ 215,428</u>	<u>\$ 167,751</u>
<b>Denominator:</b>				
Weighted average shares – basic	<u>43,099,841</u>	<u>42,628,248</u>	<u>42,719,837</u>	<u>42,555,617</u>
<b>Share equivalents:</b>				
Options	—	28,880	—	36,130
Restricted share units	298	778	594	2,546
Weighted average shares – diluted	<u>43,100,139</u>	<u>42,657,906</u>	<u>42,720,431</u>	<u>42,594,293</u>
Basic earnings per common share	<u>\$ 1.70</u>	<u>\$ 0.74</u>	<u>\$ 5.04</u>	<u>\$ 3.94</u>
Diluted earnings per common share	<u>\$ 1.70</u>	<u>\$ 0.74</u>	<u>\$ 5.04</u>	<u>\$ 3.94</u>

- (1) Represents earnings attributable to holders of unvested restricted shares issued by the Company. In periods of loss, no losses are allocated to participating common shareholders (unvested restricted shares).



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5. Earnings per share, cont'd.

Endurance Holdings declared a dividend of \$0.484375 per Series A preferred share and \$0.46875 per Series B preferred share on August 8, 2013 (2012 - Series A: \$0.484375, Series B: \$0.46875). The Series A and Series B preferred share dividends were paid on September 16, 2013 to shareholders of record on August 30, 2013. Endurance Holdings also declared a dividend of \$0.32 per common share on August 8, 2013 (2012 - \$0.31). The dividend was paid on September 30, 2013 to shareholders of record on September 16, 2013.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Dividends declared per Series A preferred share	\$ 0.484375	\$ 0.484375	\$ 1.453125	\$ 1.453125
Dividends declared per Series B preferred share	\$ 0.468750	\$ 0.468750	\$ 1.406250	\$ 1.406250
Dividends declared per common share	\$ 0.32	\$ 0.31	\$ 0.96	\$ 0.93

6. Accumulated other comprehensive income

The following table presents the changes in accumulated other comprehensive income balances by component for the three and nine months ended September 30, 2013:

	For the Three Months Ended September 30, 2013			
	Gains and losses on cash flow hedges	Unrealized gains and losses on available-for- sale securities	Foreign currency items	Total
Beginning balance	\$ (1,899)	\$ 30,636	\$ 2,701	\$ 31,438
Other comprehensive income before reclassifications	—	22,358	8,918	31,276
Amounts reclassified from accumulated other comprehensive income <sup>(1)</sup>	22	6,721	—	6,743
Net current period other comprehensive income	22	29,079	8,918	38,019
Ending balance	\$ (1,877)	\$ 59,715	\$ 11,619	\$ 69,457

(1) All amounts are net of tax.

	Nine Months Ended September 30, 2013			
	Gains and losses on cash flow hedges	Unrealized gains and losses on available-for- sale securities	Foreign currency items	Total
Beginning balance	\$ (1,944)	\$ 141,731	\$ 12,676	\$ 152,463
Other comprehensive loss before reclassifications	—	(74,001)	(1,057)	(75,058)
Amounts reclassified from accumulated other comprehensive income <sup>(1)</sup>	67	(8,015)	—	(7,948)
Net current period other comprehensive income (loss)	67	(82,016)	(1,057)	(83,006)
Ending balance	\$ (1,877)	\$ 59,715	\$ 11,619	\$ 69,457

(1) All amounts are net of tax.

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6. Accumulated other comprehensive income, cont'd.

The following table presents the significant items reclassified out of accumulated other comprehensive income during the three and nine months ended September 30, 2013:

<b>Three Months Ended September 30, 2013</b>		
Details about accumulated other comprehensive income components	Amount reclassified from accumulated other comprehensive income	Affected line item in the Unaudited Condensed Consolidated Statements of Income and Comprehensive Income
Gains and losses on cash flow hedges - Debt	\$ 22	Interest expense
	22	Total before income taxes
	—	Income tax expense
	<u>\$ 22</u>	Total net of income taxes
Unrealized losses (gains) on available-for-sale securities	\$ 6,999	Net realized and unrealized investment losses
	190	Net impairment losses recognized in earnings
	7,189	Total before income taxes
	(468)	Income tax benefit
	<u>\$ 6,721</u>	Total net of income taxes
<b>Nine Months Ended September 30, 2013</b>		
Details about accumulated other comprehensive income components	Amount reclassified from accumulated other comprehensive income	Affected line item in the Unaudited Condensed Consolidated Statements of Income and Comprehensive Income
Gains and losses on cash flow hedges - Debt	\$ 67	Interest expense
	67	Total before income taxes
	—	Income tax expense
	<u>\$ 67</u>	Total net of income taxes
Unrealized (gains) losses on available-for-sale securities	\$ (10,267)	Net realized and unrealized investment gains
	1,575	Net impairment losses recognized in earnings
	(8,692)	Total before income taxes
	677	Income tax expense
	<u>\$ (8,015)</u>	Total net of income taxes

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7. Derivatives

The Company's derivative instruments are recorded in the Condensed Consolidated Balance Sheets at fair value, with changes in fair value and gains and losses recognized in net realized and unrealized investment (losses) gains, net foreign exchange losses (gains) and other underwriting (loss) income in the Condensed Consolidated Statements of Income and Comprehensive Income.

During 2012, the Company entered into the weather risk management business through its newly formed unit, Endurance Global Weather. Endurance Global Weather regularly transacts in certain derivative-based risk management products primarily to address weather and energy risks. The trading markets for these derivatives are generally linked to energy and agriculture commodities, weather and other natural phenomena. Generally, the Company's current portfolio of such derivative contracts is of short duration and such contracts are predominantly seasonal in nature.

The Company's derivatives are not designated as hedges under current accounting guidance. The Company invests a portion of its fixed maturity assets with third party investment managers with investment guidelines that permit the use of derivative instruments. The Company may enter derivative transactions directly or as part of strategies employed by its external investment managers. The Company's objectives for holding these derivatives are as follows:

*Interest Rate Futures, Swaps, Swaptions and Options* - to manage exposure to interest rate risk, which can include increasing or decreasing its exposure to this risk through modification of the portfolio composition and duration.

*Foreign Exchange Forwards, Futures and Options* - as part of overall currency risk management and investment strategies.

*Credit Default Swaps* - to manage market exposures. The Company may assume or economically hedge credit risk through credit default swaps to replicate or hedge investment positions. The original term of these credit default swaps is generally five years or less.

*Commodity Futures and Options* - to economically hedge certain underwriting risks.

*To-Be-Announced Mortgage-backed Securities ("TBAs")* - to enhance investment performance and as part of overall investment strategy. TBAs represent commitments to purchase or sell a future issuance of agency mortgage-backed securities. For the period between purchase of a TBA and allocation of the underlying securities, the Company's position is accounted for as a derivative.

*Energy and Weather Contracts* - to address weather and energy risks. The Company may purchase or sell contracts with financial settlements based on the performance of an index linked to a quantifiable weather element, such as temperature, precipitation, snowfall or wind speed, and structures with multiple risk triggers indexed to a quantifiable weather element and a weather sensitive commodity price, such as temperature and electrical power or natural gas.

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7. Derivatives, cont'd.

The fair values and the related notional values of derivatives at September 30, 2013 and December 31, 2012 are noted below.

	September 30, 2013		December 31, 2012	
	Fair Value	Notional Principal Amount	Fair Value	Notional Principal Amount
<b>Derivatives recorded in other assets</b>				
Foreign exchange forward contracts	\$ 74	\$ 9,539	\$ 23	\$ 1,652
Credit default swaps	—	—	9	410
Interest rate swaps	1	5,600	76	5,000
Interest rate swaptions	37	23,900	57	2,200
Interest rate futures	—	64,217	—	—
TBAs	120,414	119,000	20,523	19,000
Energy and weather contracts	2,327	35,627	2,961	15,573
Total recorded in other assets	<u>\$122,853</u>		<u>\$ 23,649</u>	
<b>Derivatives recorded in other liabilities</b>				
Foreign exchange forward contracts	\$ 333	\$ 15,285	\$ 60	\$ 5,296
Interest rate swaps	764	23,214	—	—
Interest rate swaptions	134	74,200	133	14,500
TBAs	68,174	67,000	7,506	7,000
Energy and weather contracts	4,832	35,627	2,961	15,573
Total recorded in other liabilities	<u>\$ 74,237</u>		<u>\$ 10,660</u>	
Net derivative asset	<u>\$ 48,616</u>		<u>\$ 12,989</u>	

On January 1, 2013, the Company adopted new guidance that requires disclosure of financial instruments subject to a master netting agreement. At September 30, 2013, derivative assets of \$2.4 million and liabilities of \$6.1 million were traded under International Swaps and Derivatives Association Master Agreements (“ISDAs”) which provide for the ability to settle the derivative asset and liability with each counterparty on a net basis. TBAs and interest rate futures are not subject to ISDAs. At September 30, 2013 and December 31, 2012, none of the Company’s derivative instruments were netted. See Note 10 for information on collateral pledged.

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7. Derivatives, cont'd.

The gains and losses on the Condensed Consolidated Statements of Income and Comprehensive Income for derivatives for the three and nine months ended September 30, 2013 and 2012 were as follows:

	<u>Three Months Ended</u> <u>September 30,</u>		<u>Nine Months Ended</u> <u>September 30,</u>	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
Total (losses) gains included in net foreign exchange losses (gains) from foreign exchange forward contracts	\$ (123)	\$ (10)	\$ 207	\$ 141
Futures contracts	\$ 112	\$ —	\$ 64	\$ 87
Credit default swaps	(68)	3	49	46
Interest rate swaps	(67)	29	(228)	(14)
Interest rate swaptions	392	(16)	291	31
TBAs	(11)	327	(476)	662
Total gains (losses) included in net realized and unrealized investment (losses) gains	<u>\$ 358</u>	<u>\$ 343</u>	<u>\$ (300)</u>	<u>\$ 812</u>
Commodity put options	\$ —	\$ (1,384)	\$ —	\$(2,684)
Energy and weather contracts	—	—	1,172	—
Total (losses) gains included in other underwriting (loss) income	<u>\$ —</u>	<u>\$ (1,384)</u>	<u>\$ 1,172</u>	<u>\$(2,684)</u>
Total gains (losses) from derivatives	<u>\$ 235</u>	<u>\$ (1,051)</u>	<u>\$ 1,079</u>	<u>\$(1,731)</u>

8. Stock-based employee compensation and other stock plans

The Company has a stock-based employee compensation plan, that provides the Company with the ability to grant to employees and non-employee directors restricted shares, restricted share units, stock appreciation rights, share bonuses, options to purchase the Company's ordinary shares and other forms of equity incentive awards, as determined by the Compensation Committee of the Company's Board of Directors.

On May 28, 2013, the Board of Directors elected John R. Charman as the Company's Chairman and Chief Executive Officer. Mr. Charman received a stock option to purchase 800,000 ordinary shares at an exercise price of \$48.20 per share, and a grant of 708,890 restricted shares, as an employment inducement pursuant to Rule 303A.08 of the New York Stock Exchange Corporate Governance Standards.

***Stock Options***

The 800,000 options awarded to Mr. Charman will vest annually, in five equal tranches commencing on May 28, 2013, subject to Mr. Charman's continued employment, or in the event of certain terminations of employment and other events. Mr. Charman's option awards have a 10-year contractual life.

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8. Stock-based employee compensation and other stock plans, cont'd.

A summary of option activity, including options held by employees and non-employee directors, during the nine months ended September 30, 2013 is presented below:

Options Outstanding	Nine Months Ended September 30, 2013			
	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (years)	Aggregate Intrinsic Value
Beginning, December 31, 2012	39,501	\$ 27.78		
Granted	800,000	48.20		
Exercised	24,501	23.88		
Forfeited	—	—		
Outstanding, September 30, 2013	<u>815,000</u>	<u>\$ 47.94</u>	<u>9.50</u>	<u>\$ 4,711</u>
Exercisable and vested options, September 30, 2013	<u>175,000</u>	<u>\$ 46.98</u>	<u>8.89</u>	<u>\$ 1,180</u>

No options were granted during the three months ended September 30, 2013 (2012 - Nil). During the nine months ended September 30, 2013, 800,000 options were granted (2012 - Nil) with a weighted average grant date fair value of \$10.2 million (2012 - Nil). The Company uses the Black-Scholes-Merton formula to estimate the value of stock options granted. No options expired during the three and nine months ended September 30, 2013 and 2012. During the three and nine months ended September 30, 2013, Nil (2012 - 3,500) and 24,501 (2012 - 30,300) options were exercised, respectively. No options vested during the three months ended September 30, 2013 (2012 - Nil). During the nine months ended September 30, 2013, 160,000 options vested (2012 - Nil). The total intrinsic value of options exercised during the three and nine months ended September 30, 2013 was Nil (2012 - \$64,000) and \$0.5 million (2012 - \$0.7 million), respectively. The Company received proceeds of Nil (2012 - \$63,000) and \$0.6 million (2012 - \$0.5 million) from the exercise of options during the three and nine months ended September 30, 2013, respectively. The Company issued new ordinary shares in connection with the exercise of the above options.

For the three and nine months ended September 30, 2013, compensation costs recognized in earnings for all options totaled \$1.0 million (2012 - Nil) and \$3.5 million (2012 - Nil), respectively.

There was unrecognized stock-based compensation expenses of \$6.7 million related to unvested stock options at September 30, 2013. This expense is expected to be recognized between 2013 and 2017, with approximately 15.8% expected to be recognized during the remainder of 2013.

***Restricted Shares and Restricted Share Units***

The 708,890 restricted shares awarded to Mr. Charman, as discussed above, will vest annually, in five equal tranches commencing on May 28, 2013, subject to Mr. Charman's continued employment, or in the event of certain terminations of employment and other events.

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8. Stock-based employee compensation and other stock plans, cont'd.

A summary of the restricted share and restricted share unit activity during the nine months ended September 30, 2013 is presented below:

	<b>Nine Months Ended</b>	
	<b>September 30, 2013</b>	
	<b>Number of</b>	<b>Aggregate</b>
	<b>Shares/Units</b>	<b>Intrinsic Value</b>
Unvested, December 31, 2012	686,633	
Granted	1,079,108	
Settled	(406,495)	
Forfeited	(211,227)	
Unvested, September 30, 2013	<u>1,148,019</u>	
Outstanding, September 30, 2013	<u>1,148,019</u>	<u>\$ 61,672</u>

During the three and nine months ended September 30, 2013, the Company granted an aggregate of 8,453 (2012 - 6,790) and 1,079,108 (2012 - 407,358) restricted shares and restricted share units with weighted average grant date fair values of \$0.4 million (2012 - \$0.2 million) and \$50.7 million (2012 - \$15.6 million), respectively. During the three and nine months ended September 30, 2013, the aggregate fair value of restricted shares and restricted share units that vested was \$0.1 million (2012 - \$0.2 million) and \$17.0 million (2012 - \$11.7 million), respectively.

For the three and nine months ended September 30, 2013, compensation costs recognized in earnings for all restricted shares and restricted share units were \$2.6 million (2012 - \$1.9 million) and \$16.1 million (2012 - \$8.4 million), respectively. At September 30, 2013, compensation costs not yet recognized related to non-vested awards was \$31.6 million. This expense is expected to be recognized between 2013 and 2017, with approximately 18.2% expected to be recognized during the remainder of 2013.

***Employee Share Purchase Plan***

The Company also has an Employee Share Purchase Plan under which employees of Endurance Holdings and certain of its subsidiaries may purchase Endurance Holdings' ordinary shares. Total expenses related to this plan for the three and nine months ended September 30, 2013 were approximately \$42,000 (2012 - \$39,000) and \$124,000 (2012 - \$127,000), respectively.

9. Segment reporting

The determination of the Company's business segments is based on how the Company monitors the performance of its underwriting operations. The Company has two reportable business segments, Insurance and Reinsurance, which are comprised of the following lines of business:

Insurance segment lines of business

- Agriculture
- Casualty and other specialty
- Professional lines
- Property

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9. Segment reporting, cont'd.

Reinsurance segment lines of business

- Catastrophe
- Property
- Casualty
- Other specialty

Management measures segment results on the basis of the combined ratio, which is obtained by dividing the sum of the net losses and loss expenses, acquisition expenses and general and administrative expenses by net premiums earned. When purchased within a single line of business, ceded reinsurance and recoveries are accounted for within that line of business. When purchased across multiple lines of business, ceded reinsurance and recoveries are allocated to the lines of business in proportion to the related risks assumed. The Company does not manage its assets by segment; accordingly, investment income and total assets are not allocated to the individual business segments. General and administrative expenses incurred by the segments are allocated directly. Remaining general and administrative expenses not directly incurred by the segments are allocated primarily based on estimated consumption, headcount and other variables deemed relevant to the allocation of such expenses. Ceded reinsurance and recoveries are recorded within the business segment to which they apply.

The following table provides a summary of segment revenues, results and reserves for losses and loss expenses for the three months ended September 30, 2013:

	<b>Three Months Ended September 30, 2013</b>		
	<b>Insurance</b>	<b>Reinsurance</b>	<b>Total</b>
<b>Revenues</b>			
Gross premiums written	\$ 344,819	\$ 199,544	\$ 544,363
Ceded premiums written	(120,481)	(28,549)	(149,030)
Net premiums written	224,338	170,995	395,333
Net premiums earned	291,477	262,068	553,545
Other underwriting loss	—	(943)	(943)
	<u>291,477</u>	<u>261,125</u>	<u>552,602</u>
<b>Expenses</b>			
Net losses and loss expenses	228,409	110,627	339,036
Acquisition expenses	18,440	60,335	78,775
General and administrative expenses	35,641	31,829	67,470
	<u>282,490</u>	<u>202,791</u>	<u>485,281</u>
<b>Underwriting income</b>	<b>\$ 8,987</b>	<b>\$ 58,334</b>	<b>\$ 67,321</b>
Net loss ratio	78.4%	42.3%	61.3%
Acquisition expense ratio	6.3%	23.0%	14.2%
General and administrative expense ratio	12.2%	12.1%	12.2%
<b>Combined ratio</b>	<b>96.9%</b>	<b>77.4%</b>	<b>87.7%</b>
Reserve for losses and loss expenses	<u>\$2,146,136</u>	<u>\$1,905,966</u>	<u>\$4,052,102</u>



**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except for ratios, share and per share amounts)

9. Segment reporting, cont'd.

The following table provides a summary of segment revenues, results and reserves for losses and loss expenses for the three months ended September 30, 2012:

	Three Months Ended September 30, 2012		
	Insurance	Reinsurance	Total
<b>Revenues</b>			
Gross premiums written	\$ 324,808	\$ 296,447	\$ 621,255
Ceded premiums written	(103,543)	(3,632)	(107,175)
Net premiums written	221,265	292,815	514,080
Net premiums earned	283,273	268,599	551,872
Other underwriting (loss) income	(1,384)	37	(1,347)
	<u>281,889</u>	<u>268,636</u>	<u>550,525</u>
<b>Expenses</b>			
Net losses and loss expenses	288,750	118,773	407,523
Acquisition expenses	24,506	64,276	88,782
General and administrative expenses	29,409	23,306	52,715
	<u>342,665</u>	<u>206,355</u>	<u>549,020</u>
<b>Underwriting (loss) income</b>	<b>\$ (60,776)</b>	<b>\$ 62,281</b>	<b>\$ 1,505</b>
Net loss ratio	101.9%	44.2%	73.8%
Acquisition expense ratio	8.7%	23.9%	16.1%
General and administrative expense ratio	10.4%	8.7%	9.6%
Combined ratio	121.0%	76.8%	99.5%
Reserve for losses and loss expenses	<u>\$2,635,086</u>	<u>\$1,874,356</u>	<u>\$4,509,442</u>

The following table reconciles total segment results to income before income taxes for the three months ended September 30, 2013 and 2012:

	Three Months Ended September 30,	
	2013	2012
Total underwriting income	\$ 67,321	\$ 1,505
Net investment income	38,097	45,882
Net foreign exchange losses	(2,201)	(3,774)
Net realized and unrealized investment (losses) gains	(6,640)	10,097
Net impairment losses recognized in earnings	(190)	(131)
Amortization of intangibles	(1,652)	(2,434)
Interest expense	(9,048)	(9,041)
Income before income taxes	<u>\$85,687</u>	<u>\$ 42,104</u>

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except  
for ratios, share and per share amounts)

9. Segment reporting, cont'd.

The following table provides gross and net premiums written by line of business for the three months ended September 30, 2013 and 2012:

Business Segment	Gross premiums written	Net premiums written	Gross premiums written	Net premiums written
	2013	2013	2012	2012
<b>Insurance</b>				
Agriculture	\$ 200,062	\$ 120,617	\$ 171,826	\$ 106,180
Casualty and other specialty	95,862	72,431	90,873	66,686
Professional lines	34,221	20,972	43,209	34,804
Property	14,674	10,318	18,900	13,595
Total Insurance	<u>344,819</u>	<u>224,338</u>	<u>324,808</u>	<u>221,265</u>
<b>Reinsurance</b>				
Catastrophe	38,676	12,551	38,871	36,484
Casualty	53,691	53,690	77,781	77,781
Property	91,653	90,528	157,742	157,742
Other specialty	15,524	14,226	22,053	20,808
Total Reinsurance	<u>199,544</u>	<u>170,995</u>	<u>296,447</u>	<u>292,815</u>
Total	<u>\$ 544,363</u>	<u>\$ 395,333</u>	<u>\$ 621,255</u>	<u>\$ 514,080</u>

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except  
for ratios, share and per share amounts)

9. Segment reporting, cont'd.

The following table provides a summary of the segment revenues and results for the nine months ended September 30, 2013:

	<b>Nine Months Ended September 30, 2013</b>		
	<b>Insurance</b>	<b>Reinsurance</b>	<b>Total</b>
<b>Revenues</b>			
Gross premiums written	\$1,274,703	\$1,019,732	\$ 2,294,435
Ceded premiums written	(454,169)	(71,397)	(525,566)
Net premiums written	820,534	948,335	1,768,869
Net premiums earned	710,507	806,490	1,516,997
Other underwriting income	—	694	694
	<u>710,507</u>	<u>807,184</u>	<u>1,517,691</u>
<b>Expenses</b>			
Net losses and loss expenses	543,717	373,347	917,064
Acquisition expenses	48,024	174,255	222,279
General and administrative expenses	114,792	100,515	215,307
	<u>706,533</u>	<u>648,117</u>	<u>1,354,650</u>
<b>Underwriting income</b>	<b>\$ 3,974</b>	<b>\$ 159,067</b>	<b>\$ 163,041</b>
Net loss ratio	76.4%	46.3%	60.4%
Acquisition expense ratio	6.8%	21.6%	14.7%
General and administrative expense ratio	16.2%	12.5%	14.2%
Combined ratio	<u>99.4%</u>	<u>80.4%</u>	<u>89.3%</u>

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except for ratios, share and per share amounts)

9. Segment reporting, cont'd.

The following table provides a summary of the segment revenues and results for the nine months ended September 30, 2012:

	Nine Months Ended September 30, 2012		
	Insurance	Reinsurance	Total
<b>Revenues</b>			
Gross premiums written	\$1,252,814	\$1,034,166	\$2,286,980
Ceded premiums written	(417,109)	(28,322)	(445,431)
Net premiums written	835,705	1,005,844	1,841,549
Net premiums earned	710,988	771,859	1,482,847
Other underwriting (loss) income	(2,684)	1,021	(1,663)
	<u>708,304</u>	<u>772,880</u>	<u>1,481,184</u>
<b>Expenses</b>			
Net losses and loss expenses	610,956	405,231	1,016,187
Acquisition expenses	58,265	171,134	229,399
General and administrative expenses	96,663	84,702	181,365
	<u>765,884</u>	<u>661,067</u>	<u>1,426,951</u>
Underwriting (loss) income	<u>\$ (57,580)</u>	<u>\$ 111,813</u>	<u>\$ 54,233</u>
Net loss ratio	85.9%	52.4%	68.5%
Acquisition expense ratio	8.2%	22.2%	15.5%
General and administrative expense ratio	13.6%	11.0%	12.2%
Combined ratio	<u>107.7%</u>	<u>85.6%</u>	<u>96.2%</u>

The following table reconciles total segment results to income before income taxes for the nine months ended September 30, 2013 and 2012, respectively:

	Nine Months Ended	
	September 30,	
	2013	2012
Total underwriting income	\$ 163,041	\$ 54,233
Net investment income	119,870	134,723
Net foreign exchange (losses) gains	(8,496)	14,699
Net realized and unrealized investment gains	9,967	30,258
Net impairment losses recognized in earnings	(1,575)	(757)
Amortization of intangibles	(5,378)	(7,988)
Interest expense	(27,138)	(27,132)
Income before income taxes	<u>\$250,291</u>	<u>\$198,036</u>

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except for ratios, share and per share amounts)

9. Segment reporting, cont'd.

The following table provides gross and net premiums written by line of business for the nine months ended September 30, 2013 and 2012:

Business Segment	Gross premiums written	Net premiums written	Gross premiums written	Net premiums written
	2013	2013	2012	2012
<b>Insurance</b>				
Agriculture	\$ 896,169	\$ 546,284	\$ 838,932	\$ 528,349
Casualty and other specialty	239,943	179,065	236,383	173,097
Professional lines	93,481	62,963	130,573	107,841
Property	45,110	32,222	46,926	26,418
Total Insurance	<u>1,274,703</u>	<u>820,534</u>	<u>1,252,814</u>	<u>835,705</u>
<b>Reinsurance</b>				
Catastrophe	341,973	281,990	354,275	329,067
Casualty	272,602	271,174	258,352	257,113
Property	288,448	283,455	318,514	318,521
Other specialty	116,709	111,716	103,025	101,143
Total Reinsurance	<u>1,019,732</u>	<u>948,335</u>	<u>1,034,166</u>	<u>1,005,844</u>
Total	<u>\$2,294,435</u>	<u>\$1,768,869</u>	<u>\$2,286,980</u>	<u>\$1,841,549</u>

10. Commitments and contingencies

*Concentrations of credit risk.* The Company's reinsurance recoverables on paid and unpaid losses at September 30, 2013 and December 31, 2012 amounted to \$941.4 million and \$774.9 million, respectively. At September 30, 2013, substantially all reinsurance recoverables on paid and unpaid losses were due from the U.S. government or from reinsurers rated A- or better by A.M. Best Company Inc. or Standard & Poor's Corporation.

*Major production sources.* The following table shows the percentage of net premiums written generated through the Company's largest brokers for the nine months ended September 30, 2013 and 2012, respectively:

Broker	2013	2012
Aon Benfield	18.5%	17.3%
Marsh & McLennan Companies, Inc.	15.0%	16.6%
Willis Companies	12.4%	15.8%
Total of largest brokers	<u>45.9%</u>	<u>49.7%</u>

*Letters of credit.* As of September 30, 2013, the Company had issued letters of credit of \$259.5 million (December 31, 2012 – \$320.4 million) under its credit facility in favor of certain ceding companies to collateralize obligations.

**ENDURANCE SPECIALTY HOLDINGS LTD.**  
**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS – CONTINUED**

(Amounts in tables expressed in thousands of United States dollars, except  
for ratios, share and per share amounts)

10. Commitments and contingencies, cont'd.

*Investment commitments.* As of September 30, 2013 and December 31, 2012, the Company had pledged cash and cash equivalents and fixed maturity investments of \$215.8 million and \$224.4 million, respectively, in favor of certain ceding companies to collateralize obligations. As of September 30, 2013 and December 31, 2012, the Company had also pledged \$303.3 million and \$380.0 million of its cash and fixed maturity investments as required to meet collateral obligations for \$259.5 million and \$320.4 million in letters of credit outstanding under its credit facility, respectively. In addition, as of September 30, 2013 and December 31, 2012, cash and fixed maturity investments with fair values of \$274.6 million and \$280.0 million were on deposit with U.S. state regulators, respectively.

The Company is subject to certain commitments with respect to other investments at September 30, 2013 and December 31, 2012. See Note 3.

*Reinsurance commitments.* In the ordinary course of business, the Company periodically enters into reinsurance agreements that include terms which could require the Company to collateralize certain of its obligations.

*Employment agreements.* The Company has entered into employment agreements with certain officers that provide for equity incentive awards, executive benefits and severance payments under certain circumstances.

*Operating leases.* The Company leases office space and office equipment under operating leases. Future minimum lease commitments at September 30, 2013 are as follows:

<u>Twelve months ended September 30,</u>	<u>Amount</u>
2014	\$ 14,586
2015	13,822
2016	11,298
2017	9,791
2018	9,575
2019 and thereafter	41,135
	<u>\$100,207</u>

Total net lease expense under operating leases for the nine months ended September 30, 2013 was \$11.2 million (2012 – \$11.3 million).

*Legal proceedings.* The Company is party to various legal proceedings generally arising in the normal course of its business. While any proceeding contains an element of uncertainty, the Company does not believe that the eventual outcome of any litigation or arbitration proceeding to which it is presently a party could have a material adverse effect on its financial condition or business. Pursuant to the Company's insurance and reinsurance agreements, disputes are generally required to be settled by arbitration.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following is a discussion and analysis of the financial condition and results of operations for the three and nine months ended September 30, 2013 of Endurance Specialty Holdings Ltd. ("Endurance Holdings") and its wholly-owned subsidiaries (collectively, the "Company"). This discussion and analysis should be read in conjunction with the unaudited condensed consolidated financial statements and related notes contained in this Quarterly Report on Form 10-Q (this "Form 10-Q") as well as the audited consolidated financial statements and related notes for the fiscal year ended December 31, 2012, the discussions of critical accounting policies and the qualitative and quantitative disclosure about market risk contained in Endurance Holdings' Annual Report on Form 10-K for the fiscal year ended December 31, 2012 (the "2012 Form 10-K").

Some of the information contained in this discussion and analysis or set forth elsewhere in this Form 10-Q, including information with respect to the Company's plans and strategy for its business, includes forward-looking statements that involve risk and uncertainties. Please see the section "Cautionary Statement Regarding Forward-Looking Statements" below for more information on factors that could cause actual results to differ materially from the results described in or implied by any forward-looking statements contained in this discussion and analysis. You should review the "Risk Factors" set forth in the 2012 Form 10-K for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained herein.

### Overview

Endurance Holdings was organized as a Bermuda holding company on June 27, 2002 and has seven wholly-owned operating subsidiaries:

- Endurance Specialty Insurance Ltd. ("Endurance Bermuda"), domiciled in Bermuda with branch offices in Switzerland and Singapore;
- Endurance Reinsurance Corporation of America ("Endurance U.S. Reinsurance"), domiciled in Delaware;
- Endurance Worldwide Insurance Limited ("Endurance U.K."), domiciled in England;
- Endurance American Insurance Company ("Endurance American"), domiciled in Delaware;
- Endurance American Specialty Insurance Company ("Endurance American Specialty"), domiciled in Delaware;
- Endurance Risk Solutions Assurance Co. ("Endurance Risk Solutions"), domiciled in Delaware; and
- American Agri-Business Insurance Company ("American Agri-Business"), domiciled in Texas and managed by ARMtech Insurance Services, Inc. (together with American Agri-Business, "ARMtech").

The Company writes specialty lines of property and casualty insurance and reinsurance on a global basis and seeks to create a portfolio of specialty lines of business that are profitable and have limited correlation with one another. The Company's portfolio of specialty lines of business is organized into two business segments, Insurance and Reinsurance.

In the Insurance segment, the Company writes agriculture, casualty and other specialty, professional lines, and property insurance. In the Reinsurance segment, the Company writes catastrophe, property, casualty, and other specialty reinsurance.

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The Company's Insurance and Reinsurance segments both include property related coverages which provide insurance or reinsurance of an insurable interest in tangible property for property loss, damage or loss of use. In addition, the Company's Insurance and Reinsurance segments include various casualty insurance and reinsurance coverages which are primarily concerned with the losses caused by injuries to third parties, i.e., not the insured, or to property owned by third parties and the legal liability imposed on the insured resulting from such injuries.

**Application of Critical Accounting Estimates**

The Company's condensed consolidated financial statements are based on the selection of accounting policies and application of significant accounting estimates which require management to make significant estimates and assumptions. The Company believes that some of the more critical judgments in the areas of accounting estimates and assumptions that affect its financial condition and results of operations are related to the recognition of premiums written and ceded, reserves for losses and loss expenses, other-than-temporary impairments within the investment portfolio and fair value measurements of certain portions of the investment portfolio. For a detailed discussion of the Company's critical accounting estimates, please refer to the 2012 Form 10-K and the Notes to the Unaudited Condensed Consolidated Financial Statements in this Form 10-Q. There were no material changes in the application of the Company's critical accounting estimates subsequent to the 2012 Form 10-K. Management has discussed the application of these critical accounting estimates with the Company's Board of Directors and the Audit Committee of the Board of Directors.

**Consolidated Results of Operations – For the Three Months Ended September 30, 2013 and 2012**

Results of operations for the three months ended September 30, 2013 and 2012 were as follows:

	<b>Three Months Ended September 30,</b>		<b>Change<sup>(1)</sup></b>
	<b>2013</b>	<b>2012</b>	
	(U.S. dollars in thousands, except for ratios)		
<b>Revenues</b>			
Gross premiums written	\$ 544,363	\$ 621,255	(12.4)%
Ceded premiums written	(149,030)	(107,175)	39.1%
Net premiums written	395,333	514,080	(23.1)%
Net premiums earned	553,545	551,872	0.3%
Net investment income	38,097	45,882	(17.0)%
Net realized and unrealized investment (losses) gains	(6,640)	10,097	NM <sup>(2)</sup>
Net impairment losses recognized in earnings	(190)	(131)	45.0%
Other underwriting loss	(943)	(1,347)	(30.0)%
<b>Total revenues</b>	<b>583,869</b>	<b>606,373</b>	<b>(3.7)%</b>
<b>Expenses</b>			
Net losses and loss expenses	339,036	407,523	(16.8)%
Acquisition expenses	78,775	88,782	(11.3)%
General and administrative expenses	67,470	52,715	28.0%
Amortization of intangibles	1,652	2,434	(32.1)%
Net foreign exchange losses	2,201	3,774	(41.7)%
Interest expense	9,048	9,041	0.1%
Income tax expense	2,271	1,986	14.4%
<b>Net income</b>	<b>\$ 83,416</b>	<b>\$ 40,118</b>	<b>107.9%</b>
Net loss ratio	61.3%	73.8%	(12.5)
Acquisition expense ratio	14.2%	16.1%	(1.9)
General and administrative expense ratio	12.2%	9.6%	2.6
<b>Combined ratio</b>	<b>87.7%</b>	<b>99.5%</b>	<b>(11.8)</b>

(1) With respect to ratios, changes show increase or decrease in percentage points.

(2) Not meaningful.



### ***Premiums***

Gross premiums written in the three months ended September 30, 2013 were \$544.4 million, a decrease of \$76.9 million, or 12.4%, compared to the same period in 2012. Net premiums written in the three months ended September 30, 2013 were \$395.3 million, a decrease of \$118.7 million, or 23.1%. The change in net premiums written was driven by the following factors:

- A decline in net premiums in the catastrophe line of the Reinsurance segment, reflecting the purchase of retrocessional coverage on U.S. wind exposed risks;
- A decline in net premiums in the property line of the Reinsurance segment as the Company reduced participation on a few large contracts where pricing and terms were not adequate;
- A decline in net premiums in the casualty line of the Reinsurance segment as the Company chose not to renew business that no longer met profitability targets and recorded a number of negative premium adjustments;
- A decrease in professional lines net premiums in the Insurance segment, due primarily to the non-renewal of a large program relationship in late 2012; and
- An increase in net premiums in the agriculture line of the Insurance segment, due to growth in spring crop policy counts, partially offset by lower premiums from fall crops because of lower commodity prices.

The increase in ceded premiums written by the Company in the quarter ended September 30, 2013 as compared to the same period in 2012 was driven by both the agriculture line of business in the Insurance segment, as the Company ceded more premiums to the U.S. government, and the catastrophe line of the Reinsurance segment, as the Company chose to purchase additional retrocessional coverage.

Net premiums earned for the three months ended September 30, 2013 were \$553.5 million, an increase of \$1.7 million, or 0.3%, from the third quarter of 2012.

### ***Net Investment Income***

The Company's net investment income of \$38.1 million decreased by 17.0% or \$7.8 million for the quarter ended September 30, 2013 as compared to the same period in 2012. Investment income generated from the Company's available for sale investments, which consist of fixed maturity investments, short-term investments and equity securities, declined by \$6.1 million for the three months ended September 30, 2013 compared to the same period in 2012. This decline primarily resulted from lower reinvestment rates over the past 12 months. Net investment income during the third quarter of 2013 included net mark to market gains of \$13.2 million on other investments, comprised of alternative funds and specialty funds, as compared to mark to market gains of \$15.1 million in the third quarter of 2012. Investment expenses, including investment management fees, for the three months ended September 30, 2013 were \$3.8 million compared to \$3.4 million for the same period in 2012.

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The annualized net earned yield and total return of the investment portfolio for the three months ended September 30, 2013 and 2012 and the market yield and portfolio duration as of September 30, 2013 and 2012 were as follows:

	Three Months Ended September 30,	
	2013	2012
Annualized net earned yield <sup>(1)</sup>	2.43%	2.97%
Total return on investment portfolio <sup>(2)</sup>	1.32%	1.75%
Market yield <sup>(3)</sup>	1.85%	1.10%
Portfolio duration <sup>(4)</sup>	3.10 years	2.52 years

- (1) The actual net earned income from the investment portfolio after adjusting for expenses and accretion of discount and amortization of premium from the purchase price divided by the average book value of assets.
- (2) Net of investment manager fees; includes realized and unrealized gains and losses.
- (3) The internal rate of return of the investment portfolio based on the given market price or the single discount rate that equates a security price (inclusive of accrued interest) for the portfolio with its projected cash flows. Excludes other investments and operating cash.
- (4) Includes only cash and cash equivalents and fixed income investments managed by the Company's investment managers.

During the third quarter of 2013, the yield on the benchmark three year U.S. Treasury bond fluctuated within a 39 basis point range, with a high of 0.96% and a low of 0.57%. Trading activity in the Company's portfolio during the third quarter included reductions in corporate securities, asset-backed securities, and non-agency mortgage-backed securities, and increased allocations to U.S. government and government agencies securities, U.S. government agency mortgage-backed securities, foreign government bonds, equity securities and other investments. The duration of fixed income investments increased to 3.10 years at September 30, 2013 from 2.49 years at December 31, 2012, primarily due to the increase in interest rates, which reduced the estimated rate of prepayments underlying the Company's mortgage-backed securities portfolio, causing their average maturity to extend.

#### ***Net Realized and Unrealized Investment (Losses) Gains***

The Company's investment portfolio is actively managed on a fair value basis to generate attractive economic returns and income. Movements in financial markets and interest rates influence the timing and recognition of net realized investment gains and losses as the portfolio is adjusted and rebalanced. Proceeds from sales of investments classified as available for sale during the three months ended September 30, 2013 were \$986.6 million compared to \$908.0 million during the same period a year ago. Net realized investment (losses) gains decreased during the three months ended September 30, 2013 compared to the same period in 2012. Realized investment gains and losses and the change in the fair value of derivative financial instruments for the three months ended September 30, 2013 and 2012 were as follows:

	Three Months Ended September 30,	
	2013	2012
	(U.S. dollars in thousands)	
Gross realized gains on investment sales	\$ 6,180	\$ 11,976
Gross realized losses on investment sales	(13,178)	(2,222)
Change in fair value of derivative financial instruments	358	343
Net realized and unrealized investment (losses) gains	\$ (6,640)	\$ 10,097

Net impairment losses recognized in earnings for the three months ended September 30, 2013 and 2012 were \$0.2 million and \$0.1 million, respectively.

### *Net Foreign Exchange Gains and Losses*

For the three months ended September 30, 2013, the Company remeasured its monetary assets and liabilities denominated in foreign currencies, which resulted in a net foreign exchange loss of \$2.2 million compared to a net foreign exchange loss of \$3.8 million for the same period of 2012. The current period net foreign exchange loss resulted from offsetting exposures across the Company as the U.S. dollar weakened against British sterling, the Euro and New Zealand dollar. In the prior year, the net foreign exchange loss resulted from offsetting exposures across the Company as the U.S. dollar weakened against the major currencies during the period.

### *Net Losses and Loss Expenses*

The Company's net losses and loss expense ratio for the three months ended September 30, 2013 decreased compared to the same period in 2012, principally as a result of lower incurred losses in the agriculture line of business in the Insurance segment. In the Reinsurance segment, higher levels of favorable prior year loss reserve development were partially offset by increased levels of catastrophe losses.

Favorable prior year loss reserve development was \$48.1 million for the third quarter of 2013 compared to \$55.6 million during the same period in 2012. In the third quarter of 2013, prior year loss reserves emerged favorably across all lines business of the Insurance and Reinsurance segments. Favorable reserve development in the third quarter of 2013 was lower than the third quarter of 2012 principally in the Insurance segment across all business lines. Favorable reserve development in the Reinsurance segment was due to lower than expected reported losses in the property and catastrophe lines and from reductions in reserve estimates related to 2012 Superstorm Sandy losses (\$5.1 million).

The following table shows the net losses after adjustment for reinstatement premiums and other loss sensitive accruals recorded by the Company in connection with current calendar year catastrophes for the three months ended September 30, 2013 and 2012.

Three Months Ended September 30, 2013			Three Months Ended September 30, 2012		
Event Date	Event	Net Loss	Event Date	Event	Net Loss
		(U.S. dollars in millions)			
July 2013	Hailstorms in Germany	\$ 24.3	August 2012	Hurricane Isaac	\$ 6.0
	Other loss events in 2013	(6.2)	May 2012	Earthquake in Italy	4.8
				Other loss events in 2012	2.4
		<u>\$ 18.1</u>			<u>\$ 13.2</u>

For the three months ended September 30, 2013, natural catastrophe related losses added 3.7 percentage points to the Company's net loss ratio after adjustment for reinstatement premiums and other loss sensitive accruals compared to 2.5 percentage points in the same period in 2012. Offsetting the higher catastrophe losses incurred this quarter, the Company recorded a lower expected loss ratio in the third quarter of 2013 in the agriculture line of the Insurance segment as a result of improved growing conditions experienced in the U.S. compared to the prior year, which was adversely impacted by a severe drought.

The Company participates in lines of business where claims may not be reported for many years. Accordingly, management does not believe that reported claims are the only valid means for estimating ultimate obligations. Ultimate losses and loss expenses may differ materially from the amounts recorded in the Company's consolidated financial statements. These estimates are reviewed regularly and, as experience develops and new information becomes known, the reserves are adjusted as necessary. Reserve adjustments, if any, are recorded in earnings in the period in which they are determined. The overall loss reserves were established by the Company's actuaries and reflect management's best estimate of ultimate losses. See "Reserve for Losses and Loss Expenses" below for further discussion.

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***Acquisition Expenses***

The acquisition expense ratio for the three months ended September 30, 2013 was lower than the same period in 2012 due to a higher proportion of net earned premiums attributed to the agriculture line in the Insurance segment, which incurs a lower net acquisition expense rate.

***General and Administrative Expenses***

The Company's general and administrative expense ratio for the third quarter of 2013 increased by 2.6 percentage points compared to the same period in 2012 due to an increase in personnel costs related to the addition of new underwriting teams over the last twelve months, current period costs associated with the Company's senior leadership transition, and increased annual incentive costs associated with improved year to date corporate operating results. At September 30, 2013, the Company had a total of 913 employees compared to 849 employees at September 30, 2012.

***Income Tax Expense***

The Company recorded tax expense for the quarter ended September 30, 2013 of \$2.3 million compared to tax expense of \$2.0 million for the quarter ended September 30, 2012. The current period tax expense resulted from net taxable income recorded at the Company's United States taxable jurisdictions.

***Net Income***

The Company generated net income of \$83.4 million in the three months ended September 30, 2013 compared to net income of \$40.1 million in the same period of 2012 primarily as a result of a reduction in losses incurred in the agriculture line of the Insurance segment during the current period, partially offset by an increase in personnel costs and realized losses on investment sales.

**Consolidated Results of Operations – For the Nine Months Ended September 30, 2013 and 2012**

Results of operations for the nine months ended September 30, 2013 and 2012 were as follows:

	<b>Nine Months Ended September 30,</b>		<b>Change<sup>(1)</sup></b>
	<b>2013</b>	<b>2012</b>	
	(U.S. dollars in thousands, except for ratios)		
<b>Revenues</b>			
Gross premiums written	\$ 2,294,435	\$ 2,286,980	0.3%
Ceded premiums written	(525,566)	(445,431)	18.0%
Net premiums written	1,768,869	1,841,549	(3.9)%
Net premiums earned	1,516,997	1,482,847	2.3%
Net investment income	119,870	134,723	(11.0)%
Net realized and unrealized investment gains	9,967	30,258	(67.1)%
Net impairment losses recognized in earnings	(1,575)	(757)	108.1%
Other underwriting income (loss)	694	(1,663)	NM <sup>(2)</sup>
Total revenues	<u>1,645,953</u>	<u>1,645,408</u>	— %
<b>Expenses</b>			
Losses and loss expenses	917,064	1,016,187	(9.8)%
Acquisition expenses	222,279	229,399	(3.1)%
General and administrative expenses	215,307	181,365	18.7%
Amortization of intangibles	5,378	7,988	(32.7)%
Net foreign exchange losses (gains)	8,496	(14,699)	NM <sup>(2)</sup>
Interest expense	27,138	27,132	— %
Income tax expense	5,557	2,893	92.1%
Net income	<u>\$ 244,734</u>	<u>\$ 195,143</u>	<u>25.4%</u>
Net loss ratio	60.4%	68.5%	(8.1)
Acquisition expense ratio	14.7%	15.5%	(0.8)
General and administrative expense ratio	14.2%	12.2%	2.0
Combined ratio	<u>89.3%</u>	<u>96.2%</u>	<u>(6.9)</u>

(1) With respect to ratios, changes show increase or decrease in percentage points.

(2) Not meaningful.

**Premiums**

Gross premiums written in the nine months ended September 30, 2013 were \$2,294.4 million, an increase of \$7.5 million, or 0.3%, compared to the same period in 2012. Net premiums written in the nine months ended September 30, 2013 were \$1,768.9 million, a decrease of \$72.7 million, or 3.9%, compared to the same period in 2012. The change in net premiums written was driven by the following factors:

- A decline in net premiums in the property line of the Reinsurance segment as the Company reduced participation on a few large contracts where pricing was not adequate;
- A decline in net premiums in the catastrophe line of the Reinsurance segment reflecting the impact of a more competitive market where pricing declined and the selective reduction by the Company of its limits on some U.S. business, particularly in Florida, as well as the purchase by the Company of increased retrocessional coverage on business in the current year;
- A decrease in net premiums in the Insurance segment, primarily in professional lines driven by the non-renewal of a large program relationship in late 2012;

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- An expansion of net premiums in the other specialty line of the Reinsurance segment, primarily due to new business generated by the trade credit and surety team that joined the Company in late 2012, partially offset by an absence of positive premium adjustments compared to 2012 and clients increasing their retentions upon renewal of certain treaties;
- An increase of net premiums in the casualty line of the Reinsurance segment as a result of new business written on international motor and U.S. casualty treaties partially offset by the non-renewal of business that no longer met profitability targets and a number of negative premium adjustments; and
- An increase in net premiums in the agriculture line of the Insurance segment due to growth in spring crop policy counts, partially offset by lower premiums from fall crops because of lower commodity prices.

Net premiums earned for the nine months ended September 30, 2013 were \$1,517.0 million, an increase of \$34.2 million, or 2.3%, from the nine months ended September 30, 2012 principally due to growth in net premiums written in the current quarter in the agriculture line of business in the Insurance segment, partially offset by a decline in Insurance segment professional lines net premiums written and declines in net premiums written in the catastrophe and property lines of the Reinsurance segment.

### *Net Investment Income*

The Company's net investment income of \$119.9 million decreased by 11.0% or \$14.9 million for the nine months ended September 30, 2013 as compared to the same period in 2012. Net investment income during the first nine months of 2013 included net mark to market gains of \$43.1 million on other investments, comprised of alternative funds and specialty funds, as compared to mark to market gains of \$38.1 million in the first nine months of 2012. Investment income generated from the Company's available for sale investments, which consist of fixed maturity investments, short-term investments and equity securities, declined by \$19.6 million for the nine months ended September 30, 2013 compared to the same period in 2012. This decline resulted primarily from lower reinvestment rates over the past 12 months, partly offset by a higher average investment portfolio balance. Investment expenses, including investment management fees, for the nine months ended September 30, 2013 were \$11.3 million compared to \$10.0 million for the same period in 2012.

The annualized net earned yield and total return on the investment portfolio for the nine months ended September 30, 2013 and 2012 and the market yield and portfolio duration as of September 30, 2013 and 2012 were as follows:

	Nine Months Ended September 30,	
	2013	2012
Annualized net earned yield <sup>(1)</sup>	2.52%	2.87%
Total return on investment portfolio <sup>(2)</sup>	0.68%	4.08%
Market yield <sup>(3)</sup>	1.85%	1.10%
Portfolio duration <sup>(4)</sup>	3.10 years	2.52 years

(1) The actual net earned income from the investment portfolio after adjusting for expenses and accretion of discount and amortization of premium from the purchase price divided by the average book value of assets.

(2) Net of investment manager fees; includes realized and unrealized gains and losses.

(3) The internal rate of return of the investment portfolio based on the given market price or the single discount rate that equates to a security price (inclusive of accrued interest) for the portfolio with its projected cash flows. Excludes other investments and operating cash.

(4) Includes only cash and cash equivalents and fixed income investments held by the Company's investment managers.

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During the nine months ended September 30, 2013, the yield on the benchmark three year U.S. Treasury bond fluctuated within a 67 basis point range, with a high of 0.96% and a low of 0.29%. Trading activity in the Company's portfolio for the nine months ended September 30, 2013 included reductions in corporate securities, short-term investments, government and agency guaranteed corporate securities, residential mortgage-backed securities, municipal securities, and asset-backed securities, and increased allocations to equity securities, U.S. government and government agencies securities, foreign government bonds, commercial mortgage-backed securities, and other investments. The duration of the fixed income investments increased to 3.10 years at September 30, 2013 from 2.49 years at December 31, 2012, primarily due to the increase in interest rates which reduced the estimated rate of prepayments underlying the Company's mortgage-backed securities portfolio causing their average maturity to extend.

#### ***Net Realized and Unrealized Investment Gains***

The Company's investment portfolio is actively managed on a fair value basis to generate attractive economic returns and income. Movements in financial markets and interest rates influence the timing and recognition of net realized investment gains and losses as the portfolio is adjusted and rebalanced. Proceeds from sales of investments classified as available for sale during the nine months ended September 30, 2013 were \$2,382.1 million compared to \$2,460.9 million during the same period a year ago. Net realized investment gains decreased during the nine months ended September 30, 2013 compared to the same period in 2012.

Realized investment gains and losses and the change in the fair value of derivative financial instruments for the nine months ended September 30, 2013 and 2012 were as follows:

	<b>Nine Months Ended September 30,</b>	
	<b>2013</b>	<b>2012</b>
	(U.S. dollars in thousands)	
Gross realized gains on investment sales	\$ 30,191	\$ 34,837
Gross realized losses on investment sales	(19,924)	(5,391)
Change in fair value of derivative financial instruments	(300)	812
Net realized and unrealized investment gains	<u>\$ 9,967</u>	<u>\$ 30,258</u>

Net impairment losses recognized in earnings for the nine months ended September 30, 2013 and 2012 were \$1.6 million and \$0.8 million, respectively.

#### ***Net Foreign Exchange Gains***

For the nine months ended September 30, 2013, the Company remeasured its monetary assets and liabilities denominated in foreign currencies, which resulted in a net foreign exchange loss of \$8.5 million compared to a gain of \$14.7 million for the same period in 2012. The current period net foreign exchange loss resulted from offsetting exposures across the Company as the U.S. dollar strengthened against the Japanese Yen and Australian dollar in the period. In the prior year, the gain resulted from a decrease in the value of Japanese Yen net liabilities as the U.S. dollar strengthened against the Yen.

#### ***Net Losses and Loss Expenses***

The Company's net losses and loss expense ratio for the nine months ended September 30, 2013 decreased compared to the same period in 2012 due to increased levels of favorable prior year loss reserve development and lower incurred losses in the agriculture line of business in the Insurance segment, partially offset by increased levels of catastrophe losses.

Favorable prior year loss reserve development was \$161.5 million for the nine months ended September 30, 2013 as compared to \$92.1 million for the same period in 2012. In the nine months ended September 30, 2013, prior year loss reserves emerged favorably across all lines of the Insurance segment and Reinsurance segment. In the nine months ended September 30, 2012, prior year loss reserves emerged favorably across all lines of the Insurance segment and across the catastrophe, casualty and other specialty lines of the Reinsurance segment. Favorable reserve development in the nine months ended September 30, 2013 was significantly higher than the nine months ended September 30, 2012

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principally in the Reinsurance segment due to much lower than expected reported (\$17.1 million) losses in the property and catastrophe lines and from reductions in reserve estimates related to the Thailand flood losses of 2011 and Superstorm Sandy losses in 2012 (\$25.2 million). Comparatively, the nine months ended September 30, 2012 included adverse development on some of the major 2011 loss events impacting the property line of business.

The following table shows the net losses after adjustment for reinstatement premiums and other loss sensitive accruals recorded by the Company in connection with current calendar year catastrophes for the nine months ended September 30, 2013 and 2012.

Nine Months Ended September 30, 2013			Nine Months Ended September 30, 2012		
Event Date	Event	Net Loss	Event Date	Event	Net Loss
		(U.S. dollars in millions)			
June 2013	Floods in Canada	10.8	August 2012	Hurricane Isaac	6.0
June 2013	Floods in Europe	19.7	February 2012	Windstorms in Kentucky	23.1
May 2013	Windstorms in the United States	10.7	May 2012	Earthquake in Italy	10.6
July 2013	Hailstorms in Germany	24.3	March/April 2012	Windstorms in the United States	9.9
		<u>\$ 65.5</u>			<u>\$ 49.6</u>

For the nine months ended September 30, 2013, catastrophe related losses added 4.6 percentage points to the Company's net loss ratio after adjustment for reinstatement premiums and other loss sensitive accruals compared to 3.5 percentage points in the same period in 2012. The higher catastrophe losses was partially offset by lower levels of attritional losses in the Insurance segment's property and casualty and other lines in the nine months ended September 30, 2013 compared to the same period in 2012. In addition, the Company recorded a lower expected loss ratio in the agriculture line of business in the Insurance segment as a result of improved growing conditions experienced in the U.S. compared to the prior year, which was adversely impacted by a severe drought.

The Company participates in lines of business in which claims may not be reported for many years. Accordingly, management does not believe that reported claims are the only valid means for estimating ultimate obligations. Ultimate losses and loss expenses may differ materially from the amounts recorded in the Company's consolidated financial statements. These estimates are reviewed regularly and, as experience develops and new information becomes known, the reserves are adjusted as necessary. Reserve adjustments, if any, are recorded in earnings in the period in which they are determined. The overall loss reserves were established by the Company's actuaries and reflect management's best estimate of ultimate losses. See "Reserve for Losses and Loss Expenses" below for further discussion.

#### ***Acquisition Expenses***

The acquisition expense ratio for the nine months ended September 30, 2013 was modestly lower compared with the same period in 2012, primarily due to a higher proportion of net earned premiums attributed to the agriculture line of business in the Insurance segment, which incurs a lower net acquisition expense rate.

#### ***General and Administrative Expenses***

The Company's general and administrative expense ratio for the nine months ended September 30, 2013 was higher than the same period in 2012 due to an increase in personnel costs related to the addition of new underwriting teams over the last twelve months, current period costs associated with the Company's CEO transition, and increased annual incentive costs associated with improved year to date corporate operating results in 2013. The comparable period in 2012 also benefited from a lower 2012 payout of the Company's 2011 annual incentive compensation than was previously accrued.

#### ***Income Tax Expense***

The Company recorded a tax expense for the nine months ended September 30, 2013 of \$5.6 million compared to a tax expense of \$2.9 million for the same period in 2012 due to adjustments to deferred tax valuation allowances at the Company's U.S. taxable jurisdictions in 2013.



### ***Net Income***

The Company generated net income of \$244.7 million for the nine months ended September 30, 2013 compared to a net income of \$195.1 million in the same period of 2012 primarily due to increased net premiums earned, a reduction in losses incurred in the agriculture line of business in the Insurance segment during the current period, and favorable prior year loss development, partially offset by an increase in personnel costs, foreign exchange losses and realized losses on investment sales.

### **Reserve for Losses and Loss Expenses**

As of September 30, 2013, the Company had accrued losses and loss expense reserves of \$4.1 billion (December 31, 2012 - \$4.2 billion). This amount represents management's best estimate of the ultimate liability for payment of losses and loss expenses related to loss events. During the nine months ended September 30, 2013 and 2012, the Company's net paid losses and loss expenses were \$925.9 million and \$745.7 million, respectively.

As more fully described under "Reserving Process" in the Company's Management's Discussion and Analysis of Financial Condition and Results of Operations in the 2012 Form 10-K, the Company incorporates a variety of actuarial methods and judgments in its reserving process. Two key inputs in the various actuarial methods employed by the Company are initial expected loss ratios and expected loss reporting patterns. These key inputs impact the potential variability in the estimate of the reserve for losses and loss expenses and are applicable to each of the Company's business segments. The Company's loss and loss expense reserves consider and reflect, in part, deviations resulting from differences between expected loss and actual loss reporting as well as judgments relating to the weights applied to the reserve levels indicated by the actuarial methods. Expected loss reporting patterns are based upon internal and external historical data and assumptions regarding claims reporting trends over a period of time that extends beyond the Company's own operating history.

Differences between actual reported losses and expected losses are anticipated to occur in any individual period and such deviations may influence future initial expected loss ratios and/or expected loss reporting patterns as the recent actual experience becomes part of the historical data utilized as part of the ongoing reserve estimation process. The Company has demonstrated the impact of changes in the speed of the loss reporting patterns, as well as changes in the expected loss ratios, within the table under the heading "Potential Variability in Reserves for Losses and Loss Expenses" in the Company's Management's Discussion and Analysis of Financial Condition and Results of Operations in the 2012 Form 10-K.

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Losses and loss expenses for the three and nine months ended September 30, 2013 are summarized as follows:

Three Months Ended September 30, 2013	Incurred related to:		Total incurred losses
	Current year	Prior years	
	(U.S. dollars in thousands)		
<b>Insurance:</b>			
Agriculture	\$ 177,920	\$ (616)	\$ 177,304
Casualty and other specialty	36,794	(2,388)	34,406
Professional lines	17,517	(2,302)	15,215
Property	2,388	(904)	1,484
Total Insurance	<u>234,619</u>	<u>(6,210)</u>	<u>228,409</u>
<b>Reinsurance:</b>			
Catastrophe	26,120	(9,234)	16,886
Property	49,036	(21,157)	27,879
Casualty	56,983	(6,268)	50,715
Other specialty	20,338	(5,191)	15,147
Total Reinsurance	<u>152,477</u>	<u>(41,850)</u>	<u>110,627</u>
Totals	<u>\$ 387,096</u>	<u>\$ (48,060)</u>	<u>\$ 339,036</u>

  

Nine Months Ended September 30, 2013	Incurred related to:		Total incurred losses
	Current year	Prior years	
	(U.S. dollars in thousands)		
<b>Insurance:</b>			
Agriculture	\$ 386,953	\$ (5,582)	\$ 381,371
Casualty and other specialty	114,856	(9,666)	105,190
Professional lines	61,589	(2,603)	58,986
Property	9,449	(11,279)	(1,830)
Total Insurance	<u>572,847</u>	<u>(29,130)</u>	<u>543,717</u>
<b>Reinsurance:</b>			
Catastrophe	122,343	(47,584)	74,759
Property	162,605	(47,145)	115,460
Casualty	161,673	(21,229)	140,444
Other specialty	59,129	(16,445)	42,684
Total Reinsurance	<u>505,750</u>	<u>(132,403)</u>	<u>373,347</u>
Totals	<u>\$1,078,597</u>	<u>\$ (161,533)</u>	<u>\$ 917,064</u>

Losses and loss expenses for the three and nine months ended September 30, 2013 included \$48.1 million and \$161.5 million in favorable development of reserves relating to prior accident years, respectively. The favorable loss reserve development experienced during the three and nine months ended September 30, 2013 benefited the Company's reported loss ratio by approximately 8.7 and 10.6 percentage points, respectively. This net reduction in estimated losses for prior accident years reflects lower than expected claims emergence for the nine months ended September 30, 2013 in all lines of business within the Insurance and Reinsurance segments.

For the three and nine months ended September 30, 2013, the Company did not materially alter any key inputs utilized to establish reserve for losses and loss expenses (initial expected loss ratios and loss reporting patterns) related to prior years for the insurance and reinsurance segments as the variances in reported losses for those segments were within the range of possible results anticipated by the Company.

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Losses and loss expenses for the three and nine months ended September 30, 2012 are summarized as follows:

Three Months Ended September 30, 2012	Incurred related to:		Total incurred losses
	Current year	Prior years	
	(U.S. dollars in thousands)		
<b>Insurance:</b>			
Agriculture	\$ 237,023	\$ (2,701)	\$ 234,322
Casualty and other specialty	39,942	(4,146)	35,796
Professional lines	25,608	(5,937)	19,671
Property	3,616	(4,655)	(1,039)
Total Insurance	<u>306,189</u>	<u>(17,439)</u>	<u>288,750</u>
<b>Reinsurance:</b>			
Catastrophe	20,823	(5,745)	15,078
Property	49,638	(10,527)	39,111
Casualty	53,757	(9,350)	44,407
Other specialty	32,758	(12,581)	20,177
Total Reinsurance	<u>156,976</u>	<u>(38,203)</u>	<u>118,773</u>
Totals	<u>\$ 463,165</u>	<u>\$ (55,642)</u>	<u>\$ 407,523</u>

  

Nine Months Ended September 30, 2012	Incurred related to:		Total incurred losses
	Current year	Prior years	
	(U.S. dollars in thousands)		
<b>Insurance:</b>			
Agriculture	\$ 431,139	\$ (8,536)	\$ 422,603
Casualty and other specialty	120,408	(11,196)	109,212
Professional lines	77,916	(7,467)	70,449
Property	20,412	(11,720)	8,692
Total Insurance	<u>649,875</u>	<u>(38,919)</u>	<u>610,956</u>
<b>Reinsurance:</b>			
Catastrophe	90,760	(23,280)	67,480
Property	130,775	6,977	137,752
Casualty	164,953	(15,663)	149,290
Other specialty	71,919	(21,210)	50,709
Total Reinsurance	<u>458,407</u>	<u>(53,176)</u>	<u>405,231</u>
Totals	<u>\$ 1,108,282</u>	<u>\$ (92,095)</u>	<u>\$ 1,016,187</u>

Losses and loss expenses for the three and nine months ended September 30, 2012 included \$55.6 million and \$92.1 million in favorable development of reserves relating to prior accident years, respectively. The favorable loss reserve development experienced during the three and nine months ended September 30, 2012 benefited the Company's reported loss ratio by approximately 10.1 and 6.2 percentage points, respectively. This net reduction in estimated losses for prior accident years resulted primarily from lower than expected claims emergence within all lines of business for the Insurance segment and the catastrophe, casualty and other specialty lines of business in the Reinsurance segment for the three months ended September 30, 2012, and across all lines of business included within the Insurance and Reinsurance segments for the nine months ended September 30, 2012.

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For the three and nine months ended September 30, 2012, the Company did not materially alter the two key inputs utilized to establish its reserve for losses and loss expenses (initial expected loss ratios and loss reporting patterns) for business related to prior years for the insurance and reinsurance segments as the variances in reported losses for those segments were within the range of possible results anticipated by the Company.

**Insurance**

*Agriculture.* For the three and nine months ended September 30, 2013 and 2012, the Company recorded favorable loss emergence due to lower than anticipated agriculture claims settlements for the 2012 and 2011 crop years.

*Casualty and other specialty.* For the three and nine months ended September 30, 2013, the Company recorded favorable loss emergence within this line of business primarily due to lower than expected claims activity within the healthcare liability and the Bermuda based excess casualty businesses. This favorable loss emergence was partially offset by adverse development within the U.S. based casualty business. For the three and nine months ended September 30, 2012, the Company recorded favorable loss emergence within this line of business primarily due to favorable loss development within the healthcare liability business, partially offset by adverse development within the workers' compensation business. The Company exited the workers' compensation insurance line of business in 2009.

*Professional lines.* For the three and nine months ended September 30, 2013, the Company recorded favorable loss emergence within this line of business, primarily due to lower than expected reported claims activity in the Bermuda based professional liability and U.S. based director and officers' liability businesses. For the three and nine months ended September 30, 2012, the Company recorded favorable loss emergence in professional lines due to lower than expected claims activity.

*Property.* For the three and nine months ended September 30, 2013 and 2012, the favorable loss emergence within the property line of business was primarily due to lower than expected reported and favorable case reserve development.

**Reinsurance**

*Catastrophe.* For the nine months ended September 30, 2013 and 2012, the Company recorded significant favorable loss emergence within this line of business primarily due to lower than expected claims activity and favorable case reserve development, primarily related to the Thailand floods of 2011 and Superstorm Sandy in 2012.

*Property.* For the three and nine months ended September 30, 2013, the Company recorded favorable loss emergence in the property line of business due to lower than expected claims activity and favorable case reserve development, primarily related to the Thailand floods of 2011 and Superstorm Sandy in 2012. For the three and nine months ended September 30, 2012, the Company recorded unfavorable loss emergence in the property line of business due to higher than expected claims activity related to 2011 catastrophes.

*Casualty.* For the three and nine months ended September 30, 2013 and 2012, the Company recorded favorable loss emergence within this line of business primarily due to lower than expected claims reported.

*Other specialty.* For the three and nine months ended September 30, 2013 and 2012, the Company recorded favorable loss emergence within this line of business primarily due to lower than expected claims reported.

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2013: The total reserves for losses and loss expenses recorded on the Company's balance sheet were comprised of the following at September 30,

	<u>Case Reserves</u>	<u>IBNR Reserves</u>	<u>Reserve for losses and loss expenses</u>
	(U.S. dollars in thousands)		
<b>Insurance:</b>			
Agriculture	\$ 279,916	\$ 30,176	\$ 310,092
Casualty and other specialty	309,162	962,741	1,271,903
Professional lines	131,741	393,343	525,084
Property	24,337	14,720	39,057
Total Insurance	<u>745,156</u>	<u>1,400,980</u>	<u>2,146,136</u>
<b>Reinsurance:</b>			
Catastrophe	164,615	125,742	290,357
Property	201,127	153,977	355,104
Casualty	305,906	697,972	1,003,878
Other specialty	100,272	156,355	256,627
Total Reinsurance	<u>771,920</u>	<u>1,134,046</u>	<u>1,905,966</u>
Totals	<u>\$1,517,076</u>	<u>\$ 2,535,026</u>	<u>\$ 4,052,102</u>

2012: The total reserves for losses and loss expenses recorded on the Company's balance sheet were comprised of the following at December 31,

	<u>Case Reserves</u>	<u>IBNR Reserves</u>	<u>Reserve for losses and loss expenses</u>
	(U.S. dollars in thousands)		
<b>Insurance:</b>			
Agriculture	\$ 392,457	\$ 71,586	\$ 464,043
Casualty and other specialty	308,611	944,289	1,252,900
Professional lines	110,441	386,819	497,260
Property	54,196	18,653	72,849
Total Insurance	<u>865,705</u>	<u>1,421,347</u>	<u>2,287,052</u>
<b>Reinsurance:</b>			
Catastrophe	201,105	97,223	298,328
Property	281,681	133,779	415,460
Casualty	296,494	679,982	976,476
Other specialty	119,261	144,299	263,560
Total Reinsurance	<u>898,541</u>	<u>1,055,283</u>	<u>1,953,824</u>
Totals	<u>\$1,764,246</u>	<u>\$ 2,476,630</u>	<u>\$ 4,240,876</u>

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**Underwriting Results by Business Segments**

The determination of the Company's business segments is based on the manner in which management monitors the performance of the Company's underwriting operations. As a result, we report two business segments – Insurance and Reinsurance.

Management measures the Company's results on the basis of the combined ratio, which is obtained by dividing the sum of the losses and loss expenses, acquisition expenses and general and administrative expenses by net premiums earned. The Company's historic combined ratios may not be indicative of future underwriting performance. When purchased within a single line of business, ceded reinsurance and recoveries are accounted for within that line of business. When purchased across multiple lines of business, ceded reinsurance and recoveries are allocated to the lines of business in proportion to the related risks assumed. The Company does not manage its assets by business segment; accordingly, investment income and total assets are not allocated to the individual business segments. General and administrative expenses incurred by the business segments are allocated directly. Remaining general and administrative expenses not directly incurred by the business segments are allocated primarily based on estimated consumption, headcount and other variables deemed relevant to the allocation of such expenses. Ceded reinsurance and recoveries are recorded within the business segment to which they apply.

**Insurance**

The following table summarizes the underwriting results and associated ratios for the Company's Insurance segment for the three and nine months ended September 30, 2013 and 2012.

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
	(U.S. dollars in thousands, except for ratios)			
<b>Revenues</b>				
Gross premiums written	\$ 344,819	\$ 324,808	\$ 1,274,703	\$ 1,252,814
Ceded premiums written	(120,481)	(103,543)	(454,169)	(417,109)
Net premiums written	224,338	221,265	820,534	835,705
Net premiums earned	291,477	283,273	710,507	710,988
Other underwriting loss	—	(1,384)	—	(2,684)
	<u>291,477</u>	<u>281,889</u>	<u>710,507</u>	<u>708,304</u>
<b>Expenses</b>				
Losses and loss expenses	228,409	288,750	543,717	610,956
Acquisition expenses	18,440	24,506	48,024	58,265
General and administrative expenses	35,641	29,409	114,792	96,663
	<u>282,490</u>	<u>342,665</u>	<u>706,533</u>	<u>765,884</u>
<b>Underwriting income (loss)</b>	<b><u>\$ 8,987</u></b>	<b><u>\$ (60,776)</u></b>	<b><u>\$ 3,974</u></b>	<b><u>\$ (57,580)</u></b>
Net loss ratio	78.4%	101.9%	76.4%	85.9%
Acquisition expense ratio	6.3%	8.7%	6.8%	8.2%
General and administrative expense ratio	12.2%	10.4%	16.2%	13.6%
<b>Combined ratio</b>	<b><u>96.9%</u></b>	<b><u>121.0%</u></b>	<b><u>99.4%</u></b>	<b><u>107.7%</u></b>

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**Premiums.** Gross premiums written for the three months ended September 30, 2013 in the Insurance segment increased by 6.2% over the same period in 2012. Gross premiums written for the nine months ended September 30, 2013 in the Insurance segment increased by 1.7% over the same period in 2012. Gross and net premiums written for each line of business in the Insurance segment were as follows:

	<b>Three Months Ended September 30,</b>			
	<b>2013</b>		<b>2012</b>	
	<b>Gross Premiums Written</b>	<b>Net Premiums Written</b>	<b>Gross Premiums Written</b>	<b>Net Premiums Written</b>
	(U.S. dollars in thousands)			
Agriculture	\$ 200,062	\$ 120,617	\$ 171,826	\$ 106,180
Casualty and other specialty	95,862	72,431	90,873	66,686
Professional lines	34,221	20,972	43,209	34,804
Property	14,674	10,318	18,900	13,595
<b>Total</b>	<b>\$ 344,819</b>	<b>\$ 224,338</b>	<b>\$ 324,808</b>	<b>\$ 221,265</b>

	<b>Nine Months Ended September 30,</b>			
	<b>2013</b>		<b>2012</b>	
	<b>Gross Premiums Written</b>	<b>Net Premiums Written</b>	<b>Gross Premiums Written</b>	<b>Net Premiums Written</b>
	(U.S. dollars in thousands)			
Agriculture	\$ 896,169	\$ 546,284	\$ 838,932	\$ 528,349
Casualty and other specialty	239,943	179,065	236,383	173,097
Professional lines	93,481	62,963	130,573	107,841
Property	45,110	32,222	46,926	26,418
<b>Total</b>	<b>\$ 1,274,703</b>	<b>\$ 820,534</b>	<b>\$ 1,252,814</b>	<b>\$ 835,705</b>

The increase in the Insurance segment net premiums written for the three months ended September 30, 2013 and the decrease for the nine months ended September 30, 2013 compared to the same periods in 2012 were driven by the following factors:

- An increase in net premiums within the agriculture line of business due to growth in crop policy counts, partially offset by lower premiums from fall crops because of lower commodity prices, and higher cessions to the U.S. government and third parties;
- A decrease in net premiums in professional lines driven by the non-renewal of a large program relationship in late 2012;
- An increase in property net premiums written in the nine months ended September 30, 2013 as a result of a shift in underlying risks resulted in the Company retaining a higher proportion of gross premiums; and
- An increase in net premiums in the casualty and other specialty line driven primarily by the addition of new underwriting teams.

Net premiums earned by the Company in the Insurance segment increased in the three months ended September 30, 2013 compared to the same period in 2012 primarily due to the increase in net premiums written in the agriculture line of business. Net premiums earned by the Company in the Insurance segment in the nine months ended September 30, 2013 were comparable to the same period in 2012.

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**Losses and Loss Expenses.** The net loss ratio in the Company's Insurance segment decreased by 23.5 percentage points for the three month period ended September 30, 2013 compared to the same period in 2012 and decreased by 9.5 percentage points for the nine months ended September 30, 2013 and 2012. The current accident quarter loss ratio decreased by 27.6 and 10.9 percentage points for the three and nine months ended September 30, 2013, respectively, compared to the same periods in 2012 due primarily to the agriculture line of business that incurred lower levels of losses as a result of improved growing conditions experienced in the U.S. compared to the prior year, which was adversely impacted by a severe drought. In addition, lower levels of attritional losses were experienced in the property and casualty and other lines of business in 2013 compared to the prior year.

During the three and nine months ended September 30, 2013, the Company's previously estimated loss and loss expense reserve for the Insurance segment for prior accident years was reduced by \$6.2 million and \$29.1 million, respectively, which decreased the net loss ratio by 2.1 and 4.1 percentage points, respectively, as compared to reductions of \$17.4 million and \$38.9 million, which decreased the net loss ratio by 6.2 and 5.5 percentage points for the three and nine months ended September 30, 2012, respectively. The lower level of favorable loss development in the third quarter of 2013 compared to 2012 was experienced across all lines of business following lower than expected claims activity in 2012.

**Acquisition Expenses.** The Company's acquisition expense ratios in the Insurance segment in the third quarter and nine months ended September 30, 2013 decreased compared to the same periods in 2012. The change in the acquisition expense ratio over both periods was driven by a higher proportion of net earned premiums attributed to the agriculture line, which incurs a lower net acquisition expense rate, and the decline in professional lines premiums over both the three and nine months ended September 30, 2013, which conversely incurs higher commissions.

**General and Administrative Expenses.** The increase in general and administrative expenses and expense ratios in the Insurance segment in the third quarter and nine months ended September 30, 2013 compared to the same periods in 2012 was a result of an increase in personnel costs related to the addition of new underwriting teams over the last twelve months, higher annual incentive costs, and increased levels of allocated expenses primarily from increased personnel expenses associated with the Company's senior leadership transition.



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The following table summarizes the underwriting results and associated ratios for the Company's Reinsurance business segment for the three and nine months ended September 30, 2013 and 2012.

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2013</u>	<u>2012</u>	<u>2013</u>	<u>2012</u>
	(U.S. dollars in thousands, except for ratios)			
<b>Revenues</b>				
Gross premiums written	\$ 199,544	\$ 296,447	\$ 1,019,732	\$ 1,034,166
Ceded premiums written	(28,549)	(3,632)	(71,397)	(28,322)
Net premiums written	170,995	292,815	948,335	1,005,844
Net premiums earned	262,068	268,599	806,490	771,859
Other underwriting (loss) income	(943)	37	694	1,021
	<u>261,125</u>	<u>268,636</u>	<u>807,184</u>	<u>772,880</u>
<b>Expenses</b>				
Losses and loss expenses	110,627	118,773	373,347	405,231
Acquisition expenses	60,335	64,276	174,255	171,134
General and administrative expenses	31,829	23,306	100,515	84,702
	<u>202,791</u>	<u>206,355</u>	<u>648,117</u>	<u>661,067</u>
<b>Underwriting income</b>	<u>\$ 58,334</u>	<u>\$ 62,281</u>	<u>\$ 159,067</u>	<u>\$ 111,813</u>
Net loss ratio	42.3%	44.2%	46.3%	52.4%
Acquisition expense ratio	23.0%	23.9%	21.6%	22.2%
General and administrative expense ratio	12.1%	8.7%	12.5%	11.0%
Combined ratio	<u>77.4%</u>	<u>76.8%</u>	<u>80.4%</u>	<u>85.6%</u>

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**Premiums.** In the third quarter of 2013, net premiums written in the Reinsurance segment decreased by 41.6% over the same period of 2012. In the nine months ended September 30, 2013, net premiums written in the Reinsurance segment decreased by 5.7% over the same period in 2012. Gross and net premiums written for each line of business in the Reinsurance segment for the three and nine months ended September 30, 2013 and 2012 were as follows:

	Three Months Ended September 30,			
	2013		2012	
	Gross Premiums Written	Net Premiums Written	Gross Premiums Written	Net Premiums Written
	(U.S. dollars in thousands)			
Catastrophe	\$ 38,676	\$ 12,551	\$ 38,871	\$ 36,484
Casualty	53,691	53,690	77,781	77,781
Property	91,653	90,528	157,742	157,742
Other specialty	15,524	14,226	22,053	20,808
<b>Total</b>	<b>\$ 199,544</b>	<b>\$ 170,995</b>	<b>\$ 296,447</b>	<b>\$ 292,815</b>

	Nine Months Ended September 30,			
	2013		2012	
	Gross Premiums Written	Net Premiums Written	Gross Premiums Written	Net Premiums Written
	(U.S. dollars in thousands)			
Catastrophe	\$ 341,973	\$ 281,990	\$ 354,275	\$ 329,067
Casualty	272,602	271,174	258,352	257,113
Property	288,448	283,455	318,514	318,521
Other specialty	116,709	111,716	103,025	101,143
<b>Total</b>	<b>\$ 1,019,732</b>	<b>\$ 948,335</b>	<b>\$ 1,034,166</b>	<b>\$ 1,005,844</b>

The movements in net premiums written in the Reinsurance segment for the third quarter and nine months ended September 30, 2013 compared to the same periods in 2012 were primarily due to the following factors:

- A decline in net premiums written in the property line as the Company reduced participation on a few large contracts where pricing was not adequate;
- An expansion of net written premiums in the other specialty line for the nine months ended September 30 2013, primarily due to new business generated by the trade credit and surety team that joined the Company in late 2012, partially offset by an absence of positive premium adjustments compared to 2012 and clients increasing their retentions upon renewal of certain treaties;
- Higher net premiums in the casualty line in the nine month period ended September 30, 2013 as a result of new business written on international motor and U.S. casualty treaties partially offset by the non-renewal of business that no longer met profitability targets and a number of negative premium adjustments; and
- A decrease in net premiums in the catastrophe line reflecting the impact of a more competitive market where pricing declined and the selective reduction by the Company of its limits on certain U.S. business, particularly in Florida, as well as the purchase by the Company of increased retrocessional coverage on U.S. wind exposed risks.

Ceded premiums written by the Company increased in the three and nine months ended September 30, 2013 as compared to the same period in 2012 as the Company has chosen to purchase increased levels of protection in the catastrophe and property lines of business.

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Net premiums earned by the Company in the Reinsurance segment for the nine months ended September 30, 2013 increased compared to the same period in 2012 due to the growth in gross premiums written in more recent periods. Net premiums earned in the Reinsurance segment for the three months ended September 30, 2013 decreased modestly compared to the same period in 2012 due to the overall decrease in net premiums written during 2013.

**Losses and Loss Expenses.** The net loss ratio in the Company's Reinsurance segment for the three and nine months ended September 30, 2013 decreased compared to the same periods in 2012 as a result of higher levels of prior year reserve development in 2013 compared to 2012. The Company recorded \$41.9 million and \$132.4 million of favorable prior year loss reserve development in the three and nine months ended September 30, 2013 compared to \$38.2 million and \$53.2 million in the three and nine months ended September 30, 2012. During the three and nine months ended September 30, 2013, the majority of the favorable loss reserve development emanated from the property and catastrophe lines, driven by reductions in the Thailand flood losses of 2011 and Superstorm Sandy losses in 2012, and from lower than expected attritional losses. The same periods in 2012 experienced adverse development on some of the major 2011 loss events.

Partially offsetting the increased levels of favorable prior year loss reserve development in the current periods, the Company recorded catastrophe losses, net of reinstatement premiums and other loss sensitive accruals, of \$18.1 million and \$65.5 million in the quarter and nine months ended September 30, 2013. The net losses from catastrophes added 8.0 and 9.0 percentage points to the Reinsurance segment's net loss ratio for the third quarter and nine months ended September 30, 2013, respectively. During the third quarter and nine months ended September 30, 2012, the Company incurred catastrophe losses of \$13.2 million and \$49.6 million. The net losses from catastrophes added 5.6 and 6.9 percentage points to the Reinsurance segment's net loss ratio for the third quarter and nine months ended September 30, 2012, respectively.

**Acquisition Expenses.** The Company's acquisition expense ratios in the Reinsurance segment for the three and nine months ended September 30, 2013 were modestly lower than in the same periods in 2012 as a result of the growth in certain property reinsurance business lines, the addition of a new trade credit and surety team of underwriters, and reduced participation on other property reinsurance treaties that each have different earned premium and commission structures, as well as increased purchases of retrocessional coverage.

**General and Administrative Expenses.** The general and administrative expense ratios in the Reinsurance segment for the three and nine months ended September 30, 2013 increased compared to those in the same periods in 2012 due to an increase in allocated current period costs associated with higher annual incentive costs and the Company's senior leadership transition, partially offset by the impact of higher earned premiums.

## Liquidity and Capital Resources

Endurance Holdings is a holding company that does not have any significant operations or assets other than its ownership of the shares of its direct and indirect subsidiaries. Endurance Holdings relies primarily on dividends and other permitted distributions from its subsidiaries to pay its operating expenses, interest on debt and dividends, if any, on its ordinary shares, its 7.75% Non-Cumulative Preferred Shares, Series A ("Series A Preferred Shares") and its 7.5% Non-Cumulative Preferred Shares, Series B ("Series B Preferred Shares"). There are restrictions on the payment of dividends by the Company's operating subsidiaries to Endurance Holdings, which are described in more detail below.

**Ability of Subsidiaries to Pay Dividends.** The ability of Endurance Bermuda to pay dividends is dependent on its ability to meet the requirements of applicable Bermuda law and regulations. Under Bermuda law, Endurance Bermuda may not declare or pay a dividend if there are reasonable grounds for believing that Endurance Bermuda is, or would after the payment be, unable to pay its liabilities as they become due, or the realizable value of Endurance Bermuda's assets would thereby be less than the aggregate of its liabilities and its issued share capital and share premium accounts. Further, Endurance Bermuda, as a regulated insurance company in Bermuda, is subject to additional regulatory restrictions on the payment of dividends or distributions. As of September 30, 2013, Endurance Bermuda could pay a dividend or return additional paid-in capital totaling approximately \$538.8 million (December 31, 2012 – \$623.1 million) without prior regulatory approval based upon the Bermuda insurance and corporate regulations. In 2011, Endurance Holdings loaned Endurance Bermuda \$200.0 million, which remains outstanding and is callable on demand.

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Endurance U.S. Reinsurance, Endurance American, Endurance American Specialty and Endurance Risk Solutions are subject to regulation by the State of Delaware Department of Insurance and American Agri-Business is subject to regulation by the Texas Department of Insurance. Dividends for each U.S. operating subsidiary are limited to the greater of 10% of policyholders' surplus or statutory net income, excluding realized capital gains. In addition, dividends may only be declared or distributed out of earned surplus. At December 31, 2012, Endurance U.S. Reinsurance, Endurance American, Endurance Risk Solutions and Endurance American Specialty did not have earned surplus; therefore, these companies are precluded from declaring or distributing dividends at September 30, 2013 without the prior approval of the applicable insurance regulator. At September 30, 2013, American Agri-Business (with notice to the Texas Department of Insurance) could pay dividends of \$4.3 million without prior regulatory approval from the applicable regulators. In addition, any dividends paid by Endurance American, Endurance American Specialty and Endurance Risk Solutions would be subject to the dividend limitation of their respective parent insurance companies.

Under the jurisdiction of the United Kingdom's Prudential Regulation Authority ("PRA"), Endurance U.K. must maintain a margin of solvency at all times, which is determined based on the type and amount of insurance business written. The PRA regulatory requirements impose no explicit restrictions on Endurance U.K.'s ability to pay a dividend, but Endurance U.K. would have to notify the PRA 28 days prior to any proposed dividend payment. Dividends may only be distributed from profits available for distributions. At September 30, 2013, Endurance U.K. did not have profits available for distributions.

*Cash and Invested Assets.* The Company's aggregate invested assets, including fixed maturity investments, short-term investments, equity securities, other investments, cash and cash equivalents and pending securities transactions, as of September 30, 2013 totaled \$6.4 billion, which is consistent with the aggregate invested assets of \$6.6 billion as of December 31, 2012.

At September 30, 2013, the unrealized losses on the Company's fixed income investments were primarily due to an increase in interest rates and widening of credit spreads, rather than any actual credit losses on these securities. The Company had no intention to sell nor was required to sell the fixed income investments that were in an unrealized loss position at September 30, 2013. The Company has the ability and intent to hold equity securities until recovery, and the Company currently believes it is probable that it will collect all amounts due according to their respective contractual terms. Therefore, the Company does not consider its fixed income investments or equity securities to be other-than-temporarily impaired at September 30, 2013.

The Company's aggregate direct exposure to the indebtedness and equity securities of those countries whose currency is the Euro or whose sovereign debt rating is below AAA (except the U.S.) was \$222.2 million at September 30, 2013, compared to \$247.1 million at December 31, 2012.

In addition to the direct exposures above, the Company has indirect exposure to sovereign and non-sovereign investments whose currency is the Euro or whose sovereign debt rating is below AAA through a hedge fund with a primary focus on European indebtedness, principally focused on benefiting from the declining value of European sovereign indebtedness.

## Cash Flows

	Nine Months Ended September 30,	
	2013	2012
	(U.S. dollars in thousands)	
Net cash (used in) provided by operating activities	\$ (16,574)	\$ 211,449
Net cash used in investing activities	(253,487)	(146,600)
Net cash used in financing activities	(52,992)	(67,828)
Effect of exchange rate changes on cash and cash equivalents	(10,967)	7,841
Net (decrease) increase in cash and cash equivalents	(334,020)	4,862
Cash and cash equivalents, beginning of period	1,124,019	890,914
Cash and cash equivalents, end of period	\$ 789,999	\$ 895,776

The decrease in cash flows (used in) provided by operating activities in the nine months ended September 30, 2013 compared to the same period in 2012 was primarily due to the payment of claims related to prior years and a shift in settlement dates for agriculture insurance related receivables from the U.S. Federal Government, which impact third quarter cash flows as well as the nine months ended September 30, 2013.

The increase in cash used in investing activities reflected the Company's active management of its investment portfolio on a fair value basis to generate attractive economic returns and income. Movements in financial markets and interest rates influence the timing of investment sales and purchases. The increase in cash flows used in investing activities in 2013 principally reflected reduced proceeds from sales and maturities of available for sale investments partially offset by reduced purchases of available for sale investments and other investments compared to 2012.

The cash flows used in financing activities in 2013 were lower than in 2012 principally due to increased issuances of common shares, partially offset by repurchases of common shares in 2013.

On May 28, 2013, prior to John R. Charman becoming the Company's Chairman and Chief Executive Officer, Mr. Charman, together with members of his family, purchased from the Company \$30.0 million of newly issued ordinary shares.

During the nine months ended September 30, 2013, the Company used its capital to repurchase 318,252 ordinary shares in the open market for \$14.6 million at an average price per share of \$45.83. During the nine months ended September 30, 2012, the Company repurchased \$1.0 million of its 6.15% Senior Notes due October 15, 2015.

As of September 30, 2013 and December 31, 2012, the Company had pledged cash and cash equivalents and fixed maturity investments of \$215.8 million and \$224.4 million, respectively, in favor of certain ceding companies to collateralize obligations. As of September 30, 2013 and December 31, 2012, the Company had also pledged \$303.3 million and \$380.0 million of its cash and fixed maturity investments to meet collateral obligations for \$259.5 million and \$320.4 million in letters of credit outstanding under its credit facility, respectively. In addition, at September 30, 2013 and December 31, 2012, cash and fixed maturity investments with fair values of \$274.6 million and \$280.0 million were on deposit with U.S. state regulators, respectively.

*Credit Facility.* Under the Company's credit facility, the Company and its subsidiaries have access to a revolving line of credit of up to \$700.0 million, which expires April 19, 2016. As of September 30, 2013, there were no borrowings under this facility and letters of credit outstanding under the facility were \$259.5 million.

Historically, the operating subsidiaries of the Company have generated sufficient cash flows to meet all of their obligations. Because of the inherent volatility of the business written by the Company, the seasonality in the timing of payments by ceding companies, the irregular timing of loss payments, the impact of a change in interest rates on the Company's investment returns as well as seasonality in coupon payment dates for fixed maturity investments, cash flows from the Company's operating activities may vary significantly between periods. The Company expects to generate

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positive operating cash flows through 2013, absent the occurrence of additional significant loss events. In the event that paid losses accelerate beyond the ability to fund such payments from operating cash flows, the Company would use its cash balances available, liquidate a portion of its investment portfolio, access its existing credit facility, or arrange for additional financing. However, there can be no assurance that the Company will be successful in executing these strategies.

### **Currency and Foreign Exchange**

The Company's functional currencies are U.S. dollars for its U.S. and Bermuda operations and British Sterling for its U.K. operations. The reporting currency for all operations is U.S. dollars. The Company maintains a portion of its investments and liabilities in currencies other than the U.S. dollar. The Company has made a significant investment in the capitalization of Endurance U.K, which is subject to the PRA's rules concerning the matching of the currency of its assets to the currency of its liabilities. Depending on the profile of Endurance U.K.'s liabilities, it may be required to hold some of its assets in currencies corresponding to the currencies of its liabilities. The Company may, from time to time, experience gains or losses resulting from fluctuations in the values of foreign currencies, which could have a material adverse effect on the Company's results of operations.

Assets and liabilities of foreign operations whose functional currency is not the U.S. dollar are translated at exchange rates in effect at the balance sheet date. Revenues and expenses of such foreign operations are translated at average exchange rates during the year. The effect of the translation adjustments for foreign operations is included in accumulated other comprehensive income.

Other monetary assets and liabilities denominated in foreign currencies are revalued at the exchange rates in effect at the balance sheet date with the resulting foreign exchange gains and losses included in earnings. Revenues and expenses denominated in foreign currencies are translated at the prevailing exchange rate on the transaction date.

### **Effects of Inflation**

The effects of inflation could cause the severity of claims to rise in the future. The Company's estimates for losses and loss expenses include assumptions about future payments for settlement of claims and claims handling expenses, such as medical treatments and litigation costs. To the extent inflation causes these costs to increase above reserves established for these claims, the Company will be required to increase the reserve for losses and loss expenses with a corresponding reduction in its earnings in the period in which the deficiency is identified. In addition, inflation could lead to higher interest rates causing the current unrealized gain position on the Company's fixed maturity portfolio to decrease or become an unrealized loss position. In response, the Company may choose to hold its fixed income investments to maturity, which would result in the unrealized gains largely amortizing through net investment income.

### **Cautionary Statement Regarding Forward-Looking Statements**

Some of the statements under "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations" and elsewhere in this Quarterly Report on Form 10-Q may include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 ("PSLRA"). The PSLRA provides a "safe harbor" for forward-looking statements. These forward-looking statements reflect our current views with respect to us specifically and the insurance and reinsurance business generally, investments, capital markets and the general economic environments in which we operate. Statements which include the words "expect," "intend," "plan," "believe," "project," "anticipate," "seek," "will," and similar statements of a future or forward-looking nature identify forward-looking statements for purposes of the PSLRA or otherwise.

All forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause actual results to differ materially from those indicated in such statements. We believe that these factors include, but are not limited to, the following:

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- the effects of competitors' pricing policies, and of changes in laws and regulations on competition, industry consolidation and development of competing financial products;
- greater frequency or severity of claims and loss activity, including as a result of natural or man-made catastrophic events or as a result of changing climate conditions, than our underwriting, reserving or investment practices have anticipated;
- changes in market conditions in the agriculture industry, which may vary depending upon demand for agricultural products, weather, commodity prices, natural disasters, technological advances in agricultural practices, changes in U.S. and foreign legislation and policies related to agricultural products and producers;
- termination of or changes in the terms of the U.S. multiple peril crop insurance program and termination or changes to the U.S. farm bill, including modifications to the Standard Reinsurance Agreement put in place by the Risk Management Agency of the U.S. Department of Agriculture;
- decreased demand for property and casualty insurance or reinsurance or increased competition due to an increase in capacity of property and casualty insurers and reinsurers;
- changes in the availability, cost or quality of reinsurance or retrocessional coverage;
- the inability to renew business previously underwritten or acquired;
- the inability to obtain or maintain financial strength or claims-paying ratings by one or more of our subsidiaries;
- our ability to effectively integrate acquired operations and to continue to expand our business;
- uncertainties in our reserving process, including the potential for adverse development of our loss reserves or failure of our loss limitation methods;
- the ability of the counterparty institutions with which we conduct business to continue to meet their obligations to us;
- the failure or delay of the Florida Hurricane Catastrophe Fund or private market participants in Florida to promptly pay claims, particularly following a large windstorm or of multiple smaller storms;
- our continued ability to comply with applicable financial standards and restrictive covenants, the breach of which could trigger significant collateral or prepayment obligations;
- Endurance Holdings or Endurance Bermuda becomes subject to income taxes in jurisdictions outside of Bermuda;
- changes in tax regulations or laws applicable to us, our subsidiaries, brokers or customers;
- state, federal and foreign regulations that impede our ability to charge adequate rates and efficiently allocate capital;
- changes in insurance regulations in the U.S. or other jurisdictions in which we operate, including the new Federal Insurance Office within the U.S. Department of the Treasury and other regulatory changes mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 in the United States and the implementation of Solvency II by the European Commission;
- reduced acceptance of our existing or new products and services;
- loss of business provided by any one of a few brokers on whom we depend for a large portion of our revenue, and our exposure to the credit risk of our brokers;
- actions by our competitors, many of which are larger or have greater financial resources than we do;
- assessments by states for high risk or otherwise uninsured individuals;
- the impact of acts of terrorism and acts of war;

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- the effects of terrorist related insurance legislation and laws;
- loss of key personnel;
- political stability of Bermuda;
- changes in the political environment of certain countries in which we operate or underwrite business;
- changes in accounting regulation, policies or practices;
- our investment performance;
- the valuation of our invested assets and the determination of impairments of those assets, if any;
- the breach of our investment guidelines or the inability of those guidelines to mitigate investment risk;
- the possible further downgrade of U.S. or foreign government securities by credit rating agencies, and the resulting effect on the value of U.S. or foreign government and other securities in our investment portfolio as well as the uncertainty in the market generally;
- the need for additional capital in the future which may not be available or only available on unfavorable terms;
- the ability to maintain the availability of our systems and safeguard the security of our data in the event of a disaster or other unanticipated event; and
- changes in general economic conditions, including inflation, foreign currency exchange rates, interest rates, and other factors.

The foregoing review of important factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included in our 2012 Form 10-K, including the risk factors set forth in Item 1A thereof. We undertake no obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise.



**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

There have been no material changes in market risk from the information provided under the caption “Management’s Discussion and Analysis of Financial Condition and Results of Operations - Quantitative and Qualitative Information about Market Risk” included in the Company’s 2012 Form 10-K.

**Item 4. Controls and Procedures**

a) Disclosure Controls and Procedures. The Company’s management, with the participation of the Company’s Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company’s disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) as of the end of the period covered by this report. Based on such evaluation, the Company’s Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company’s disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act.

(b) Internal Control Over Financial Reporting. There have not been any changes in the Company’s internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the Company’s third fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

**PART II  
OTHER INFORMATION**

**Item 1. Legal Proceedings**

We are party to various legal proceedings generally arising in the normal course of our business. While any proceeding contains an element of uncertainty, we do not believe that the eventual outcome of any litigation or arbitration proceeding to which we are presently a party could have a material adverse effect on our financial condition or business. Pursuant to our insurance and reinsurance agreements, disputes are generally required to be finally settled by arbitration.

**Item 1A. Risk Factors**

There have been no material changes to the risk factors disclosed in Item 1A. Risk Factors in our 2012 Form 10-K.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

**ISSUER PURCHASES OF EQUITY SECURITIES**

Period	(a) Total Number of Shares Purchased <sup>(1)</sup>	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>(1) (2)</sup>	(d) Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs <sup>(1) (2)</sup>
July 1, 2013 – July 31, 2013	—	\$ —	—	6,430,439
August 1, 2013 – August 31, 2013	—	\$ —	—	6,430,439
September 1, 2013 – September 30, 2013	—	\$ —	—	6,430,439
Total	—	\$ —	—	6,430,439

(1) Ordinary shares or share equivalents.

(2) At its meeting on November 9, 2011, the Board of Directors of the Company authorized the repurchase of up to a total of 7,000,000 ordinary shares and share equivalents through November 30, 2013, superseding all previous authorizations.

**Item 3. Defaults Upon Senior Securities**

None

**Item 4. Mine Safety Disclosures**

Not applicable

**Item 5. Other Information**

None

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**Item 6. Exhibits**

- (a) The following sets forth those exhibits filed pursuant to Item 601 of Regulation S-K:

<b>Exhibit Number</b>	<b>Description</b>
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Exchange Act.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Exchange Act.
32	Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Condensed Consolidated Balance Sheets as at September 30, 2013 (unaudited) and December 31, 2012; (ii) the Unaudited Condensed Consolidated Statements of Income and Comprehensive Income for the three and nine months ended September 30, 2013 and 2012; (iii) the Unaudited Condensed Consolidated Statements of Changes in Shareholders' Equity for the nine months ended September 30, 2013 and 2012; (iv) the Unaudited Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2013 and 2012; and (v) the Notes to the Unaudited Condensed Consolidated Financial Statements for the nine months ended September 30, 2013 and 2012.

\*\* Management contract or compensatory plan or arrangement

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, this Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ENDURANCE SPECIALTY HOLDINGS LTD.

Date: November 7, 2013

By: /s/ John R. Charman

John R. Charman  
Chief Executive Officer

Date: November 7, 2013

By: /s/ Michael J. McGuire

Michael J. McGuire  
Chief Financial Officer (Principal Financial Officer)

**Endurance Specialty Holdings Ltd.**  
**Certification of Chief Executive Officer**  
**Pursuant to Rule 13a-14(a)**

I, John R. Charman, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Endurance Specialty Holdings Ltd.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 7, 2013

By: /s/ John R. Charman  
*Chief Executive Officer*

**Endurance Specialty Holdings Ltd.**  
**Certification of Chief Financial Officer**  
**Pursuant to Rule 13a-14(a)**

I, Michael J. McGuire, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Endurance Specialty Holdings Ltd.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and we have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 7, 2013

By: /s/ Michael J. McGuire  
*Chief Financial Officer*

**Endurance Specialty Holdings Ltd.**  
**CERTIFICATION PURSUANT TO SECTION 906**  
**OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Endurance Specialty Holdings Ltd. (the "Company") for the quarterly period ended September 30, 2013 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, in the capacities and on the dates indicated below, each hereby certify pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that (1) to the best of his knowledge the Report fully complies with requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 7, 2013

By: /s/ John R. Charman  
John R. Charman  
*Chief Executive Officer*

Date: November 7, 2013

By: /s/ Michael J. McGuire  
Michael J. McGuire  
*Chief Financial Officer*

This certification accompanies the Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

