

ARCH CAPITAL GROUP LTD.

Form 10-Q

November 09, 2015

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

FORM 10-Q

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

For the period ended September 30, 2015

Or

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

Commission file number: 001-26456

ARCH CAPITAL GROUP LTD.
(Exact name of registrant as specified in its charter)

Bermuda
(State or other jurisdiction of incorporation or organization)

Not Applicable
(I.R.S. Employer Identification No.)

Waterloo House, Ground Floor
100 Pitts Bay Road, Pembroke HM 08
(Address of principal executive offices)

(441) 278-9250
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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 (§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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

company” in Rule 12b-2 of the Exchange Act.

Large accelerated Filer Accelerated Filer Non-accelerated Filer 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

As of October 30, 2015, there were 122,450,741 common shares, \$0.0033 par value per share, of the registrant outstanding.

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
Arch Capital Group Ltd.:

We have reviewed the accompanying consolidated balance sheet of Arch Capital Group Ltd. and its subsidiaries (the “Company”) as of September 30, 2015, and the related consolidated statements of income and comprehensive income for the three-month and nine-month periods ended September 30, 2015 and September 30, 2014, and the consolidated statements of changes in shareholders’ equity and cash flows for the nine-month periods ended September 30, 2015 and September 30, 2014. These interim financial statements are the responsibility of the Company’s management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2014, and the related consolidated statements of income, comprehensive income, changes in shareholders’ equity, and cash flows for the year then ended (not presented herein), and in our report dated February 27, 2015, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet information as of December 31, 2014, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP

New York, New York
November 9, 2015

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(U.S. dollars in thousands, except share data)

	(Unaudited)	
	September 30, 2015	December 31, 2014
Assets		
Investments:		
Fixed maturities available for sale, at fair value (amortized cost: \$10,550,931 and \$10,701,557)	\$ 10,560,635	\$ 10,750,770
Short-term investments available for sale, at fair value (amortized cost: \$711,390 and \$801,758)	708,428	797,226
Collateral received under securities lending, at fair value (amortized cost: \$282,783 and \$40,473)	286,659	44,301
Equity securities available for sale, at fair value (cost: \$575,292 and \$562,534)	606,259	658,182
Other investments available for sale, at fair value (cost: \$245,356 and \$264,747)	281,014	296,224
Investments accounted for using the fair value option	2,783,165	2,425,053
Investments accounted for using the equity method	589,277	349,014
Total investments	15,815,437	15,320,770
Cash	649,779	485,702
Accrued investment income	76,142	74,316
Securities pledged under securities lending, at fair value (amortized cost: \$285,979 and \$52,076)	285,632	50,802
Premiums receivable	1,074,884	948,695
Reinsurance recoverable on unpaid and paid losses and loss adjustment expenses	1,832,386	1,812,845
Contractholder receivables	1,436,154	1,309,192
Prepaid reinsurance premiums	442,346	377,078
Deferred acquisition costs, net	448,893	414,525
Receivable for securities sold	705,821	78,170
Goodwill and intangible assets	103,620	109,539
Other assets	899,498	1,024,447
Total assets	\$ 23,770,592	\$ 22,006,081
Liabilities		
Reserve for losses and loss adjustment expenses	\$ 9,084,855	\$ 9,036,448
Unearned premiums	2,467,691	2,231,578
Reinsurance balances payable	235,562	219,312
Contractholder payables	1,436,154	1,309,192
Collateral held for insured obligations	242,928	184,219
Deposit accounting liabilities	270,876	327,384
Senior notes	791,264	791,141
Revolving credit agreement borrowings	339,077	100,000
Securities lending payable	292,838	50,529
Payable for securities purchased	817,371	128,413
Other liabilities	649,910	509,219
Total liabilities	16,628,526	14,887,435
Commitments and Contingencies		

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Redeemable noncontrolling interests	205,089	219,512
Shareholders' Equity		
Non-cumulative preferred shares	325,000	325,000
Common shares (\$0.0033 par, shares issued: 172,903,518 and 171,672,408)	576	572
Additional paid-in capital	450,948	383,073
Retained earnings	7,317,277	6,854,571
Accumulated other comprehensive income, net of deferred income tax	9,809	128,856
Common shares held in treasury, at cost (shares: 50,464,964 and 44,304,474)	(1,940,795)	(1,562,019)
Total shareholders' equity available to Arch	6,162,815	6,130,053
Non-redeemable noncontrolling interests	774,162	769,081
Total shareholders' equity	6,936,977	6,899,134
Total liabilities, noncontrolling interests and shareholders' equity	\$23,770,592	\$22,006,081

See Notes to Consolidated Financial Statements

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(U.S. dollars in thousands, except share data)

	(Unaudited) Three Months Ended September 30,		(Unaudited) Nine Months Ended September 30,	
	2015	2014	2015	2014
Revenues				
Net premiums written	\$971,972	\$959,539	\$2,982,547	\$2,996,457
Change in unearned premiums	(35,289)	(55,888)	(192,162)	(325,874)
Net premiums earned	936,683	903,651	2,790,385	2,670,583
Net investment income	86,233	80,105	252,190	220,089
Net realized gains (losses)	(89,698)	18,515	(42,075)	92,356
Other-than-temporary impairment losses	(8,901)	(8,593)	(17,274)	(26,313)
Less investment impairments recognized in other comprehensive income, before taxes	3,033	—	4,494	—
Net impairment losses recognized in earnings	(5,868)	(8,593)	(12,780)	(26,313)
Other underwriting income	7,623	1,702	26,876	5,317
Equity in net income (loss) of investment funds accounted for using the equity method	(2,118)	4,966	19,938	17,459
Other income (loss)	(265)	(7,815)	52	(5,069)
Total revenues	932,590	992,531	3,034,586	2,974,422
Expenses				
Losses and loss adjustment expenses	531,741	501,673	1,544,883	1,423,431
Acquisition expenses	171,566	163,547	510,067	482,047
Other operating expenses	156,959	149,480	483,449	451,629
Interest expense	13,300	4,152	30,047	32,890
Net foreign exchange gains	(14,680)	(56,031)	(61,598)	(47,174)
Total expenses	858,886	762,821	2,506,848	2,342,823
Income before income taxes	73,704	229,710	527,738	631,599
Income tax expense	(9,704)	(6,446)	(29,162)	(17,473)
Net income	\$64,000	\$223,264	\$498,576	\$614,126
Amounts attributable to noncontrolling interests	16,033	5,411	(19,417)	5,065
Net income available to Arch	80,033	228,675	479,159	619,191
Preferred dividends	(5,484)	(5,484)	(16,453)	(16,453)
Net income available to Arch common shareholders	\$74,549	\$223,191	\$462,706	\$602,738
Net income per common share				
Basic	\$0.62	\$1.69	\$3.79	\$4.56
Diluted	\$0.60	\$1.64	\$3.66	\$4.42
Weighted average common shares and common share equivalents outstanding				
Basic	120,567,410	131,945,962	122,151,971	132,151,824
Diluted	125,011,773	135,876,605	126,354,759	136,354,172

See Notes to Consolidated Financial Statements

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(U.S. dollars in thousands)

	(Unaudited) Three Months Ended September 30, 2015		(Unaudited) Nine Months Ended September 30, 2014	
Comprehensive Income				
Net income	\$64,000	\$223,264	\$498,576	\$614,126
Other comprehensive income (loss), net of deferred income tax				
Unrealized appreciation (decline) in value of available-for-sale investments:				
Unrealized holding gains (losses) arising during period	(53,891)	(90,619)	(51,522)	89,162)
Portion of other-than-temporary impairment losses recognized in other comprehensive income, net of deferred income tax	(3,033)	—	(4,494)	—
Reclassification of net realized (gains) losses, net of income taxes, included in net income	12,278	(17,483)	(39,868)	(47,017)
Foreign currency translation adjustments	(12,082)	(23,595)	(23,259)	(14,923)
Comprehensive income	7,272	91,567	379,433	641,348
Amounts attributable to noncontrolling interests	16,129	5,411	(19,321)	5,065
Comprehensive income available to Arch	\$23,401	\$96,978	\$360,112	\$646,413

See Notes to Consolidated Financial Statements

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(U.S. dollars in thousands)

	(Unaudited)	
	Nine Months Ended	
	September 30,	
	2015	2014
Non-cumulative preferred shares		
Balance at beginning and end of period	\$325,000	\$325,000
Common shares		
Balance at beginning of year	572	565
Common shares issued, net	4	6
Balance at end of period	576	571
Additional paid-in capital		
Balance at beginning of year	383,073	299,517
Common shares issued, net	7,440	6,401
Exercise of stock options	12,363	14,891
Amortization of share-based compensation	46,575	45,118
Other	1,497	481
Balance at end of period	450,948	366,408
Retained earnings		
Balance at beginning of year	6,854,571	6,042,154
Net income	498,576	614,126
Amounts attributable to noncontrolling interests	(19,417	) 5,065
Preferred share dividends	(16,453	) (16,453
Balance at end of period	7,317,277	6,644,892
Accumulated other comprehensive income		
Balance at beginning of year	128,856	74,964
Unrealized appreciation in value of available-for-sale investments, net of deferred income tax:		
Balance at beginning of year	161,598	80,692
Unrealized holding (losses) gains arising during period, net of reclassification adjustment	(91,390	) 42,145
Portion of other-than-temporary impairment losses recognized in other comprehensive income, net of deferred income tax	(4,494) —
Balance at end of period	65,714	122,837
Foreign currency translation adjustments:		
Balance at beginning of year	(32,742	) (5,728
Foreign currency translation adjustments	(23,163	) (14,923
Balance at end of period	(55,905	) (20,651
Balance at end of period	9,809	102,186
Common shares held in treasury, at cost		
Balance at beginning of year	(1,562,019) (1,094,704
Shares repurchased for treasury	(378,776) (263,307

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Balance at end of period	(1,940,795)	(1,358,011)
Total shareholders' equity available to Arch	6,162,815	6,081,046
Non-redeemable noncontrolling interests	774,162	782,020
Total shareholders' equity	\$6,936,977	\$6,863,066

See Notes to Consolidated Financial Statements

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(U.S. dollars in thousands)

	(Unaudited)	
	Nine Months Ended	
	September 30,	
	2015	2014
Operating Activities		
Net income	\$498,576	\$614,126
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized losses (gains)	21,980	(113,033)
Net impairment losses recognized in earnings	12,780	26,313
Equity in net income or loss of investment funds accounted for using the equity method and other income or loss	3,983	3,784
Share-based compensation	46,575	45,118
Changes in:		
Reserve for losses and loss adjustment expenses, net of unpaid losses and loss adjustment expenses recoverable	139,577	94,255
Unearned premiums, net of prepaid reinsurance premiums	192,162	325,874
Premiums receivable	(108,741)	(279,766)
Deferred acquisition costs, net	(41,722)	(72,120)
Reinsurance balances payable	4,242	49,621
Other liabilities	6,638	117,889
Other items	31,529	(12,402)
Net Cash Provided By Operating Activities	807,579	799,659
Investing Activities		
Purchases of fixed maturity investments	(22,382,104)	(22,030,862)
Purchases of equity securities	(485,526)	(366,578)
Purchases of other investments	(1,320,250)	(1,136,285)
Proceeds from sales of fixed maturity investments	21,411,554	20,273,351
Proceeds from sales of equity securities	509,008	305,034
Proceeds from sales, redemptions and maturities of other investments	858,368	566,518
Proceeds from redemptions and maturities of fixed maturity investments	630,397	636,729
Net settlements of derivative instruments	81,114	15,495
Proceeds from investment in joint venture	40,000	—
Net sales of short-term investments	181,741	678,388
Change in cash collateral related to securities lending	28,685	(2,737)
Purchase of business, net of cash acquired	818	(235,578)
Purchases of fixed assets	(10,901)	(14,575)
Change in other assets	(43,654)	—
Net Cash Used For Investing Activities	(500,750)	(1,311,100)
Financing Activities		
Purchases of common shares under share repurchase program	(365,383)	(251,919)
Proceeds from common shares issued, net	697	3,248
Proceeds from borrowings	239,077	—
Change in cash collateral related to securities lending	(28,685)	2,737
Third party investment in non-redeemable noncontrolling interests	—	796,903
Third party investment in redeemable noncontrolling interests	—	219,233
Dividends paid to redeemable noncontrolling interests	(13,810)	(9,632)

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Other	50,463	6,559	
Preferred dividends paid	(16,453) (16,453)
Net Cash Provided By (Used For) Financing Activities	(134,094) 750,676	
Effects of exchange rate changes on foreign currency cash	(8,658	) (9,566)
Increase in cash	164,077	229,669	
Cash beginning of year	485,702	434,057	
Cash end of period	\$649,779	\$663,726	
Income taxes paid	\$35,460	\$13,335	
Interest paid	\$25,195	\$22,111	

See Notes to Consolidated Financial Statements

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. General

Arch Capital Group Ltd. (“ACGL”) is a Bermuda public limited liability company which provides insurance and reinsurance on a worldwide basis through its subsidiaries (together with ACGL, the “Company”). The Company’s consolidated financial statements include the results of Watford Holdings Ltd., the parent of Watford Re Ltd. (see Note 3).

The interim consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”). All significant intercompany transactions and balances have been eliminated in consolidation. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and assumptions. In the opinion of management, the accompanying unaudited interim consolidated financial statements reflect all adjustments (consisting of normally recurring accruals) necessary for a fair statement of results on an interim basis. The results of any interim period are not necessarily indicative of the results for a full year or any future periods.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted; however, management believes that the disclosures are adequate to make the information presented not misleading. This report should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2014 (“2014 Form 10-K”), including the Company’s audited consolidated financial statements and related notes.

The Company has reclassified the presentation of certain prior year information to conform to the current presentation. Such reclassifications had no effect on the Company’s net income, comprehensive income, shareholders’ equity or cash flows. Tabular amounts are in U.S. Dollars in thousands, except share amounts, unless otherwise noted.

Acquisition of Gulf Reinsurance Limited

In May 2008, the Company provided \$100.0 million of funding to Gulf Reinsurance Limited, a wholly owned subsidiary of Gulf Re Holdings Limited (collectively, “Gulf Re”), pursuant to the joint venture agreement with Gulf Investment Corporation GSC (“GIC”). Under the agreement, Arch Re Bermuda and GIC each owned 50% of Gulf Re. The Company entered into a number of strategic initiatives related to Gulf Re in the 2014 fourth quarter, including an agreement to acquire complete ownership and effective control of Gulf Re. Such agreement was approved by the Dubai Financial Services Authority in April 2015 and the transaction closed on May 14, 2015. Pursuant to the agreement, Gulf Re distributed \$130.6 million in total to the Company and GIC, and Gulf Re maintained \$50.7 million of equity capital. The Company purchased GIC’s remaining investment in Gulf Re for \$25.6 million through a transfer of fixed maturity investments. GIC will continue to participate equally with the Company in the financial results of Gulf Re and have the ability to purchase shares in Gulf Re over the next seven years. The acquisition resulted in no goodwill or other intangible assets as the fair value of Gulf Re was equal to its book value at closing.

2. Recent Accounting Pronouncements

Recently Issued Accounting Standards Adopted

The Company adopted accounting guidance in the 2015 second quarter which changes the accounting for repurchase and resale-to-maturity agreements by requiring that such agreements be recognized as financing arrangements, and requires that a transfer of a financial asset and a repurchase agreement entered into contemporaneously be accounted for separately. The new accounting guidance also requires additional disclosures about certain transferred financial assets accounted for as sales and certain securities lending transactions. Disclosures are not required to be presented for comparative periods before the effective date. See Note 6, “Investment Information—Securities Lending Agreements.”

The Company adopted accounting guidance in the 2015 second quarter which relates to the presentation of debt issuance costs. Such guidance requires presentation of debt issuance costs in the balance sheet as a deduction from the carrying amount of the related debt liability instead of a deferred charge. The Company previously included its debt issuance costs within ‘other assets.’ The guidance was applied retrospectively and resulted in reductions in ‘other assets’ and ‘senior notes’ at June 30, 2015

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

of \$8.8 million, respectively, and \$8.9 million at December 31, 2014, respectively. The adoption of this change in accounting principle did not impact the Company's shareholders' equity or net income.

The Company adopted accounting guidance pertaining to the categorization within the fair value hierarchy of certain investments measured at fair value using the net asset value per share as a practical expedient. These investments are no longer required to be categorized within the fair value hierarchy but are still required to be reported in the fair value hierarchy table to permit reconciliation back to the consolidated balance sheet. Additionally, certain disclosures are no longer applicable for investments that are eligible to be measured using the practical expedient, but for which the practical expedient was not elected. The guidance was applied retrospectively and only impacted the Company's disclosures. See Note 7, "Fair Value."

Recently Issued Accounting Standards Not Yet Adopted

An accounting standard was issued in the 2014 second quarter which will change the manner in which most companies recognize revenue. The standard requires that revenue reflect the transfer of goods or services to customers based on the consideration or payment the company expects to be entitled to in exchange for those goods or services; however, the standard does not change the accounting for insurance contracts or financial instruments. The new standard also requires enhanced disclosures about revenue. This accounting guidance is effective in the 2018 first quarter and may be applied on a full retrospective or modified retrospective approach. The Company is assessing the impact the implementation of this standard will have on its consolidated financial statements.

An accounting standard was issued in the 2015 first quarter providing targeted improvements to consolidation guidance for limited partnerships and other similarly structured entities. The new standard addresses instances where a reporting entity consolidates another entity when the reporting entity is simply acting on the behalf of others, amongst other related issues. While the standard is targeted, the application is relevant for all companies that are required to assess whether or not to consolidate certain entities. The standard is effective in the 2016 first quarter and early adoption is permitted. The Company is assessing the impact the implementation of this standard will have on its consolidated financial statements.

A new accounting standard was issued in the 2015 second quarter requiring new disclosures about the reserve for losses and loss adjustment expenses for short-duration insurance contracts. These disclosures will provide additional insight into an insurance entity's ability to underwrite and anticipate costs associated with claims. This accounting guidance is effective for the 2016 annual reporting period and interim periods thereafter and should be applied retrospectively. The Company is assessing the impact the implementation of this standard will have on its consolidated financial statements.

3. Variable Interest Entity and Noncontrolling Interests

Variable interest entity

On March 20, 2014, the Company invested \$100.0 million and acquired approximately 11% of Watford Holdings Ltd.'s common equity and a warrant to purchase additional common equity. Watford Holdings Ltd. is the parent of Watford Re Ltd., a multi-line Bermuda reinsurance company (together with Watford Holdings Ltd., "Watford Re"). Watford Re is considered a variable interest entity ("VIE") and the Company concluded that it is the primary beneficiary of Watford Re. As such, the results of Watford Re are included in the Company's consolidated financial statements.

The Company concluded that Watford Re represents a separate operating segment and provides the income statement and total investable assets, total assets and total liabilities of Watford Re within Note 5. At September 30, 2015, Watford Re's liabilities included unearned premiums of \$274.7 million and reserves for losses and loss adjustment expenses of \$223.9 million, some of which is related to transactions with the Company, along with \$239.1 million of revolving credit agreement borrowings (see Note 9). For the nine months ended September 30, 2015, Watford Re generated \$204.3 million of cash provided by operating activities and \$268.3 million of cash provided by financing activities, partially offset by \$354.5 million of cash used for investing activities.

The Company does not guarantee or provide credit support for Watford Re, and the Company's financial exposure to Watford Re is limited to its investment in Watford Re's common and preferred shares and counterparty credit risk (mitigated by collateral) arising from the reinsurance transactions.

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Non-redeemable noncontrolling interests

The Company accounts for the portion of Watford Re's common equity attributable to third party investors in the shareholders' equity section of its consolidated balance sheets. The noncontrolling ownership in Watford Re's common shares was approximately 89% at September 30, 2015. The portion of Watford Re's income or loss attributable to third party investors is recorded in the consolidated statements of income in 'amounts attributable to noncontrolling interests.' The following table sets forth activity in the non-redeemable noncontrolling interests:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
Balance, beginning of period	\$794,880	\$792,340	\$769,081	\$—
Sale of shares to noncontrolling interests	—	—	—	796,903
Amounts attributable to noncontrolling interests	(20,621)	(10,320)	5,178	(14,883)
Foreign currency translation adjustments	(97)	—	(97)	—
Balance, end of period	\$774,162	\$782,020	\$774,162	\$782,020

Redeemable noncontrolling interests

The Company accounts for redeemable noncontrolling interests in the mezzanine section of its consolidated balance sheets in accordance with applicable accounting guidance. Such redeemable noncontrolling interests relate to the 9,065,200 cumulative redeemable preference shares ("Watford Preference Shares") issued in late March 2014 with a par value of \$0.01 per share and a liquidation preference of \$25.00 per share. Preferred dividends, including the accretion of the discount and issuance costs, are included in 'amounts attributable to noncontrolling interests' in the Company's consolidated statements of income. The following table sets forth activity in the redeemable non-controlling interests:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
Balance, beginning of period	\$204,996	\$219,326	\$219,512	\$—
Sale of shares to noncontrolling interests	—	—	—	219,233
Shares acquired by the Company (1)	—	—	(14,700)	—
Accretion of preference share issuance costs	93	93	277	186
Balance, end of period	\$205,089	\$219,419	\$205,089	\$219,419

During the 2015 second quarter, the Company acquired Gulf Re, which owns 600,000 Watford Preference Shares. (1) Such shares, net of a discount, along with related dividends and accretion of the discount, are eliminated in consolidation.

The portion of Watford Re's income or loss attributable to third party investors is recorded in the consolidated statements of income in 'amounts attributable to noncontrolling interests' as summarized in the table below:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
Amounts attributable to non-redeemable noncontrolling interests	\$20,621	\$10,320	\$(5,178)	\$14,883
Dividends attributable to redeemable noncontrolling interests	(4,588)	(4,909)	(14,239)	(9,818)
Amounts attributable to noncontrolling interests	\$16,033	\$5,411	\$(19,417)	\$5,065

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

4. Earnings Per Common Share

The following table sets forth the computation of basic and diluted earnings per common share:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Numerator:				
Net income	\$64,000	\$223,264	\$498,576	\$614,126
Amounts attributable to noncontrolling interests	16,033	5,411	(19,417)	5,065
Net income available to Arch	80,033	228,675	479,159	619,191
Preferred dividends	(5,484)	(5,484)	(16,453)	(16,453)
Net income available to Arch common shareholders	\$74,549	\$223,191	\$462,706	\$602,738
Denominator:				
Weighted average common shares outstanding — basic	120,567,410	131,945,962	122,151,971	132,151,824
Effect of dilutive common share equivalents:				
Nonvested restricted shares	1,322,053	1,156,790	1,260,247	1,134,481
Stock options (1)	3,122,310	2,773,853	2,942,541	3,067,867
Weighted average common shares and common share equivalents outstanding — diluted	125,011,773	135,876,605	126,354,759	136,354,172
Earnings per common share:				
Basic	\$0.62	\$1.69	\$3.79	\$4.56
Diluted	\$0.60	\$1.64	\$3.66	\$4.42

Certain stock options were not included in the computation of diluted earnings per share where the exercise price of the stock options exceeded the average market price and would have been anti-dilutive or where, when applying the treasury stock method to in-the-money options, the sum of the proceeds, including unrecognized compensation, (1) exceeded the average market price and would have been anti-dilutive. For the 2015 third quarter and 2014 third quarter, the number of stock options excluded were 390,406 and 1,355,087, respectively. For the nine months ended September 30, 2015 and 2014, the number of stock options excluded were 957,838 and 1,378,249, respectively.

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5. Segment Information

The Company classifies its businesses into three underwriting segments — insurance, reinsurance and mortgage — and two other operating segments — ‘other’ and corporate (non-underwriting). The Company determined its reportable segments using the management approach described in accounting guidance regarding disclosures about segments of an enterprise and related information. The accounting policies of the segments are the same as those used for the preparation of the Company’s consolidated financial statements. Intersegment business is allocated to the segment accountable for the underwriting results.

The Company’s insurance, reinsurance and mortgage segments each have managers who are responsible for the overall profitability of their respective segments and who are directly accountable to the Company’s chief operating decision makers, the Chairman, President and Chief Executive Officer of ACGL and the Chief Financial Officer of ACGL. The chief operating decision makers do not assess performance, measure return on equity or make resource allocation decisions on a line of business basis. Management measures segment performance for its three underwriting segments based on underwriting income or loss. The Company does not manage its assets by underwriting segment, with the exception of goodwill and intangible assets, and, accordingly, investment income is not allocated to each underwriting segment.

The insurance segment consists of the Company’s insurance underwriting units which offer specialty product lines on a worldwide basis. Product lines include: construction and national accounts; excess and surplus casualty; lenders products; professional lines; programs; property, energy, marine and aviation; travel, accident and health; and other (consisting of alternative markets, excess workers' compensation and surety business).

The reinsurance segment consists of the Company’s reinsurance underwriting units which offer specialty product lines on a worldwide basis. Product lines include: casualty; marine and aviation; other specialty; property catastrophe; property excluding property catastrophe (losses on a single risk, both excess of loss and pro rata); and other (consisting of life reinsurance, casualty clash and other).

The mortgage segment includes the results of Arch Mortgage Insurance Company (“Arch MI U.S.”) and Arch Mortgage Insurance Limited, leading providers of mortgage insurance products and services to the U.S. and European markets, respectively. Arch MI U.S. is approved as an eligible mortgage insurer by Federal National Mortgage Association (“Fannie Mae”) and Federal Home Loan Mortgage Corporation (“Freddie Mac”), each a government sponsored enterprise, or “GSE.” The mortgage segment also includes GSE credit risk-sharing transactions and mortgage reinsurance for the U.S. and Australian markets.

The corporate (non-underwriting) segment results include net investment income, other income (loss), other expenses incurred by the Company, interest expense, net realized gains or losses, net impairment losses included in earnings, equity in net income or loss of investment funds accounted for using the equity method, net foreign exchange gains or losses, income taxes and items related to the Company’s non-cumulative preferred shares. Such amounts exclude the results of the ‘other’ segment.

The ‘other’ segment includes the results of Watford Re (see Note 3). Watford Re has its own management and board of directors that is responsible for the overall profitability of the ‘other’ segment. For the ‘other’ segment, performance is measured based on net income or loss.

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The following tables summarize the Company's underwriting income or loss by segment, together with a reconciliation of underwriting income or loss to net income available to common shareholders:

	Three Months Ended September 30, 2015					
	Insurance	Reinsurance	Mortgage	Sub-Total	Other	Total
Gross premiums written (1)	\$752,438	\$329,327	\$74,657	\$1,158,451	\$131,165	\$1,189,192
Premiums ceded	(209,443)	(92,182)	(7,832)	(311,486)	(6,158)	(217,220)
Net premiums written	542,995	237,145	66,825	846,965	125,007	971,972
Change in unearned premiums	(20,451)	23,286	(12,277)	(9,442)	(25,847)	(35,289)
Net premiums earned	522,544	260,431	54,548	837,523	99,160	936,683
Other underwriting income	519	2,783	3,565	6,867	756	7,623
Losses and loss adjustment expenses	(339,859)	(115,780)	(9,562)	(465,201)	(66,540)	(531,741)
Acquisition expenses, net	(77,076)	(55,416)	(10,428)	(142,920)	(28,646)	(171,566)
Other operating expenses	(84,620)	(37,131)	(21,048)	(142,799)	(3,421)	(146,220)
Underwriting income (loss)	\$21,508	\$54,887	\$17,075	93,470	1,309	94,779
Net investment income				67,251	18,982	86,233
Net realized gains (losses)				(53,480)	(36,218)	(89,698)
Net impairment losses recognized in earnings				(5,868)	—	(5,868)
Equity in net income (loss) of investment funds accounted for using the equity method				(2,118)	—	(2,118)
Other income (loss)				(265)	—	(265)
Other expenses				(10,739)	—	(10,739)
Interest expense				(12,014)	(1,286)	(13,300)
Net foreign exchange gains (losses)				16,056	(1,376)	14,680
Income (loss) before income taxes				92,293	(18,589)	73,704
Income tax expense				(9,704)	—	(9,704)
Net income (loss)				82,589	(18,589)	64,000
Dividends attributable to redeemable noncontrolling interests				—	(4,588)	(4,588)
Amounts attributable to noncontrolling interests				—	20,621	20,621
Net income (loss) available to Arch				82,589	(2,556)	80,033
Preferred dividends				(5,484)	—	(5,484)
Net income (loss) available to Arch common shareholders				\$77,105	\$(2,556)	\$74,549

Underwriting Ratios

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Loss ratio	65.0	% 44.5	% 17.5	% 55.5	% 67.1	% 56.8	%
Acquisition expense ratio	14.8	% 21.3	% 19.1	% 17.1	% 28.9	% 18.3	%
Other operating expense ratio	16.2	% 14.3	% 38.6	% 17.1	% 3.4	% 15.6	%
Combined ratio	96.0	% 80.1	% 75.2	% 89.7	% 99.4	% 90.7	%
Goodwill and intangible assets	\$29,834	\$2,149	\$71,637	\$103,620	\$—	\$103,620	
Total investable assets				\$14,733,732	\$1,593,523	\$16,327,255	
Total assets				21,679,795	2,090,797	23,770,592	
Total liabilities				15,627,574	1,000,952	16,628,526	

Certain amounts included in the gross premiums written of each segment are related to intersegment transactions. (1) Accordingly, the sum of gross premiums written for each segment does not agree to the total gross premiums written as shown in the table above due to the elimination of intersegment transactions in the total.

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

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	Three Months Ended September 30, 2014						
	Insurance	Reinsurance	Mortgage	Sub-Total	Other	Total	
Gross premiums written (1)	\$726,683	\$345,747	\$66,389	\$1,138,392	\$103,483	\$1,159,907	
Premiums ceded	(187,689)	(83,502)	(7,904)	(278,668)	(3,668)	(200,368))
Net premiums written	538,994	262,245	58,485	859,724	99,815	959,539	
Change in unearned premiums	(19,607)	34,303	(5,539)	9,157	(65,045)	(55,888))
Net premiums earned	519,387	296,548	52,946	868,881	34,770	903,651	
Other underwriting income	499	215	988	1,702	—	1,702	
Losses and loss adjustment expenses	(338,319)	(123,784)	(15,987)	(478,090)	(23,583)	(501,673))
Acquisition expenses, net	(81,775)	(60,205)	(11,958)	(153,938)	(9,609)	(163,547))
Other operating expenses	(83,138)	(36,337)	(17,913)	(137,388)	(1,658)	(139,046))
Underwriting income (loss)	\$16,654	\$76,437	\$8,076	101,167	(80)	101,087)
Net investment income				72,239	7,866	80,105	
Net realized gains (losses)				31,411	(12,896)	18,515)
Net impairment losses recognized in earnings				(8,593)	—	(8,593))
Equity in net income (loss) of investment funds accounted for using the equity method				4,966	—	4,966	
Other income (loss)				(7,815)	—	(7,815))
Other expenses				(10,434)	—	(10,434))
Interest expense				(4,152)	—	(4,152))
Net foreign exchange gains (losses)				57,611	(1,580)	56,031)
Income (loss) before income taxes				236,400	(6,690)	229,710)
Income tax expense				(6,446)	—	(6,446))
Net income (loss)				229,954	(6,690)	223,264)
Dividends attributable to redeemable noncontrolling interests				—	(4,909)	(4,909))
Amounts attributable to noncontrolling interests				—	10,320	10,320	
Net income (loss) available to Arch				229,954	(1,279)	228,675)
Preferred dividends				(5,484)	—	(5,484))
Net income (loss) available to Arch common shareholders				\$224,470	\$(1,279)	\$223,191)
Underwriting Ratios							
Loss ratio	65.1	% 41.7	% 30.2	% 55.0	% 67.8	% 55.5	%
Acquisition expense ratio	15.7	% 20.3	% 22.6	% 17.7	% 27.6	% 18.1	%
Other operating expense ratio	16.0	% 12.3	% 33.8	% 15.8	% 4.8	% 15.4	%

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Combined ratio	96.8	% 74.3	% 86.6	% 88.5	% 100.2	% 89.0	%
Goodwill and intangible assets	\$24,024	\$3,939	\$83,565	\$111,528	\$—	\$111,528	
Total investable assets				\$14,580,425	\$1,124,048	\$15,704,473	
Total assets				21,205,209	1,403,018	22,608,227	
Total liabilities				15,221,030	304,712	15,525,742	

Certain amounts included in the gross premiums written of each segment are related to intersegment transactions. (1) Accordingly, the sum of gross premiums written for each segment does not agree to the total gross premiums written as shown in the table above due to the elimination of intersegment transactions in the total.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

	Nine Months Ended						Total
	September 30, 2015						
	Insurance	Reinsurance	Mortgage	Sub-Total	Other		
Gross premiums written (1)	\$2,263,401	\$1,156,540	\$203,770	\$3,625,382	\$387,752	\$3,730,423	
Premiums ceded	(669,336)	(318,197)	(23,404)	(1,012,608)	(17,979)	(747,876)	
Net premiums written	1,594,065	838,343	180,366	2,612,774	369,773	2,982,547	
Change in unearned premiums	(53,782)	(24,230)	(22,992)	(101,004)	(91,158)	(192,162)	
Net premiums earned	1,540,283	814,113	157,374	2,511,770	278,615	2,790,385	
Other underwriting income	1,467	6,870	14,969	23,306	3,570	26,876	
Losses and loss adjustment expenses	(978,681)	(339,495)	(33,010)	(1,351,186)	(193,697)	(1,544,883)	
Acquisition expenses, net	(228,877)	(170,380)	(31,046)	(430,303)	(79,764)	(510,067)	
Other operating expenses	(261,793)	(114,182)	(61,096)	(437,071)	(8,876)	(445,947)	
Underwriting income (loss)	\$72,399	\$196,926	\$47,191	316,516	(152)	316,364	
Net investment income				204,710	47,480	252,190	
Net realized gains (losses)				(14,831)	(27,244)	(42,075)	
Net impairment losses recognized in earnings				(12,780)	—	(12,780)	
Equity in net income (loss) of investment funds accounted for using the equity method				19,938	—	19,938	
Other income (loss)				52	—	52	
Other expenses				(37,502)	—	(37,502)	
Interest expense				(28,761)	(1,286)	(30,047)	
Net foreign exchange gains (losses)				60,338	1,260	61,598	
Income (loss) before income taxes				507,680	20,058	527,738	
Income tax expense				(29,162)	—	(29,162)	
Net income (loss)				478,518	20,058	498,576	
Dividends attributable to redeemable noncontrolling interests				—	(14,239)	(14,239)	
Amounts attributable to noncontrolling interests				—	(5,178)	(5,178)	
Net income (loss) available to Arch				478,518	641	479,159	
Preferred dividends				(16,453)	—	(16,453)	
Net income (loss) available to Arch common shareholders				\$462,065	\$641	\$462,706	
Underwriting Ratios							
Loss ratio	63.5	% 41.7	% 21.0	% 53.8	% 69.5	% 55.4	%
Acquisition expense ratio	14.9	% 20.9	% 19.7	% 17.1	% 28.6	% 18.3	%
Other operating expense ratio	17.0	% 14.0	% 38.8	% 17.4	% 3.2	% 16.0	%

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Combined ratio	95.4	% 76.6	% 79.5	% 88.3	% 101.3	% 89.7	%
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Certain amounts included in the gross premiums written of each segment are related to intersegment transactions. (1) Accordingly, the sum of gross premiums written for each segment does not agree to the total gross premiums written as shown in the table above due to the elimination of intersegment transactions in the total.

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

	Nine Months Ended						Total
	September 30, 2014						
	Insurance	Reinsurance	Mortgage	Sub-Total	Other		
Gross premiums written (1)	\$2,309,560	\$1,212,641	\$169,772	\$3,690,462	\$190,239	\$3,726,804	
Premiums ceded	(646,082)	(215,623)	(17,622)	(877,816)	(6,428)	(730,347)	
Net premiums written	1,663,478	997,018	152,150	2,812,646	183,811	2,996,457	
Change in unearned premiums	(158,878)	(23,495)	(9,606)	(191,979)	(133,895)	(325,874)	
Net premiums earned	1,504,600	973,523	142,544	2,620,667	49,916	2,670,583	
Other underwriting income	1,513	834	2,970	5,317	—	5,317	
Losses and loss adjustment expenses	(936,615)	(413,745)	(39,938)	(1,390,298)	(33,133)	(1,423,431)	
Acquisition expenses, net	(235,156)	(199,673)	(32,593)	(467,422)	(14,625)	(482,047)	
Other operating expenses	(250,111)	(110,198)	(48,077)	(408,386)	(4,402)	(412,788)	
Underwriting income (loss)	\$84,231	\$250,741	\$24,906	359,878	(2,244)	357,634	
Net investment income				211,690	8,399	220,089	
Net realized gains (losses)				102,074	(9,718)	92,356	
Net impairment losses recognized in earnings				(26,313)	—	(26,313)	
Equity in net income (loss) of investment funds accounted for using the equity method				17,459	—	17,459	
Other income (loss)				(5,069)	—	(5,069)	
Other expenses				(36,512)	(2,329)	(38,841)	
Interest expense				(32,890)	—	(32,890)	
Net foreign exchange gains (losses)				48,191	(1,017)	47,174	
Income (loss) before income taxes				638,508	(6,909)	631,599	
Income tax expense				(17,473)	—	(17,473)	
Net income (loss)				621,035	(6,909)	614,126	
Dividends attributable to redeemable noncontrolling interests				—	(9,818)	(9,818)	
Amounts attributable to noncontrolling interests				—	14,883	14,883	
Net income (loss) available to Arch				621,035	(1,844)	619,191	
Preferred dividends				(16,453)	—	(16,453)	
Net income (loss) available to Arch common shareholders				\$604,582	\$(1,844)	\$602,738	
Underwriting Ratios							
Loss ratio	62.3	% 42.5	% 28.0	% 53.1	% 66.4	% 53.3	%
Acquisition expense ratio	15.6	% 20.5	% 22.9	% 17.8	% 29.3	% 18.1	%
Other operating expense ratio	16.6	% 11.3	% 33.7	% 15.6	% 8.8	% 15.5	%

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Combined ratio	94.5	% 74.3	% 84.6	% 86.5	% 104.5	% 86.9	%
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Certain amounts included in the gross premiums written of each segment are related to intersegment transactions. (1) Accordingly, the sum of gross premiums written for each segment does not agree to the total gross premiums written as shown in the table above due to the elimination of intersegment transactions in the total.

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6. Investment Information

At September 30, 2015, total investable assets of \$16.33 billion included \$14.73 billion managed by the Company and \$1.59 billion attributable to Watford Re.

Available For Sale Investments

The following table summarizes the fair value and cost or amortized cost of the Company's investments classified as available for sale:

	Estimated Fair Value	Gross Unrealized Gains	Gross Unrealized Losses	Cost or Amortized Cost	OTTI Unrealized Losses (2)
September 30, 2015					
Fixed maturities (1):					
Corporate bonds	\$2,796,038	\$28,418	\$(54,489)	\$2,822,109	\$(3,033)
Mortgage backed securities	809,876	13,155	(2,998)	799,719	(3,554)
Municipal bonds	1,830,987	27,600	(2,771)	1,806,158	—
Commercial mortgage backed securities	810,973	10,058	(2,594)	803,509	—
U.S. government and government agencies	2,338,724	14,352	(2,138)	2,326,510	—
Non-U.S. government securities	887,120	13,070	(36,488)	910,538	—
Asset backed securities	1,372,549	9,032	(4,850)	1,368,367	(22)
Total	10,846,267	115,685	(106,328)	10,836,910	(6,609)
Equity securities	606,259	68,494	(37,527)	575,292	—
Other investments	281,014	39,287	(3,629)	245,356	—
Short-term investments	708,428	166	(3,128)	711,390	—
Total	\$12,441,968	\$223,632	\$(150,612)	\$12,368,948	\$(6,609)
December 31, 2014					
Fixed maturities (1):					
Corporate bonds	\$3,108,513	\$37,928	\$(38,974)	\$3,109,559	\$(317)
Mortgage backed securities	943,343	18,843	(3,842)	928,342	(3,307)
Municipal bonds	1,494,122	31,227	(1,044)	1,463,939	—
Commercial mortgage backed securities	1,114,528	14,594	(3,822)	1,103,756	—
U.S. government and government agencies	1,447,972	8,345	(1,760)	1,441,387	—
Non-U.S. government securities	1,015,153	21,311	(37,203)	1,031,045	—
Asset backed securities	1,677,941	8,425	(6,089)	1,675,605	(22)
Total	10,801,572	140,673	(92,734)	10,753,633	(3,646)
Equity securities	658,182	109,012	(13,364)	562,534	—
Other investments	296,224	31,839	(362)	264,747	—
Short-term investments	797,226	738	(5,270)	801,758	—
Total	\$12,553,204	\$282,262	\$(111,730)	\$12,382,672	\$(3,646)

(1)

In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See “—Securities Lending Agreements.”

(2) Represents the total other-than-temporary impairments (“OTTI”) recognized in accumulated other comprehensive income (“AOCI”). It does not include the change in fair value subsequent to the impairment measurement date. At September 30, 2015, the net unrealized loss related to securities for which a non-credit OTTI was recognized in AOCI was \$2.3 million, compared to a net unrealized gain of \$0.9 million at December 31, 2014.

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The following table summarizes, for all available for sale securities in an unrealized loss position, the fair value and gross unrealized loss by length of time the security has been in a continual unrealized loss position:

	Less than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
September 30, 2015						
Fixed maturities (1):						
Corporate bonds	\$1,208,894	\$(37,606)	\$135,135	\$(16,883)	\$1,344,029	\$(54,489)
Mortgage backed securities	235,252	(1,986)	52,621	(1,012)	287,873	(2,998)
Municipal bonds	219,610	(2,567)	9,717	(204)	229,327	(2,771)
Commercial mortgage backed securities	263,779	(2,376)	19,774	(218)	283,553	(2,594)
U.S. government and government agencies	283,534	(2,138)	—	—	283,534	(2,138)
Non-U.S. government securities	391,631	(23,526)	52,976	(12,962)	444,607	(36,488)
Asset backed securities	467,485	(3,262)	126,982	(1,588)	594,467	(4,850)
Total	3,070,185	(73,461)	397,205	(32,867)	3,467,390	(106,328)
Equity securities	311,608	(37,527)	—	—	311,608	(37,527)
Other investments	45,151	(3,629)	—	—	45,151	(3,629)
Short-term investments	33,873	(3,128)	—	—	33,873	(3,128)
Total	\$3,460,817	\$(117,745)	\$397,205	\$(32,867)	\$3,858,022	\$(150,612)
December 31, 2014						
Fixed maturities (1):						
Corporate bonds	\$1,309,637	\$(32,903)	\$148,963	\$(6,071)	\$1,458,600	\$(38,974)
Mortgage backed securities	293,624	(1,476)	59,107	(2,366)	352,731	(3,842)
Municipal bonds	210,614	(588)	13,643	(456)	224,257	(1,044)
Commercial mortgage backed securities	232,147	(770)	125,894	(3,052)	358,041	(3,822)
U.S. government and government agencies	618,381	(1,626)	3,438	(134)	621,819	(1,760)
Non-U.S. government securities	510,766	(31,172)	46,910	(6,031)	557,676	(37,203)
Asset backed securities	612,950	(2,486)	243,452	(3,603)	856,402	(6,089)
Total	3,788,119	(71,021)	641,407	(21,713)	4,429,526	(92,734)
Equity securities	181,002	(13,364)	—	—	181,002	(13,364)
Other investments	59,638	(362)	—	—	59,638	(362)
Short-term investments	79,271	(5,270)	—	—	79,271	(5,270)
Total	\$4,108,030	\$(90,017)	\$641,407	\$(21,713)	\$4,749,437	\$(111,730)

(1) In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See “—Securities Lending

Agreements.”

At September 30, 2015, on a lot level basis, approximately 2,300 security lots out of a total of approximately 5,540 security lots were in an unrealized loss position and the largest single unrealized loss from a single lot in the Company’s fixed maturity portfolio was \$3.6 million. At December 31, 2014, on a lot level basis, approximately 1,900 security lots out of a total of approximately 4,790 security lots were in an unrealized loss position and the largest single unrealized loss from a single lot in the Company’s fixed maturity portfolio was \$2.9 million.

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The contractual maturities of the Company's fixed maturities are shown in the following table. Expected maturities, which are management's best estimates, will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Maturity	September 30, 2015		December 31, 2014	
	Estimated Fair Value	Amortized Cost	Estimated Fair Value	Amortized Cost
Due in one year or less	\$329,589	\$331,322	\$235,930	\$233,794
Due after one year through five years	4,510,824	4,518,625	4,074,562	4,077,408
Due after five years through 10 years	2,583,000	2,585,634	2,475,726	2,461,356
Due after 10 years	429,456	429,734	279,542	273,372
	7,852,869	7,865,315	7,065,760	7,045,930
Mortgage backed securities	809,876	799,719	943,343	928,342
Commercial mortgage backed securities	810,973	803,509	1,114,528	1,103,756
Asset backed securities	1,372,549	1,368,367	1,677,941	1,675,605
Total (1)	\$10,846,267	\$10,836,910	\$10,801,572	\$10,753,633

(1) In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See "—Securities Lending Agreements."

Securities Lending Agreements

From time to time, the Company enters into securities lending agreements with financial institutions to enhance investment income. The Company loans certain of its securities to third parties, primarily major brokerage firms, for short periods of time through a lending agent. The Company maintains legal control over the securities it lends, retains the earnings and cash flows associated with the loaned securities and receives a fee from the borrower for the temporary use of the securities. An indemnification agreement with the lending agent protects the Company in the event a borrower becomes insolvent or fails to return any of the securities on loan to the Company.

The Company receives collateral in the form of cash or securities. Cash collateral primarily consists of short-term investments. At September 30, 2015, the fair value of the cash collateral received on securities lending was \$15.7 million, which included \$5.4 million that was reinvested in sub-prime mortgage backed securities, and the fair value of security collateral received was \$271.0 million. At December 31, 2014, the fair value of the cash collateral received on securities lending was \$44.3 million, which included \$5.8 million that was reinvested in sub-prime mortgage backed securities, and the fair value of security collateral received was nil.

The Company's securities lending transactions were accounted for as secured borrowings with significant investment categories as follows:

Securities Lending Transactions	September 30, 2015				
	Remaining Contractual Maturity of the Agreements				
	Overnight and Continuous	Less than 30 Days	30-90 Days	90 Days or More	Total
U.S. government and government agencies	\$225,898	\$—	\$22,784	\$3,569	\$252,251
Corporate bonds	35,266	—	—	—	35,266

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Equity securities	5,321	—	—	—	5,321
Total	\$266,485	\$—	\$22,784	\$3,569	\$292,838
Gross amount of recognized liabilities for securities lending in offsetting disclosure in Note 8					\$—
Amounts related to securities lending not included in offsetting disclosure in Note 8					\$292,838

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Other Investments

The following table summarizes the Company's other investments, including available for sale and fair value option components:

	September 30, 2015	December 31, 2014
Available for sale:		
Asian and emerging markets	\$ 210,680	\$ 236,586
Investment grade fixed income	31,429	59,638
Credit related funds	13,722	—
Other	25,183	—
Total available for sale	281,014	296,224
Fair value option:		
Term loan investments (par value: \$1,188,216 and \$1,094,337)	1,152,693	1,073,649
Mezzanine debt funds	112,782	121,341
Credit related funds	194,957	114,436
Investment grade fixed income	58,204	69,108
Asian and emerging markets	59,667	25,800
Other (1)	124,591	137,094
Total fair value option	1,702,894	1,541,428
Total	\$ 1,983,908	\$ 1,837,652

(1) Includes fund investments with strategies in mortgage servicing rights, transportation and infrastructure assets and other.

Certain of the Company's other investments are in investment funds for which the Company has the option to redeem at agreed upon values as described in each investment fund's subscription agreement. Depending on the terms of the various subscription agreements, investments in investment funds may be redeemed daily, monthly, quarterly or on other terms. Two common redemption restrictions which may impact the Company's ability to redeem these investment funds are gates and lockups. A gate is a suspension of redemptions which may be implemented by the general partner or investment manager of the fund in order to defer, in whole or in part, the redemption request in the event the aggregate amount of redemption requests exceeds a predetermined percentage of the investment fund's net assets which may otherwise hinder the general partner or investment manager's ability to liquidate holdings in an orderly fashion in order to generate the cash necessary to fund extraordinarily large redemption payouts. A lockup period is the initial amount of time an investor is contractually required to hold the security before having the ability to redeem. If the investment funds are eligible to be redeemed, the time to redeem such fund can take weeks or months following the notification.

Fair Value Option

The following table summarizes the Company's assets and liabilities which are accounted for using the fair value option:

	September 30, 2015	December 31, 2014
Fixed maturities	\$ 926,589	\$ 632,024
Other investments	1,702,894	1,541,428
Short-term investments	153,604	251,601

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Equity securities	78	—
Investments accounted for using the fair value option	\$ 2,783,165	\$ 2,425,053

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Net Investment Income

The components of net investment income were derived from the following sources:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
Fixed maturities	\$70,626	\$66,052	\$210,497	\$194,370
Term loan investments	16,922	14,066	49,699	26,643
Equity securities (dividends)	3,486	2,779	8,743	8,971
Short-term investments	127	905	548	1,417
Other (1)	10,277	7,913	33,513	21,732
Gross investment income	101,438	91,715	303,000	253,133
Investment expenses	(15,205)	(11,610)	(50,810)	(33,044)
Net investment income	\$86,233	\$80,105	\$252,190	\$220,089

(1) Includes income distributions from investment funds and other items.

Net Realized Gains (Losses)

Net realized gains (losses) were as follows, excluding other-than-temporary impairment provisions:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
Available for sale securities:				
Gross gains on investment sales	\$51,933	\$62,727	\$231,757	\$185,541
Gross losses on investment sales	(53,953)	(35,012)	(168,087)	(108,053)
Change in fair value of assets and liabilities accounted for using the fair value option:				
Fixed maturities	(41,236)	(9,023)	(49,729)	318
Other investments	(75,251)	(1,085)	(68,179)	27,676
Equity securities	71	—	—	—
Short-term investments	(9)	638	1,462	638
Derivative instruments (1)	35,889	7,449	31,069	7,083
Other (2)	(7,142)	(7,179)	(20,368)	(20,847)
Net realized gains (losses)	\$(89,698)	\$18,515	\$(42,075)	\$92,356

(1) See Note 8 for information on the Company's derivative instruments.

(2) Includes the re-measurement of contingent consideration liability amounts.

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Other-Than-Temporary Impairments

The Company performs quarterly reviews of its available for sale investments in order to determine whether declines in fair value below the amortized cost basis were considered other-than-temporary in accordance with applicable guidance. The following table details the net impairment losses recognized in earnings by asset class:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Fixed maturities:				
Mortgage backed securities	\$(85)	\$(2)	\$(1,483)	\$(2)
Corporate bonds	(4,282)	(147)	(6,268)	(811)
Commercial mortgage backed securities	—	(7)	—	(7)
Asset backed securities	—	(29)	—	(40)
Total	(4,367)	(185)	(7,751)	(860)
Short-term investments	—	—	(2,341)	—
Equity securities	(1,501)	(95)	(1,754)	(373)
Other investments	—	(8,313)	(934)	(25,080)
Net impairment losses recognized in earnings	\$(5,868)	\$(8,593)	\$(12,780)	\$(26,313)

A description of the methodology and significant inputs used to measure the amount of net impairment losses recognized in earnings 2015 third quarter is as follows:

Corporate bonds — the Company reviewed the business prospects, credit ratings, estimated loss given default factors, foreign currency impacts and information received from asset managers and rating agencies for certain corporate bonds. Approximately half of the impairment losses for the 2015 third quarter resulted from non-investment grade corporate bonds in the energy sector, reflecting current market conditions, with the remaining half related to foreign currency fluctuations on non-U.S. Dollar denominated investments based on the remaining time to maturity. The amortized cost basis of the corporate bonds were adjusted down, if required, to the expected recovery value calculated in the OTTI review process;

Equity securities – the Company utilized information received from asset managers on common stocks, including the business prospects, recent events, industry and market data and other factors. For certain equities which were in an unrealized loss position and where the Company determined that it did not have the intent or ability to hold such securities for a reasonable period of time by which the fair value of the securities would increase and the Company would recover its cost, the cost basis of such securities was adjusted down accordingly.

The Company believes that the \$6.6 million of OTTI included in accumulated other comprehensive income at September 30, 2015 on the securities which were considered by the Company to be impaired was due to market and sector-related factors (i.e., not credit losses). At September 30, 2015, the Company did not intend to sell these securities, or any other securities which were in an unrealized loss position, and determined that it is more likely than not that the Company will not be required to sell such securities before recovery of their cost basis.

The following table provides a roll forward of the amount related to credit losses recognized in earnings for which a portion of an OTTI was recognized in accumulated other comprehensive income:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014

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Balance at start of period	\$20,906	\$21,441	\$20,196	\$60,062
Credit loss impairments recognized on securities not previously impaired	4,024	—	8,794	—
Credit loss impairments recognized on securities previously impaired	41	151	175	162
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	—	(217) (4,194) (38,849
Balance at end of period	\$24,971	\$21,375	\$24,971	\$21,375

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Restricted Assets

The Company is required to maintain assets on deposit, which primarily consist of fixed maturities, with various regulatory authorities to support its insurance and reinsurance operations. The Company's insurance and reinsurance subsidiaries maintain assets in trust accounts as collateral for insurance and reinsurance transactions with affiliated companies and also have investments in segregated portfolios primarily to provide collateral or guarantees for letters of credit to third parties. See Note 9 for further details. The following table details the value of the Company's restricted assets:

	September 30, 2015	December 31, 2014
Assets used for collateral or guarantees:		
Affiliated transactions	\$ 3,737,514	\$ 4,138,527
Third party agreements	1,071,260	970,120
Deposits with U.S. regulatory authorities	405,817	337,981
Deposits with non-U.S. regulatory authorities	40,365	—
Trust funds	100,789	72,461
Total restricted assets	\$ 5,355,745	\$ 5,519,089

7. Fair Value

Accounting guidance regarding fair value measurements addresses how companies should measure fair value when they are required to use a fair value measure for recognition or disclosure purposes under GAAP and provides a common definition of fair value to be used throughout GAAP. It defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly fashion between market participants at the measurement date. In addition, it establishes a three-level valuation hierarchy for the disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The level in the hierarchy within which a given fair value measurement falls is determined based on the lowest level input that is significant to the measurement (Level 1 being the highest priority and Level 3 being the lowest priority).

The levels in the hierarchy are defined as follows:

Level 1: Inputs to the valuation methodology are observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets

Level 2: Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement

Following is a description of the valuation methodologies used for securities measured at fair value, as well as the general classification of such securities pursuant to the valuation hierarchy. The Company reviews its securities measured at fair value and discusses the proper classification of such investments with investment advisers and others.

The Company determines the existence of an active market based on its judgment as to whether transactions for the financial instrument occur in such market with sufficient frequency and volume to provide reliable pricing

information. The independent pricing sources obtain market quotations and actual transaction prices for securities that have quoted prices in active markets. The Company uses quoted values and other data provided by nationally recognized independent pricing sources as inputs into its process for determining fair values of its fixed maturity investments. To validate the techniques or models used by pricing sources, the Company's review process includes, but is not limited to: (i) quantitative analysis (e.g., comparing the quarterly return for each managed portfolio to its target benchmark, with significant differences identified and investigated); (ii) a review of the average number of prices obtained in the pricing process and the range of resulting fair values; (iii) initial and ongoing evaluation of methodologies used by outside parties to calculate fair value; (iv) a comparison of the fair value estimates to the Company's knowledge of the current market; (v) a comparison of the pricing services' fair values to other pricing services' fair values for the same investments; and (vi) periodic back-testing, which includes randomly selecting purchased or sold securities and comparing the executed prices to the fair value estimates from the pricing service. A price source hierarchy was maintained in order to determine which price source would be used (i.e., a price obtained from a pricing

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service with more seniority in the hierarchy will be used over a less senior one in all cases). The hierarchy prioritizes pricing services based on availability and reliability and assigns the highest priority to index providers. Based on the above review, the Company will challenge any prices for a security or portfolio which are considered not to be representative of fair value. The Company did not adjust any of the prices obtained from the independent pricing sources at September 30, 2015.

In certain circumstances, when fair values are unavailable from these independent pricing sources, quotes are obtained directly from broker-dealers who are active in the corresponding markets. Such quotes are subject to the validation procedures noted above. Of the \$15.36 billion of financial assets and liabilities measured at fair value at September 30, 2015, approximately \$300.7 million, or 2.0%, were priced using non-binding broker-dealer quotes. Of the \$15.06 billion of financial assets and liabilities measured at fair value at December 31, 2014, approximately \$260.8 million, or 1.7%, were priced using non-binding broker-dealer quotes.

Fixed maturities. The Company uses the market approach valuation technique to estimate the fair value of its fixed maturity securities, when possible. The market approach includes obtaining prices from independent pricing services, such as index providers and pricing vendors, as well as to a lesser extent quotes from broker-dealers. The independent pricing sources obtain market quotations and actual transaction prices for securities that have quoted prices in active markets. Each source has its own proprietary method for determining the fair value of securities that are not actively traded. In general, these methods involve the use of “matrix pricing” in which the independent pricing source uses observable market inputs including, but not limited to, investment yields, credit risks and spreads, benchmarking of like securities, broker-dealer quotes, reported trades and sector groupings to determine a reasonable fair value.

The following describes the significant inputs generally used to determine the fair value of the Company’s fixed maturity securities by asset class:

U.S. government and government agencies — valuations provided by independent pricing services, with all prices provided through index providers and pricing vendors. The Company determined that all U.S. Treasuries would be classified as Level 1 securities due to observed levels of trading activity, the high number of strongly correlated pricing quotes received on U.S. Treasuries and other factors. The fair values of U.S. government agency securities are generally determined using the spread above the risk-free yield curve. As the yields for the risk-free yield curve and the spreads for these securities are observable market inputs, the fair values of U.S. government agency securities are classified within Level 2.

- Corporate bonds — valuations provided by independent pricing services, substantially all through index providers and pricing vendors with a small amount through broker-dealers. The fair values of these securities are generally determined using the spread above the risk-free yield curve. These spreads are generally obtained from the new issue market, secondary trading and from broker-dealers who trade in the relevant security market. As the significant inputs used in the pricing process for corporate bonds are observable market inputs, the fair value of these securities are classified within Level 2.

• Mortgage-backed securities — valuations provided by independent pricing services, substantially all through pricing vendors and index providers with a small amount through broker-dealers. The fair values of these securities are generally determined through the use of pricing models (including Option Adjusted Spread) which use spreads to determine the expected average life of the securities. These spreads are generally obtained from the new issue market, secondary trading and from broker-dealers who trade in the relevant security market. The pricing services also review prepayment speeds and other indicators, when applicable. As the significant inputs used in the pricing process for mortgage-backed securities are observable market inputs, the fair value of these securities are classified within Level

2.

Municipal bonds — valuations provided by independent pricing services, with all prices provided through index providers and pricing vendors. The fair values of these securities are generally determined using spreads obtained from broker-dealers who trade in the relevant security market, trade prices and the new issue market. As the significant inputs used in the pricing process for municipal bonds are observable market inputs, the fair value of these securities are classified within Level 2.

Commercial mortgage-backed securities — valuations provided by independent pricing services, substantially all through index providers and pricing vendors with a small amount through broker-dealers. The fair values of these securities are generally determined through the use of pricing models which use spreads to determine the appropriate average life of the securities. These spreads are generally obtained from the new issue market, secondary trading and from broker-dealers

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who trade in the relevant security market. The pricing services also review prepayment speeds and other indicators, when applicable. As the significant inputs used in the pricing process for commercial mortgage-backed securities are observable market inputs, the fair value of these securities are classified within Level 2.

Non-U.S. government securities — valuations provided by independent pricing services, with all prices provided through index providers and pricing vendors. The fair values of these securities are generally based on international indices or valuation models which include daily observed yield curves, cross-currency basis index spreads and country credit spreads. As the significant inputs used in the pricing process for non-U.S. government securities are observable market inputs, the fair value of these securities are classified within Level 2.

Asset-backed securities — valuations provided by independent pricing services, substantially all through index providers and pricing vendors with a small amount through broker-dealers. The fair values of these securities generally determined through the use of pricing models (including Option Adjusted Spread) which use spreads to determine the appropriate average life of the securities. These spreads are generally obtained from the new issue market, secondary trading and from broker-dealers who trade in the relevant security market. The pricing services also review prepayment speeds and other indicators, when applicable. As the significant inputs used in the pricing process for asset-backed securities are observable market inputs, the fair value of these securities are classified within Level 2.

During the 2015 second quarter, the Company transferred \$44.6 million of U.S. government agency securities from Level 1 to Level 2 based on a review of the pricing of such securities, as described above.

Equity securities. The Company determined that exchange-traded equity securities would be included in Level 1 as their fair values are based on quoted market prices in active markets. Other equity securities are included in Level 2 of the valuation hierarchy.

Other investments. The Company determined that exchange-traded investments in mutual funds would be included in Level 1 as their fair values are based on quoted market prices in active markets. Other investments also include term loan investments for which fair values are estimated by using quoted prices of term loan investments with similar characteristics, pricing models or matrix pricing. Such investments are generally classified within Level 2. The fair values for certain of the Company's other investments are determined using net asset values as advised by external fund managers. The net asset value is based on the fund manager's valuation of the underlying holdings in accordance with the fund's governing documents. In accordance with applicable accounting guidance, certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy.

During the 2015 second quarter, the Company transferred \$99.7 million of other investments from Level 2 to Level 1 based on a review of the pricing of such securities, as described above.

Derivative instruments. The Company's futures contracts, foreign currency forward contracts, interest rate swaps and other derivatives trade in the over-the-counter derivative market. The Company uses the market approach valuation technique to estimate the fair value for these derivatives based on significant observable market inputs from third party pricing vendors, non-binding broker-dealer quotes and/or recent trading activity. As the significant inputs used in the pricing process for these derivative instruments are observable market inputs, the fair value of these securities are classified within Level 2.

Short-term investments. The Company determined that certain of its short-term investments held in highly liquid money market-type funds would be included in Level 1 as their fair values are based on quoted market prices in active

markets. The fair values of other short-term investments are generally determined using the spread above the risk-free yield curve and are classified within Level 2.

Contingent consideration liabilities. Contingent consideration liabilities (included in 'other liabilities' in the consolidated balance sheets) includes amounts related to the acquisition of CMG Mortgage Insurance Company and its affiliated mortgage insurance companies and other acquisitions. Such amounts are remeasured at fair value at each balance sheet date with changes in fair value recognized in 'net realized gains (losses).' To determine the fair value of contingent consideration liabilities, the Company estimates future payments using an income approach based on modeled inputs which include a weighted average cost of capital. The Company determined that contingent consideration liabilities would be included within Level 3.

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The following table presents the Company's financial assets and liabilities measured at fair value by level at September 30, 2015:

	Estimated Fair Value	Estimated Fair Value Measurements Using:		
		Quoted Prices in Significant Active Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets measured at fair value:				
Available for sale securities:				
Fixed maturities (1):				
Corporate bonds	\$2,796,038	\$—	\$2,796,038	\$—
Mortgage backed securities	809,876	—	809,876	—
Municipal bonds	1,830,987	—	1,830,987	—
Commercial mortgage backed securities	810,973	—	810,973	—
U.S. government and government agencies	2,338,724	2,292,409	46,315	—
Non-U.S. government securities	887,120	—	887,120	—
Asset backed securities	1,372,549	—	1,315,049	57,500
Total	10,846,267	2,292,409	8,496,358	57,500
Equity securities	606,259	605,677	582	—
Short-term investments	708,428	703,316	5,112	—
Other investments	60,526	60,526	—	—
Other investments measured at net asset value (2)	220,488	—	—	—
Total other investments	281,014	60,526	—	—
Derivative instruments (4)	16,865	—	16,865	—
Fair value option:				
Corporate bonds	767,567	—	767,567	—
Non-U.S. government bonds	76,973	—	76,973	—
Mortgage backed securities	59,435	—	59,435	—
Asset backed securities	22,499	—	22,499	—
U.S. government and government agencies	115	115	—	—
Short-term investments	153,604	153,604	—	—
Equity securities	78	78	—	—
Other investments	1,221,194	68,501	1,152,693	—
Other investments measured at net asset value (2)	481,700	—	—	—
Total	2,783,165	222,298	2,079,167	—
Total assets measured at fair value	\$15,241,998	\$3,884,226	\$10,598,084	\$57,500
Liabilities measured at fair value:				
Contingent consideration liabilities	\$(80,852)) \$—	\$—	\$(80,852)
Securities sold but not yet purchased (3)	(25,384)) —	(25,384)) —

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Derivative instruments (4)	(38,027)	—	(38,027)	—
Total liabilities measured at fair value	\$(144,263)	\$—	\$(63,411)	\$(80,852)

(1) In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See Note 6, “Investment Information—Securities Lending Agreements.”

(2) In accordance with applicable accounting guidance, certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheets.

(3) Represents the Company’s obligations to deliver securities that it did not own at the time of sale. Such amounts are included in “other liabilities” on the Company’s consolidated balance sheets.

(4) See Note 8, “Derivative Instruments.”

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The following table presents the Company's financial assets and liabilities measured at fair value by level at December 31, 2014:

	Estimated Fair Value	Estimated Fair Value Measurements Using:		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets measured at fair value:				
Available for sale securities:				
Fixed maturities (1):				
Corporate bonds	\$3,108,513	\$—	\$3,108,513	\$—
Mortgage backed securities	943,343	—	943,343	—
Municipal bonds	1,494,122	—	1,494,122	—
Commercial mortgage backed securities	1,114,528	—	1,114,528	—
U.S. government and government agencies	1,447,972	1,447,972	—	—
Non-U.S. government securities	1,015,153	—	1,015,153	—
Asset backed securities	1,677,941	—	1,620,441	57,500
Total	10,801,572	1,447,972	9,296,100	57,500
Equity securities	658,182	658,182	—	—
Short-term investments	797,226	759,621	37,605	—
Other investments	97,372	—	97,372	—
Other investments measured at net asset value (2)	198,852	—	—	—
Total other investments	296,224	—	97,372	—
Derivative instruments (3)	15,876	—	15,876	—
Fair value option:				
Corporate bonds	497,101	—	497,101	—
Non-U.S. government bonds	88,411	—	88,411	—
Mortgage backed securities	22,190	—	22,190	—
Asset backed securities	24,322	—	24,322	—
Short-term investments	251,601	250,580	1,021	—
Other investments	1,140,266	—	1,140,266	—
Other investments measured at net asset value (2)	401,162	—	—	—
Total	2,425,053	250,580	1,773,311	—
Total assets measured at fair value	\$14,994,133	\$3,116,355	\$11,220,264	\$57,500
Liabilities measured at fair value:				
Contingent consideration liabilities	\$(61,845)	) \$—	\$—	\$(61,845)
Derivative instruments (3)	(5,397)	) —	(5,397)) —
Total liabilities measured at fair value	\$(67,242)	) \$—	\$(5,397)	) \$(61,845)

(1) In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See Note 6, “Investment Information—Securities Lending Agreements.”

(2) In accordance with applicable accounting guidance, certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheets.

(3) See Note 8, “Derivative Instruments.”

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The following table presents a reconciliation of the beginning and ending balances for all financial assets and liabilities measured at fair value on a recurring basis using Level 3 inputs:

s	Assets				Fair Value Option Total	Liabilities
	Available For Sale	Asset Backed Securities	Corporate Bonds	Other Investments		Contingent Consideration Liabilities
Three Months Ended September 30, 2015						
Balance at beginning of period	\$57,500	\$—	\$—	\$—	\$57,500	\$ (71,256)
Total gains or (losses) (realized/unrealized)						
Included in earnings (1)	—	—	—	—	—	(9,596)
Included in other comprehensive income	—	—	—	—	—	—
Purchases, issuances, sales and settlements						
Purchases	—	—	—	—	—	—
Issuances	—	—	—	—	—	—
Sales	—	—	—	—	—	—
Settlements	—	—	—	—	—	—
Transfers in and/or out of Level 3	—	—	—	—	—	—
Balance at end of period	\$57,500	\$—	\$—	\$—	\$57,500	\$ (80,852)
Three Months Ended September 30, 2014						
Balance at beginning of period	\$—	\$—	\$—	\$—	\$—	\$ (53,099)
Total gains or (losses) (realized/unrealized)						
Included in earnings (1)	—	—	—	—	—	(5,562)
Included in other comprehensive income	—	—	—	—	—	—
Purchases, issuances, sales and settlements						
Purchases	—	—	—	—	—	—
Issuances	—	—	—	—	—	—
Sales	—	—	—	—	—	—
Settlements	—	—	—	—	—	—
Transfers in and/or out of Level 3	—	—	—	—	—	—
Balance at end of period	\$—	\$—	\$—	\$—	\$—	\$ (58,661)
Nine Months Ended September 30, 2015						
Balance at beginning of period	\$57,500	\$—	\$—	\$—	\$57,500	\$ (61,845)
Total gains or (losses) (realized/unrealized)						
Included in earnings (1)	—	—	—	—	—	(17,939)

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Included in other comprehensive income	—	—	—	—	—	—
Purchases, issuances, sales and settlements						
Purchases	—	—	—	—	—	—
Issuances	—	—	—	—	—	(1,068)
Sales	—	—	—	—	—	—
Settlements	—	—	—	—	—	—
Transfers in and/or out of Level 3	—	—	—	—	—	—
Balance at end of period	\$57,500	\$—	\$—	\$—	\$57,500	\$(80,852)
Nine Months Ended September 30, 2014						
Balance at beginning of period	\$—	\$2,045	\$170,420	\$377,525	\$549,990	\$—
Total gains or (losses) (realized/unrealized)						
Included in earnings (1)	—	—	—	—	—	(16,899)
Included in other comprehensive income	—	—	—	—	—	—
Purchases, issuances, sales and settlements						
Purchases	—	—	—	—	—	—
Issuances	—	—	—	—	—	(41,762)
Sales	—	(2,045)	—	—	(2,045)	—
Settlements	—	—	—	—	—	—
Transfers in and/or out of Level 3 (2)	—	—	(170,420)	(377,525)	(547,945)	—
Balance at end of period	\$—	\$—	\$—	\$—	\$—	\$(58,661)

Gains or losses on fixed maturities available for sale were included in net realized gains (losses) while gains or (1) losses on other investments were included in net realized gains (losses) or net investment income. Gains or losses on contingent consideration liabilities were included in net realized gains (losses).

In accordance with applicable accounting guidance, certain investments that are measured at fair value using the (2) net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The transfers out of Level 3 presented in this table are intended to permit reconciliation to information previously presented.

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Financial Instruments Disclosed, But Not Carried, At Fair Value

The Company uses various financial instruments in the normal course of its business. The carrying values of cash, accrued investment income, receivable for securities sold, certain other assets, payable for securities purchased and certain other liabilities approximated their fair values at September 30, 2015, due to their respective short maturities. As these financial instruments are not actively traded, their respective fair values are classified within Level 2.

At September 30, 2015, the senior notes of ACGL were carried at their cost, net of debt issuance costs, of \$296.9 million and had a fair value of \$387.6 million while the senior notes of Arch-U.S. were carried at their cost, net of debt issuance costs, of \$494.4 million and had a fair value of \$543.7 million. The fair values of the senior notes were obtained from a third party pricing service and are based on observable market inputs. As such, the fair value of the senior notes is classified within Level 2.

8. Derivative Instruments

The Company's investment strategy allows for the use of derivative securities. The Company's derivative instruments are recorded on its consolidated balance sheets at fair value. The Company utilizes exchange traded U.S. Treasury note, Eurodollar and other futures contracts and commodity futures to manage portfolio duration or replicate investment positions in its portfolios and the Company routinely utilizes foreign currency forward contracts, currency options, index futures contracts and other derivatives as part of its total return objective. In addition, certain of the Company's investments are managed in portfolios which incorporate the use of foreign currency forward contracts which are intended to provide an economic hedge against foreign currency movements.

In addition, the Company purchases to-be-announced mortgage backed securities ("TBAs") as part of its investment strategy. TBAs represent commitments to purchase a future issuance of agency mortgage backed securities. For the period between purchase of a TBA and issuance of the underlying security, the Company's position is accounted for as a derivative. The Company purchases TBAs in both long and short positions to enhance investment performance and as part of its overall investment strategy.

The Company did not hold any derivatives which were designated as hedging instruments at September 30, 2015 or December 31, 2014. The following table summarizes information on the fair values and notional values of the Company's derivative instruments.

	Estimated Fair Value			
	Asset Derivatives	Liability Derivatives	Net Derivatives	Notional Value (1)
September 30, 2015				
Futures contracts (2)	\$189	\$(3,528)	) \$(3,339	) \$1,702,327
Foreign currency forward contracts (2)	10,678	(7,235)	) 3,443	1,018,620
TBAs (3)	307,356	(290,865)	) 16,491	568,463
Other (2)	5,998	(27,264)	) (21,266)	) 1,446,622
Total	\$324,221	\$(328,892)	) \$(4,671))
December 31, 2014				
Futures contracts (2)	\$2,156	\$(1,907)	) \$249	\$2,549,027
Foreign currency forward contracts (2)	10,511	(1,145)	) 9,366	397,106
TBAs (3)	10,592	—) 10,592	10,056
Other (2)	3,209	(2,345)) 864	735,684

Total \$26,468 \$(5,397) \$21,071

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- (1) Represents the absolute notional value of all outstanding contracts, consisting of long and short positions.
(2) The fair value of asset derivatives are included in 'other assets' and the fair value of liability derivatives are included in 'other liabilities.'
(3) The fair value of TBAs are included in 'fixed maturities available for sale, at fair value.'

The Company's derivative instruments can be traded under master netting agreements, which establish terms that apply to all derivative transactions with a counterparty. In the event of a bankruptcy or other stipulated event of default, such agreements provide that the non-defaulting party may elect to terminate all outstanding derivative transactions, in which case all individual derivative positions (loss or gain) with a counterparty are closed out and netted and replaced with a single amount, usually

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referred to as the termination amount, which is expressed in a single currency. The resulting single net amount, where positive, is payable to the party “in-the-money” regardless of whether or not it is the defaulting party, unless the parties have agreed that only the non-defaulting party is entitled to receive a termination payment where the net amount is positive and is in its favor. Effectively, contractual close-out netting reduces derivatives credit exposure from gross to net exposure. At September 30, 2015, asset derivatives and liability derivatives of \$298.4 million and \$309.6 million, respectively, were subject to a master netting agreement, compared to \$25.3 million and \$5.4 million, respectively, at December 31, 2014. The remaining derivatives included in the table above were not subject to a master netting agreement.

All realized and unrealized contract gains and losses on the Company’s derivative instruments are reflected in net realized gains (losses) in the consolidated statements of income, as summarized in the following table:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
Derivatives not designated as hedging instruments:	2015	2014	2015	2014
Net realized gains (losses):				
Futures contracts	\$28,562	\$(354)	\$16,442	\$4,969
Foreign currency forward contracts	5,395	6,558	13,490	2,490
TBAs	1,064	660	1,368	353
Other	868	585	(231)	(729)
Total	\$35,889	\$7,449	\$31,069	\$7,083

9. Commitments and Contingencies

Letter of Credit and Revolving Credit Facilities

As of September 30, 2015, the Company had a \$300 million unsecured revolving loan and letter of credit facility and a \$500 million secured letter of credit facility (the “Credit Agreement”). The Credit Agreement expires on June 30, 2019. In addition, the Company had access to secured letter of credit facilities of approximately \$228.6 million as of September 30, 2015, which are available on a limited basis and for limited purposes (together with the secured portion of the Credit Agreement and these letter of credit facilities, the “LOC Facilities”). At September 30, 2015, the Company had \$451.8 million in outstanding letters of credit under the LOC Facilities, which were secured by investments with a fair value of \$517.4 million, and had \$100.0 million of borrowings outstanding under the Credit Agreement. The Company was in compliance with all covenants contained in the LOC Facilities at September 30, 2015.

As of September 30, 2015, Watford Re had a \$100 million letter of credit facility expiring on May 19, 2016 and an \$800 million secured credit facility expiring on June 4, 2018, that provides for borrowings and the issuance of letters of credit not to exceed \$400 million. At September 30, 2015, Watford Re had \$102.8 million in outstanding letters of credit under the two facilities and \$239.1 million of borrowings outstanding under the secured credit facility, backed by Watford Re’s investment portfolio. Watford Re was in compliance with all covenants contained in both of its credit facilities at September 30, 2015. The Company does not guarantee or provide credit support for Watford Re, and the Company’s financial exposure to Watford Re is limited to its investment in Watford Re’s common and preferred shares and counterparty credit risk (mitigated by collateral) arising from the reinsurance transactions.

Investment Commitments

The Company’s investment commitments, which are primarily related to agreements entered into by the Company to invest in funds and separately managed accounts when called upon, were approximately \$1.23 billion at September

30, 2015, compared to \$968.9 million at December 31, 2014.

10. Share Transactions

Share Repurchases

The board of directors of ACGL has authorized the investment in ACGL's common shares through a share repurchase program. Since the inception of the share repurchase program, ACGL has repurchased approximately 124.1 million common shares for an aggregate purchase price of \$3.61 billion. During the nine months ended September 30, 2015, ACGL repurchased 5.9 million common shares for an aggregate purchase price of \$365.4 million, compared to 4.6 million common shares

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repurchased for an aggregate purchase price of \$251.9 million during the 2014 period. At September 30, 2015, \$521.8 million of share repurchases were available under the program. The timing and amount of the repurchase transactions under this program will depend on a variety of factors, including market conditions and corporate and regulatory considerations.

11. Income Taxes

ACGL is incorporated under the laws of Bermuda and, under current Bermuda law, is not obligated to pay any taxes in Bermuda based upon income or capital gains. The Company has received a written undertaking from the Minister of Finance in Bermuda under the Exempted Undertakings Tax Protection Act 1966 that, in the event that any legislation is enacted in Bermuda imposing any tax computed on profits, income, gain or appreciation on any capital asset, or any tax in the nature of estate duty or inheritance tax, such tax will not be applicable to ACGL or any of its operations until March 31, 2035. This undertaking does not, however, prevent the imposition of taxes on any person ordinarily resident in Bermuda or any company in respect of its ownership of real property or leasehold interests in Bermuda.

ACGL and its non-U.S. subsidiaries will be subject to U.S. federal income tax only to the extent that they derive U.S. source income that is subject to U.S. withholding tax or income that is effectively connected with the conduct of a trade or business within the U.S. and is not exempt from U.S. tax under an applicable income tax treaty with the U.S. ACGL and its non-U.S. subsidiaries will be subject to a withholding tax on dividends from U.S. investments and interest from certain U.S. payors (subject to reduction by any applicable income tax treaty). ACGL and its non-U.S. subsidiaries intend to conduct their operations in a manner that will not cause them to be treated as engaged in a trade or business in the United States and, therefore, will not be required to pay U.S. federal income taxes (other than U.S. excise taxes on insurance and reinsurance premium and withholding taxes on dividends and certain other U.S. source investment income). However, because there is uncertainty as to the activities which constitute being engaged in a trade or business within the United States, there can be no assurances that the U.S. Internal Revenue Service will not contend successfully that ACGL or its non-U.S. subsidiaries are engaged in a trade or business in the United States. If ACGL or any of its non-U.S. subsidiaries were subject to U.S. income tax, ACGL's shareholders' equity and earnings could be materially adversely affected. ACGL has subsidiaries and branches that operate in various jurisdictions around the world that are subject to tax in the jurisdictions in which they operate. The significant jurisdictions in which ACGL's subsidiaries and branches are subject to tax are the United States, United Kingdom, Ireland, Canada, Switzerland and Denmark.

The Company's income tax provision on income before income taxes resulted in an expense of 5.5% for the nine months ended September 30, 2015, compared to an expense of 2.8% for the 2014 period. The Company's effective tax rate, which is based upon the expected annual effective tax rate, may fluctuate from period to period based on the relative mix of income or loss reported by jurisdiction and the varying tax rates in each jurisdiction. The Company had a net deferred tax asset of \$139.9 million at September 30, 2015, compared to \$131.0 million at December 31, 2014. In addition, the Company paid \$35.5 million in income taxes for the nine months ended September 30, 2015, while the Company paid \$13.3 million for the 2014 period.

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12. Other Comprehensive Income (Loss)

The following tables present details about amounts reclassified from accumulated other comprehensive income and the tax effects allocated to each component of other comprehensive income (loss):

Details About AOCI Components	Consolidated Statement of Income Line Item That Includes Reclassification	Amounts Reclassified from AOCI			
		Three Months Ended September 30,		Nine Months Ended September 30,	
		2015	2014	2015	2014
Unrealized appreciation on available-for-sale investments					
	Net realized gains (losses)	\$ (2,019)	\$ 27,715	\$ 63,671	\$ 77,488
	Other-than-temporary impairment losses	(8,901)	(8,593)	(17,274)	(26,313)
	Total before tax	(10,920)	19,122	46,397	51,175
	Income tax (expense) benefit	(1,358)	(1,639)	(6,529)	(4,158)
	Net of tax	\$ (12,278)	\$ 17,483	\$ 39,868	\$ 47,017
			Before Tax Amount	Tax Expense (Benefit)	Net of Tax Amount
Three Months Ended September 30, 2015					
Unrealized appreciation (decline) in value of investments:					
	Unrealized holding gains (losses) arising during period		\$ (44,687)	\$ 9,204	\$ (53,891)
	Portion of other-than-temporary impairment losses recognized in other comprehensive income (loss)		(3,033)	—	(3,033)
	Less reclassification of net realized gains (losses) included in net income		(10,920)	1,358	(12,278)
	Foreign currency translation adjustments		(12,638)	(556)	(12,082)
	Other comprehensive income (loss)		\$ (49,438)	\$ 7,290	\$ (56,728)
Three Months Ended September 30, 2014					
Unrealized appreciation (decline) in value of investments:					
	Unrealized holding gains (losses) arising during period		\$ (90,276)	\$ 343	\$ (90,619)
	Portion of other-than-temporary impairment losses recognized in other comprehensive income (loss)		—	—	—
	Less reclassification of net realized gains (losses) included in net income		19,122	1,639	17,483
	Foreign currency translation adjustments		(23,595)	—	(23,595)
	Other comprehensive income (loss)		\$ (132,993)	\$ (1,296)	\$ (131,697)
Nine Months Ended September 30, 2015					
Unrealized appreciation (decline) in value of investments:					
	Unrealized holding gains (losses) arising during period		\$ (46,929)	\$ 4,593	\$ (51,522)
	Portion of other-than-temporary impairment losses recognized in other comprehensive income (loss)		(4,494)	—	(4,494)
	Less reclassification of net realized gains (losses) included in net income		46,397	6,529	39,868
	Foreign currency translation adjustments		(24,567)	(1,308)	(23,259)
	Other comprehensive income (loss)		\$ (122,387)	\$ (3,244)	\$ (119,143)
Nine Months Ended September 30, 2014					
Unrealized appreciation (decline) in value of investments:					

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Unrealized holding gains (losses) arising during period	\$ 100,274	\$ 11,112	\$ 89,162
Portion of other-than-temporary impairment losses recognized in other comprehensive income (loss)	—	—	—
Less reclassification of net realized gains (losses) included in net income	51,175	4,158	47,017
Foreign currency translation adjustments	(14,923)	—	(14,923)
Other comprehensive income (loss)	\$ 34,176	\$ 6,954	\$ 27,222

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

13. Guarantor Financial Information

The following tables present condensed financial information for ACGL, Arch Capital Group (U.S.) Inc. (“Arch-U.S.”), a 100% owned subsidiary of ACGL, and ACGL’s other subsidiaries.

September 30, 2015

Condensed Consolidating Balance Sheet	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Assets					
Total investments	\$34	\$55,053	\$15,775,050	\$(14,700)	\$15,815,437
Cash	10,381	9,256	630,142	—	649,779
Investments in subsidiaries	6,579,718	1,715,121	—	(8,294,839)	—
Due from subsidiaries and affiliates	—	48,548	442,508	(491,056)	—
Premiums receivable	—	—	1,521,960	(447,076)	1,074,884
Reinsurance recoverable on unpaid and paid losses and loss adjustment expenses	—	—	5,739,246	(3,906,860)	1,832,386
Contractholder receivables	—	—	1,436,154	—	1,436,154
Prepaid reinsurance premiums	—	—	1,602,870	(1,160,524)	442,346
Deferred acquisition costs, net	—	—	448,893	—	448,893
Other assets	3,534	43,860	2,644,143	(620,824)	2,070,713
Total assets	\$6,593,667	\$1,871,838	\$30,240,966	\$(14,935,879)	\$23,770,592
Liabilities					
Reserve for losses and loss adjustment expenses	\$—	\$—	\$12,969,850	\$(3,884,995)	\$9,084,855
Unearned premiums	—	—	3,628,215	(1,160,524)	2,467,691
Reinsurance balances payable	—	—	669,285	(433,723)	235,562
Contractholder payables	—	—	1,436,154	—	1,436,154
Collateral held for insured obligations	—	—	242,928	—	242,928
Deposit accounting liabilities	—	—	482,756	(211,880)	270,876
Senior notes	296,854	494,410	—	—	791,264
Revolving credit agreement borrowings	100,000	—	239,077	—	339,077
Due to subsidiaries and affiliates	14,080	35,000	441,976	(491,056)	—
Other liabilities	19,918	49,904	2,134,460	(444,163)	1,760,119
Total liabilities	430,852	579,314	22,244,701	(6,626,341)	16,628,526
Redeemable noncontrolling interests	—	—	219,789	(14,700)	205,089
Shareholders’ Equity					
Total shareholders’ equity available to Arch	6,162,815	1,292,524	7,002,314	(8,294,838)	6,162,815
Non-redeemable noncontrolling interests	—	—	774,162	—	774,162
Total shareholders’ equity	6,162,815	1,292,524	7,776,476	(8,294,838)	6,936,977
Total liabilities, noncontrolling interests and shareholders’ equity	\$6,593,667	\$1,871,838	\$30,240,966	\$(14,935,879)	\$23,770,592

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

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Condensed Consolidating Balance Sheet	December 31, 2014				
	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Assets					
Total investments	\$ 107	\$ 62,867	\$ 15,257,796	\$—	\$ 15,320,770
Cash	3,218	2,787	479,697	—	485,702
Investments in subsidiaries	6,536,644	1,685,185	—	(8,221,829)	—
Due from subsidiaries and affiliates	48	7,517	370,429	(377,994)	—
Premiums receivable	—	—	1,331,511	(382,816)	948,695
Reinsurance recoverable on unpaid and paid losses and loss adjustment expenses	—	—	5,584,973	(3,772,128)	1,812,845
Contractholder receivables	—	—	1,309,192	—	1,309,192
Prepaid reinsurance premiums	—	—	1,373,008	(995,930)	377,078
Deferred acquisition costs, net	—	—	414,525	—	414,525
Other assets	4,386	43,921	1,705,546	(416,579)	1,337,274
Total assets	\$ 6,544,403	\$ 1,802,277	\$ 27,826,677	\$ (14,167,276)	\$ 22,006,081
Liabilities					
Reserve for losses and loss adjustment expenses	\$—	\$—	\$ 12,784,030	\$(3,747,582)	\$ 9,036,448
Unearned premiums	—	—	3,227,508	(995,930)	2,231,578
Reinsurance balances payable	—	—	589,289	(369,977)	219,312
Contractholder payables	—	—	1,309,192	—	1,309,192
Collateral held for insured obligations	—	—	184,219	—	184,219
Deposit accounting liabilities	—	—	587,050	(259,666)	327,384
Senior notes	296,796	494,345	—	—	791,141
Revolving credit agreement borrowings	100,000	—	—	—	100,000
Due to subsidiaries and affiliates	417	7,505	370,072	(377,994)	—
Other liabilities	17,137	49,403	815,919	(194,298)	688,161
Total liabilities	414,350	551,253	19,867,279	(5,945,447)	14,887,435
Redeemable noncontrolling interests	—	—	219,512	—	219,512
Shareholders' Equity					
Total shareholders' equity available to Arch	6,130,053	1,251,024	6,970,805	(8,221,829)	6,130,053
Non-redeemable noncontrolling interests	—	—	769,081	—	769,081
Total shareholders' equity	6,130,053	1,251,024	7,739,886	(8,221,829)	6,899,134
Total liabilities, noncontrolling interests and shareholders' equity	\$ 6,544,403	\$ 1,802,277	\$ 27,826,677	\$ (14,167,276)	\$ 22,006,081

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

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Condensed Consolidating Statement of Income and Comprehensive Income	Three Months Ended September 30, 2015				
	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Revenues					
Net premiums earned	\$—	\$—	\$936,683	\$—	\$936,683
Net investment income	—	764	92,773	(7,304)	86,233
Net realized gains (losses)	—	—	(89,698)	—	(89,698)
Net impairment losses recognized in earnings	—	—	(5,868)	—	(5,868)
Other underwriting income	—	—	7,623	—	7,623
Equity in net income (loss) of investment funds accounted for using the equity method	—	—	(2,118)	—	(2,118)
Other income (loss)	—	—	(265)	—	(265)
Total revenues	—	764	939,130	(7,304)	932,590
Expenses					
Losses and loss adjustment expenses	—	—	531,741	—	531,741
Acquisition expenses	—	—	171,566	—	171,566
Other operating expenses	10,536	720	145,703	—	156,959
Interest expense	5,863	6,689	7,734	(6,986)	13,300
Net foreign exchange (gains) losses	—	—	(11,762)	(2,918)	(14,680)
Total expenses	16,399	7,409	844,982	(9,904)	858,886
Income (loss) before income taxes	(16,399)	(6,645)	94,148	2,600	73,704
Income tax (expense) benefit	—	2,324	(12,028)	—	(9,704)
Income (loss) before equity in net income of subsidiaries	(16,399)	(4,321)	82,120	2,600	64,000
Equity in net income of subsidiaries	96,432	13,620	—	(110,052)	—
Net income	80,033	9,299	82,120	(107,452)	64,000
Amounts attributable to noncontrolling interests	—	—	15,712	321	16,033
Net income available to Arch	80,033	9,299	97,832	(107,131)	80,033
Preferred dividends	(5,484)	—	—	—	(5,484)
Net income available to Arch common shareholders	\$74,549	\$9,299	\$97,832	\$(107,131)	\$74,549
Comprehensive income (loss) available to Arch	\$23,401	\$15,705	\$44,127	\$(59,832)	\$23,401

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Condensed Consolidating Statement of Income and Comprehensive Income	Three Months Ended September 30, 2014				
	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Revenues					
Net premiums earned	\$—	\$—	\$903,651	\$—	\$903,651
Net investment income	—	—	79,936	169	80,105
Net realized gains (losses)	—	—	18,515	—	18,515
Net impairment losses recognized in earnings	—	—	(8,593)	) —	(8,593)
Other underwriting income	—	—	1,702	—	1,702
Equity in net income (loss) of investment funds accounted for using the equity method	—	—	4,966	—	4,966
Other income (loss)	—	—	(7,815)	) —	(7,815)
Total revenues	—	—	992,362	169	992,531
Expenses					
Losses and loss adjustment expenses	—	—	501,673	—	501,673
Acquisition expenses	—	—	163,547	—	163,547
Other operating expenses	10,056	810	138,614	—	149,480
Interest expense	5,858	6,433	(8,308)	) 169	4,152
Net foreign exchange (gains) losses	—	—	(35,244)	) (20,787)	(56,031)
Total expenses	15,914	7,243	760,282	(20,618)	762,821
Income (loss) before income taxes	(15,914)	) (7,243)	) 232,080	20,787	229,710
Income tax (expense) benefit	—	2,097	(8,543)	) —	(6,446)
Income (loss) before equity in net income of subsidiaries	(15,914)	) (5,146)	) 223,537	20,787	223,264
Equity in net income of subsidiaries	244,589	10,459	—	(255,048)) —
Net income	228,675	5,313	223,537	(234,261)	) 223,264
Amounts attributable to noncontrolling interests	—	—	5,411	—	5,411
Net income available to Arch	228,675	5,313	228,948	(234,261)	) 228,675
Preferred dividends	(5,484)	) —	—	—	(5,484)
Net income available to Arch common shareholders	\$223,191	\$5,313	\$228,948	\$ (234,261)	) \$223,191
Comprehensive income (loss) available to Arch	\$96,978	\$(10,614)) \$104,501	\$ (93,887)) \$96,978

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Condensed Consolidating Statement of Income and Comprehensive Income	Nine Months Ended September 30, 2015				
	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Revenues					
Net premiums earned	\$—	\$—	\$2,790,385	\$—	\$2,790,385
Net investment income	—	1,569	265,937	(15,316)	252,190
Net realized gains (losses)	—	1	(42,076)	—	(42,075)
Net impairment losses recognized in earnings	—	—	(12,780)	—	(12,780)
Other underwriting income	—	—	26,876	—	26,876
Equity in net income (loss) of investment funds accounted for using the equity method	—	—	19,938	—	19,938
Other income (loss)	—	—	52	—	52
Total revenues	—	1,570	3,048,332	(15,316)	3,034,586
Expenses					
Losses and loss adjustment expenses	—	—	1,544,883	—	1,544,883
Acquisition expenses	—	—	510,067	—	510,067
Other operating expenses	36,068	2,991	444,390	—	483,449
Interest expense	17,581	19,824	7,476	(14,834)	30,047
Net foreign exchange (gains) losses	—	—	(44,450)	(17,148)	(61,598)
Total expenses	53,649	22,815	2,462,366	(31,982)	2,506,848
Income (loss) before income taxes	(53,649)	(21,245)	585,966	16,666	527,738
Income tax (expense) benefit	—	7,434	(36,596)	—	(29,162)
Income (loss) before equity in net income of subsidiaries	(53,649)	(13,811)	549,370	16,666	498,576
Equity in net income of subsidiaries	532,808	42,192	—	(575,000)	—
Net income	479,159	28,381	549,370	(558,334)	498,576
Amounts attributable to noncontrolling interests	—	—	(19,902)	485	(19,417)
Net income available to Arch	479,159	28,381	529,468	(557,849)	479,159
Preferred dividends	(16,453)	—	—	—	(16,453)
Net income available to Arch common shareholders	\$462,706	\$28,381	\$529,468	\$(557,849)	\$462,706
Comprehensive income (loss) available to Arch	\$360,112	\$13,950	\$427,569	\$(441,519)	\$360,112

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Condensed Consolidating Statement of Income and Comprehensive Income	Nine Months Ended September 30, 2014				
	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Revenues					
Net premiums earned	\$—	\$—	\$2,670,583	\$—	\$2,670,583
Net investment income	—	—	237,317	(17,228)	220,089
Net realized gains (losses)	—	—	92,356	—	92,356
Net impairment losses recognized in earnings	—	—	(26,313)	—	(26,313)
Other underwriting income	—	—	5,317	—	5,317
Equity in net income (loss) of investment funds accounted for using the equity method	—	—	17,459	—	17,459
Other income (loss)	—	—	(5,069)	—	(5,069)
Total revenues	—	—	2,991,650	(17,228)	2,974,422
Expenses					
Losses and loss adjustment expenses	—	—	1,423,431	—	1,423,431
Acquisition expenses	—	—	482,047	—	482,047
Other operating expenses	35,613	2,281	413,735	—	451,629
Interest expense	17,565	19,395	13,158	(17,228)	32,890
Net foreign exchange (gains) losses	—	—	(28,449)	(18,725)	(47,174)
Total expenses	53,178	21,676	2,303,922	(35,953)	2,342,823
Income (loss) before income taxes	(53,178)	(21,676)	687,728	18,725	631,599
Income tax (expense) benefit	—	8,179	(25,652)	—	(17,473)
Income (loss) before equity in net income of subsidiaries	(53,178)	(13,497)	662,076	18,725	614,126
Equity in net income of subsidiaries	672,369	41,945	—	(714,314)	—
Net income	619,191	28,448	662,076	(695,589)	614,126
Amounts attributable to noncontrolling interests	—	—	5,065	—	5,065
Net income available to Arch	619,191	28,448	667,141	(695,589)	619,191
Preferred dividends	(16,453)	—	—	—	(16,453)
Net income available to Arch common shareholders	\$602,738	\$28,448	\$667,141	\$(695,589)	\$602,738
Comprehensive income (loss) available to Arch	\$646,413	\$29,792	\$691,968	\$(721,760)	\$646,413

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Condensed Consolidating Statement of Cash Flows	Nine Months Ended September 30, 2015				
	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Operating Activities					
Net Cash Provided By (Used For) Operating Activities	\$ 382,329	\$ 10,622	\$ 859,525	\$(444,897)	\$ 807,579
Investing Activities					
Purchases of fixed maturity investments	—	(3,505)	(22,378,599)	—	(22,382,104)
Purchases of equity securities	(8,070)	—	(477,456)	—	(485,526)
Purchases of other investments	—	—	(1,320,250)	—	(1,320,250)
Proceeds from the sales of fixed maturity investments	—	23,507	21,388,047	—	21,411,554
Proceeds from the sales of equity securities	—	—	509,008	—	509,008
Proceeds from the sales, redemptions and maturities of other investments	—	—	858,368	—	858,368
Proceeds from redemptions and maturities of fixed maturity investments	—	—	630,397	—	630,397
Net settlements of derivative instruments	—	—	81,114	—	81,114
Proceeds from investment in joint venture	—	—	40,000	—	40,000
Net (purchases) sales of short-term investments	73	(12,183)	193,851	—	181,741
Change in cash collateral related to securities lending	—	—	28,685	—	28,685
Contributions to subsidiaries	—	—	(9,290)	9,290	—
Intercompany loans issued	—	(39,500)	(41,523)	81,023	—
Purchase of business, net of cash acquired	—	—	818	—	818
Purchases of fixed assets	(53)	—	(10,848)	—	(10,901)
Change in other assets	—	—	(43,654)	—	(43,654)
Net Cash Provided By (Used For) Investing Activities	(8,050)	(31,681)	(551,332)	90,313	(500,750)
Financing Activities					
Purchases of common shares under share repurchase program	(365,383)	—	—	—	(365,383)
Proceeds from common shares issued, net	697	—	9,290	(9,290)	697
Proceeds from intercompany borrowings	14,023	27,500	39,500	(81,023)	—
Proceeds from borrowings	—	—	239,077	—	239,077
Change in cash collateral related to securities lending	—	—	(28,685)	—	(28,685)
Dividends paid to redeemable noncontrolling interests	—	—	(14,447)	637	(13,810)
Dividends paid to parent	—	—	(444,260)	444,260	—
Other	—	28	50,435	—	50,463

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Preferred dividends paid	(16,453) —	—	—	(16,453)
Net Cash Provided By (Used For) Financing Activities	(367,116) 27,528	(149,090) 354,584	(134,094)
Effects of exchange rates changes on foreign currency cash	—	—	(8,658	) —	(8,658)
Increase (decrease) in cash	7,163	6,469	150,445	—	164,077	
Cash beginning of year	3,218	2,787	479,697	—	485,702	
Cash end of period	\$10,381	\$9,256	\$630,142	\$—	\$649,779	

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Condensed Consolidating Statement of Cash Flows	Nine Months Ended September 30, 2014				
	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Operating Activities					
Net Cash Provided By (Used For) Operating Activities	\$265,694	\$8,407	\$822,558	\$(297,000)	\$799,659
Investing Activities					
Purchases of fixed maturity investments	—	(78,509)	(21,952,353)	—	(22,030,862)
Purchases of equity securities	—	—	(366,578)	—	(366,578)
Purchases of other investments	—	—	(1,136,285)	—	(1,136,285)
Proceeds from the sales of fixed maturity investments	—	—	20,273,351	—	20,273,351
Proceeds from the sales of equity securities	—	—	305,034	—	305,034
Proceeds from the sales, redemptions and maturities of other investments	—	—	566,518	—	566,518
Proceeds from redemptions and maturities of fixed maturity investments	—	—	636,729	—	636,729
Net settlements of derivative instruments	—	—	15,495	—	15,495
Net (purchases) sales of short-term investments	2,396	408,760	267,232	—	678,388
Change in cash collateral related to securities lending	—	—	(2,737)	—	(2,737)
Contributions to subsidiaries	—	(313,207)	(100,000)	413,207	—
Intercompany loans issued	—	—	10,250	(10,250)	—
Purchase of business, net of cash acquired	—	—	(235,578)	—	(235,578)
Purchases of fixed assets	(220)	—	(14,355)	—	(14,575)
Change in other assets	—	—	—	—	—
Net Cash Provided By (Used For) Investing Activities	2,176	17,044	(1,733,277)	402,957	(1,311,100)
Financing Activities					
Purchases of common shares under share repurchase program	(251,919)	—	—	—	(251,919)
Proceeds from common shares issued, net	3,248	—	413,207	(413,207)	3,248
Repayments of intercompany borrowings	—	(10,250)	—	10,250	—
Change in cash collateral related to securities lending	—	—	2,737	—	2,737
Third party investment in non-redeemable noncontrolling interests	—	—	796,903	—	796,903
Third party investment in redeemable noncontrolling interests	—	—	219,233	—	219,233
Dividends paid to redeemable noncontrolling interests	—	—	(9,632)	—	(9,632)

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Dividends paid to parent	—	—	(297,000) 297,000	—
Other	—	—	6,559	—	6,559
Preferred dividends paid	(16,453) —	—	—	(16,453
Net Cash Provided By (Used For)	(265,124	) (10,250	) 1,132,007	(105,957	) 750,676
Financing Activities					
Effects of exchange rates changes on foreign currency cash	—	—	(9,566	) —	(9,566
Increase (decrease) in cash	2,746	15,201	211,722	—	229,669
Cash beginning of year	3,223	509	430,325	—	434,057
Cash end of period	\$5,969	\$15,710	\$642,047	\$—	\$663,726

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

14. Legal Proceedings

The Company, in common with the insurance industry in general, is subject to litigation and arbitration in the normal course of its business. As of September 30, 2015, the Company was not a party to any litigation or arbitration which is expected by management to have a material adverse effect on the Company's results of operations and financial condition and liquidity.

15. Transactions with Related Parties

Kewsong Lee, a director of ACGL, is a Managing Director and Deputy Chief Investment Officer for Corporate Private Equity of The Carlyle Group ("Carlyle"). As part of its investment philosophy, the Company invests a portion of its investment portfolio in alternative investment funds. As of September 30, 2015, the Company had aggregate commitments of \$670.9 million to funds managed by Carlyle, of which \$462.4 million was unfunded. The Company may make additional commitments to funds managed by Carlyle from time to time. During the nine months ended September 30, 2015 and 2014, the Company made aggregate capital contributions to funds managed by Carlyle of \$97.7 million and \$55.5 million, respectively. During the nine months ended September 30, 2015 and 2014, the Company received aggregate cash distributions from funds managed by Carlyle of \$30.3 million and \$41.0 million, respectively, of which \$25.5 million and \$32.8 million, respectively, represented a return of capital.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following is a discussion and analysis of our financial condition and results of operations. This should be read in conjunction with our consolidated financial statements included in Item 1 of this report and also our Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the year ended December 31, 2014 ("2014 Form 10-K"). In addition, readers should review "Risk Factors" set forth in Item 1A of Part I of our 2014 Form 10-K. Tabular amounts are in U.S. Dollars in thousands, except share amounts, unless otherwise noted.

Arch Capital Group Ltd. ("ACGL" and, together with its subsidiaries, "we" or "us") is a Bermuda public limited liability company with approximately \$7.05 billion in capital at September 30, 2015 and, through operations in Bermuda, the United States, Europe and Canada, writes specialty lines of property and casualty insurance and reinsurance, as well as mortgage insurance and reinsurance, on a worldwide basis.

Current Outlook

The broad market environment continues to be competitive in our business reflecting a continuation of softening in pricing and broadening pressures on terms and conditions. This has been true in both our insurance and reinsurance property casualty segments and has led us to continue to reduce writings in certain lines in the 2015 third quarter. With the continued low interest rate environment, additional increases are needed in many lines in order for us to achieve our return requirements. Our underwriting teams continue to execute a disciplined strategy by emphasizing small and medium-sized accounts over large accounts.

Arch Mortgage Insurance Company ("Arch MI U.S.") continues to expand into the U.S. mortgage insurance marketplace. As of September 30, 2015, Arch MI U.S. reviewed and approved 835 master policy applications from banks, with 45 national accounts and the balance consisting of regional banks. In addition, Arch MI U.S. recently announced RateStar, a new risk-based pricing program expected to be implemented in the 2015 fourth quarter. RateStar uses a combination of loan characteristics and other risk factors to determine premium rates for each loan.

Our objective is to achieve an average operating return on average equity of 15% or greater over the insurance cycle, which we believe to be an attractive return to our common shareholders given the risks we assume. We continue to look for opportunities to find acceptable books of business to underwrite without sacrificing underwriting discipline and continue to write a portion of our overall book in catastrophe-exposed business which has the potential to increase the volatility of our operating results.

Changing economic conditions could have a material impact on the frequency and severity of claims and, therefore, could negatively impact our underwriting returns. In addition, volatility in the financial markets could continue to significantly affect our investment returns, reported results and shareholders' equity. We consider the potential impact of economic trends in the estimation process for establishing unpaid losses and loss adjustment expenses and in determining our investment strategies. In addition, weakness of the U.S., European countries and other key economies, projected budget deficits for the U.S., European countries and other governments and the consequences associated with potential downgrades of securities of the U.S., European countries and other governments by credit rating agencies is inherently unpredictable and could have a material adverse effect on financial markets and economic conditions in the U.S. and throughout the world. In turn, this could have a material adverse effect on our business, financial condition and results of operations and, in particular, this could have a material adverse effect on the value and liquidity of securities in our investment portfolio.

Natural Catastrophe Risk

We monitor our natural catastrophe risk globally for all perils and regions, in each case, where we believe there is significant exposure. Our models employ both proprietary and vendor-based systems and include cross-line correlations for property, marine, offshore energy, aviation, workers compensation and personal accident. Currently, we seek to limit our 1-in-250 year return period net probable maximum pre-tax loss from a severe catastrophic event in any geographic zone to approximately 25% of total shareholders' equity available to Arch. We reserve the right to change this threshold at any time. Based on in-force exposure estimated as of October 1, 2015, our modeled peak zone catastrophe exposure was a windstorm affecting the Northeastern U.S., with a net probable maximum pre-tax loss of \$509 million, followed by windstorms affecting the Gulf of Mexico and Florida Tri-County with net probable maximum pre-tax losses of \$473 million and \$414 million, respectively. Our exposures to other perils, such as U.S. earthquake and international events, were less than the exposures arising from U.S. windstorms and hurricanes in both periods. As of October 1, 2015, our modeled peak zone earthquake exposure (Los Angeles earthquake) represented approximately 58% of our peak zone catastrophe exposure, and our modeled

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peak zone international exposure (Japan earthquake) was substantially less than both our peak zone windstorm and earthquake exposures.

Net probable maximum pre-tax loss estimates are net of expected reinsurance recoveries, before income tax and before excess reinsurance reinstatement premiums. Loss estimates are reflective of the zone indicated and not the entire portfolio. Since hurricanes and windstorms can affect more than one zone and make multiple landfalls, our loss estimates include clash estimates from other zones. The loss estimates shown above do not represent our maximum exposures and it is highly likely that our actual incurred losses would vary materially from the modeled estimates. There can be no assurances that we will not suffer a net loss greater than 25% of total shareholders' equity available to Arch from one or more catastrophic events due to several factors, including the inherent uncertainties in estimating the frequency and severity of such events and the margin of error in making such determinations resulting from potential inaccuracies and inadequacies in the data provided by clients and brokers, the modeling techniques and the application of such techniques or as a result of a decision to change the percentage of shareholders' equity exposed to a single catastrophic event. Actual losses may also increase if our reinsurers fail to meet their obligations to us or the reinsurance protections purchased by us are exhausted or are otherwise unavailable. See "Risk Factors—Risk Relating to Our Industry" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Natural and Man-Made Catastrophic Events" in our 2014 Form 10-K.

Financial Measures

Management uses the following three key financial indicators in evaluating our performance and measuring the overall growth in value generated for ACGL's common shareholders:

Book Value per Common Share

Book value per common share represents total common shareholders' equity available to Arch divided by the number of common shares outstanding. Management uses growth in book value per common share as a key measure of the value generated for our common shareholders each period and believes that book value per common share is the key driver of ACGL's share price over time. Book value per common share is impacted by, among other factors, our underwriting results, investment returns and share repurchase activity, which has an accretive or dilutive impact on book value per common share depending on the purchase price. Book value per common share was \$47.68 at September 30, 2015, compared to \$47.49 at June 30, 2015 and \$44.04 at September 30, 2014. The 0.4% increase in the 2015 third quarter reflected underwriting returns substantially offset by negative return on investments, while the 8.3% increase over the trailing twelve months reflected strong investment and underwriting returns.

Operating Return on Average Common Equity

Operating return on average common equity ("Operating ROAE") represents annualized after-tax operating income available to Arch common shareholders divided by the average of beginning and ending common shareholders' equity available to Arch during the period. After-tax operating income available to Arch common shareholders, a "non-GAAP measure" as defined in the SEC rules, represents net income available to Arch common shareholders, excluding net realized gains or losses, net impairment losses recognized in earnings, equity in net income or loss of investment funds accounted for using the equity method and net foreign exchange gains or losses, net of income taxes. Management uses Operating ROAE as a key measure of the return generated to common shareholders and has set an objective to achieve an average Operating ROAE of 15% or greater over the insurance cycle, which it believes to be an attractive return to common shareholders given the risks we assume. See "Comment on Non-GAAP Financial Measures." Our Operating ROAE was 8.6% for the 2015 third quarter, compared to 9.7% for the 2014 third quarter, and 9.7% for the nine months ended September 30, 2015, compared to 11.2% for the 2014 period. Operating ROAE for the 2015 periods primarily reflected a lower level of underwriting income, reflecting current market conditions and

changes in mix of business, compared to the 2014 periods.

Total Return on Investments

Total return on investments includes investment income, equity in net income or loss of investment funds accounted for using the equity method, net realized gains and losses and the change in unrealized gains and losses generated by Arch's investment portfolio. Total return is calculated on a pre-tax basis and before investment expenses, excluding amounts reflected in the 'other' segment, and reflects the effect of financial market conditions along with foreign currency fluctuations. Management uses total return on investments as a key measure of the return generated to Arch common shareholders on the capital held in the business, and compares the return generated by our investment portfolio against benchmark returns which we measured our portfolio against during the periods.

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The benchmark return index is a customized combination of indices intended to approximate a target portfolio by asset mix and average credit quality while also matching the approximate estimated duration and currency mix of our insurance and reinsurance liabilities. Although the estimated duration and average credit quality of this index will move as the duration and rating of its constituent securities change, generally we do not adjust the composition of the benchmark return index except to incorporate the currency mix as noted above. The benchmark return index should not be interpreted as expressing a preference for or aversion to any particular sector or sector weight. The index is intended solely to provide, unlike many master indices that change based on the size of their constituent indices, a relatively stable basket of investable indices.

At September 30, 2015, the benchmark return index had an average credit quality of “Aa2” by Moody’s Investors Service (“Moody’s”), an estimated duration of 3.49 years and included weightings to the following indices:

	Weighting	
The Bank of America Merrill Lynch 1-10 Year AA U.S. Corporate & Yankees Index	21.250	%
The Bank of America Merrill Lynch 1-5 Year U.S. Treasury Index	13.000	
The Bank of America Merrill Lynch U.S. Mortgage Backed Securities Index	11.875	
Barclays Capital CMBS, AAA Index	10.000	
The Bank of America Merrill Lynch 1-10 Year U.S. Municipal Securities Index	7.125	
The Bank of America Merrill Lynch 1-10 Year EMU Governments Index	5.500	
The Bank of America Merrill Lynch U.S. High Yield Constrained Index	5.500	
The Bank of America Merrill Lynch U.S. Bullet Agency Securities 1-10 Years Index	5.000	
MSCI All Country World Gross Total Return Index	5.000	
The Bank of America Merrill Lynch 0-3 Month U.S. Treasury Bill Index	5.000	
The Bank of America Merrill Lynch 5-10 Year U.S. Treasury Index	3.250	
The Bank of America Merrill Lynch 1-5 Year U.K. Gilt Index	3.000	
The Bank of America Merrill Lynch 1-10 Year Australian Governments Index	2.500	
The Bank of America Merrill Lynch 1-5 Year CAD Governments Index	2.000	
Total	100.000	%

The following table summarizes the pre-tax total return (before investment expenses) of investments managed by Arch compared to the benchmark return against which we measured our portfolio during the periods:

	Arch Portfolio		Benchmark Return	
Pre-tax total return (before investment expenses):				
2015 third quarter	(0.31	)%	(0.21)%
2014 third quarter	(0.51	)%	(0.89)%
Nine Months Ended September 30, 2015	0.76	%	(0.07)%
Nine Months Ended September 30, 2014	2.32	%	2.17	%

Total return for the 2015 third quarter reflected the impact of the U.S. Dollar strengthening against the British Pound Sterling, Canadian Dollar and other major currencies on non-U.S. Dollar denominated investments. Excluding the effects of foreign exchange, total return was 0.04% for the 2015 third quarter, as investment-grade fixed income returns were substantially offset by negative returns on equities, high yield and alternative strategies.

Comment on Non-GAAP Financial Measures

Throughout this filing, we present our operations in the way we believe will be the most meaningful and useful to investors, analysts, rating agencies and others who use our financial information in evaluating the performance of our company. This presentation includes the use of after-tax operating income available to Arch common shareholders, which is defined as net income available to Arch common shareholders, excluding net realized gains or losses, net impairment losses recognized in earnings, equity in net income or loss of investment funds accounted for using the equity method and net foreign exchange gains or losses, net of income taxes. The presentation of after-tax operating income available to Arch common shareholders is a “non-GAAP financial measure” as defined in Regulation G. The reconciliation of such measure to net income available to Arch common shareholders (the most directly comparable GAAP financial measure) in accordance with Regulation G is included under “Results of Operations” below.

We believe that net realized gains or losses, net impairment losses recognized in earnings, equity in net income or loss of investment funds accounted for using the equity method and net foreign exchange gains or losses in any particular period are not indicative of the performance of, or trends in, our business. Although net realized gains or losses, net impairment losses

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recognized in earnings, equity in net income or loss of investment funds accounted for using the equity method and net foreign exchange gains or losses are an integral part of our operations, the decision to realize investment gains or losses, the recognition of the change in the carrying value of investments accounted for using the fair value option in net realized gains or losses, the recognition of net impairment losses, the recognition of equity in net income or loss of investment funds accounted for using the equity method and the recognition of foreign exchange gains or losses are independent of the insurance underwriting process and result, in large part, from general economic and financial market conditions. Furthermore, certain users of our financial information believe that, for many companies, the timing of the realization of investment gains or losses is largely opportunistic. In addition, net impairment losses recognized in earnings on our investments represent other-than-temporary declines in expected recovery values on securities without actual realization. The use of the equity method on certain of our investments in certain funds that invest in fixed maturity securities is driven by the ownership structure of such funds (either limited partnerships or limited liability companies). In applying the equity method, these investments are initially recorded at cost and are subsequently adjusted based on our proportionate share of the net income or loss of the funds (which include changes in the market value of the underlying securities in the funds). This method of accounting is different from the way we account for our other fixed maturity securities and the timing of the recognition of equity in net income or loss of investment funds accounted for using the equity method may differ from gains or losses in the future upon sale or maturity of such investments. Due to these reasons, we exclude net realized gains or losses, net impairment losses recognized in earnings, equity in net income or loss of investment funds accounted for using the equity method and net foreign exchange gains or losses from the calculation of after-tax operating income available to Arch common shareholders.

We believe that showing net income available to Arch common shareholders exclusive of the items referred to above reflects the underlying fundamentals of our business since we evaluate the performance of and manage our business to produce an underwriting profit. In addition to presenting net income available to Arch common shareholders, we believe that this presentation enables investors and other users of our financial information to analyze our performance in a manner similar to how management analyzes performance. We also believe that this measure follows industry practice and, therefore, allows the users of financial information to compare our performance with our industry peer group. We believe that the equity analysts and certain rating agencies which follow us and the insurance industry as a whole generally exclude these items from their analyses for the same reasons.

RESULTS OF OPERATIONS

The following table summarizes, on an after-tax basis, our consolidated financial data, including a reconciliation of after-tax operating income available to Arch common shareholders to net income available to Arch common shareholders:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
After-tax operating income available to Arch common shareholders	\$125,798	\$142,055	\$421,600	\$467,128
Net realized gains (losses), net of tax	(58,048	) 27,476	(24,188	) 96,016
Net impairment losses recognized in earnings, net of tax	(5,868	) (8,593	) (12,780	) (26,313
Equity in net income (loss) of investment funds accounted for using the equity method, net of tax	(2,373	) 4,765	19,272	16,983
Net foreign exchange gains (losses), net of tax	15,040	57,488	58,802	48,924
Net income available to Arch common shareholders	\$74,549	\$223,191	\$462,706	\$602,738

Segment Information

We classify our businesses into three underwriting segments — insurance, reinsurance and mortgage — and two other operating segments — ‘other’ and corporate (non-underwriting). Our insurance, reinsurance and mortgage segments each have managers who are responsible for the overall profitability of their respective segments and who are directly accountable to our chief operating decision makers, the Chairman, President and Chief Executive Officer of ACGL and the Chief Financial Officer of ACGL. The chief operating decision makers do not assess performance, measure return on equity or make resource allocation decisions on a line of business basis. Management measures segment performance for our three underwriting segments based on underwriting income or loss. We do not manage our assets by underwriting segment, with the exception of goodwill and intangible assets, and, accordingly, investment income is not allocated to each underwriting segment.

We determined our reportable segments using the management approach described in accounting guidance regarding disclosures about segments of an enterprise and related information. The accounting policies of the segments are the same as those used for the preparation of our consolidated financial statements. Intersegment business is allocated to the segment accountable for the underwriting results. The corporate (non-underwriting) segment results include net investment income,

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other income (loss), other expenses incurred by us, interest expense, net realized gains or losses, net impairment losses included in earnings, equity in net income or loss of investment funds accounted for using the equity method, net foreign exchange gains or losses, income taxes and items related to our non-cumulative preferred shares. Such amounts exclude the results of the ‘other’ segment.

The mortgage segment includes the results of Arch MI U.S. and Arch Mortgage Insurance Limited, leading providers of mortgage insurance products and services to the U.S. and European markets, respectively. Arch MI U.S. is approved as an eligible mortgage insurer by Federal National Mortgage Association (“Fannie Mae”) and Federal Home Loan Mortgage Corporation (“Freddie Mac”), each a government sponsored enterprise, or “GSE.” The mortgage segment also includes GSE credit risk-sharing transactions and mortgage reinsurance for the U.S. and Australian markets.

In March 2014, we invested \$100.0 million and acquired approximately 11% of Watford Holdings Ltd.’s common equity and a warrant to purchase additional common equity. Watford Holdings Ltd. is the parent of Watford Re Ltd., a multi-line Bermuda reinsurance company (together with Watford Holdings Ltd., “Watford Re”). Watford Re is considered a variable interest entity (“VIE”) and we concluded that we are the primary beneficiary of Watford Re. As such, the results of Watford Re are included in our consolidated financial statements. The ‘other’ segment includes the results of Watford Re. Watford Re has its own management and board of directors that is responsible for the overall profitability of its results. The portion of Watford Re’s earnings attributable to third party investors is recorded in the consolidated statements of income as ‘amounts attributable to noncontrolling interests.’ For the ‘other’ segment, performance is measured based on net income or loss.

Insurance Segment

The following table sets forth our insurance segment’s underwriting results:

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2015	2014	% Change	2015	2014	% Change
Gross premiums written	\$752,438	\$726,683	3.5	\$2,263,401	\$2,309,560	(2.0)
Premiums ceded	(209,443)	(187,689)		(669,336)	(646,082)	
Net premiums written	542,995	538,994	0.7	1,594,065	1,663,478	(4.2)
Change in unearned premiums	(20,451)	(19,607)		(53,782)	(158,878)	
Net premiums earned	522,544	519,387	0.6	1,540,283	1,504,600	2.4
Other underwriting income	519	499		1,467	1,513	
Losses and loss adjustment expenses	(339,859)	(338,319)		(978,681)	(936,615)	
Acquisition expenses, net	(77,076)	(81,775)		(228,877)	(235,156)	
Other operating expenses	(84,620)	(83,138)		(261,793)	(250,111)	
Underwriting income	\$21,508	\$16,654	29.1	\$72,399	\$84,231	(14.0)
Underwriting Ratios			% Point Change			% Point Change
Loss ratio	65.0	% 65.1	% (0.1)	63.5	% 62.3	% 1.2
Acquisition expense ratio	14.8	% 15.7	% (0.9)	14.9	% 15.6	% (0.7)
Other operating expense ratio	16.2	% 16.0	% 0.2	17.0	% 16.6	% 0.4
Combined ratio	96.0	% 96.8	% (0.8)	95.4	% 94.5	% 0.9

The insurance segment consists of our insurance underwriting units which offer specialty product lines on a worldwide basis. Product lines include:

Construction and national accounts: primary and excess casualty coverages to middle and large accounts in the construction industry and a wide range of products for middle and large national accounts, specializing in loss

sensitive primary casualty insurance programs (including large deductible, self-insured retention and retrospectively rated programs).

Excess and surplus casualty: primary and excess casualty insurance coverages, including middle market energy business, and contract binding, which primarily provides casualty coverage through a network of appointed agents to small and medium risks.

Lenders products: collateral protection, debt cancellation and service contract reimbursement products to banks, credit unions, automotive dealerships and original equipment manufacturers and other specialty programs that pertain to automotive lending and leasing.

Professional lines: directors' and officers' liability, errors and omissions liability, employment practices liability, fiduciary liability, crime, professional indemnity and other financial related coverages for corporate, private equity, venture capital,

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real estate investment trust, limited partnership, financial institution and not-for-profit clients of all sizes and medical professional and general liability insurance coverages for the healthcare industry. The business is predominately written on a claims-made basis.

Programs: primarily package policies, underwriting workers' compensation and umbrella liability business in support of desirable package programs, targeting program managers with unique expertise and niche products offering general liability, commercial automobile, inland marine and property business with minimal catastrophe exposure.

Property, energy, marine and aviation: primary and excess general property insurance coverages, including catastrophe-exposed property coverage, for commercial clients. Coverages for marine include hull, war, specie and liability. Aviation and stand alone terrorism are also offered.

Travel, accident and health: specialty travel and accident and related insurance products for individual, group travelers, travel agents and suppliers, as well as accident and health, which provides accident, disability and medical plan insurance coverages for employer groups, medical plan members, students and other participant groups.

Other: includes alternative market risks (including captive insurance programs), excess workers' compensation and employer's liability insurance coverages for qualified self-insured groups, associations and trusts, and contract and commercial surety coverages, including contract bonds (payment and performance bonds) primarily for medium and large contractors and commercial surety bonds for Fortune 1,000 companies and smaller transaction business programs.

Premiums Written.

The following table sets forth our insurance segment's net premiums written by major line of business:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2015		2014		2015		2014	
	Amount	%	Amount	%	Amount	%	Amount	%
Programs	\$120,028	22.1	\$129,227	24.0	\$344,404	21.6	\$378,189	22.7
Professional lines	118,563	21.8	119,798	22.2	329,841	20.7	357,117	21.5
Construction and national accounts	60,320	11.1	55,342	10.3	233,919	14.7	230,010	13.8
Property, energy, marine and aviation	51,802	9.5	53,485	9.9	172,518	10.8	200,771	12.1
Excess and surplus casualty	51,170	9.4	50,552	9.4	154,511	9.7	153,281	9.2
Travel, accident and health	49,386	9.1	44,500	8.3	123,714	7.8	119,731	7.2
Lenders products	29,212	5.4	27,799	5.2	76,039	4.8	74,714	4.5
Other	62,514	11.5	58,291	10.8	159,119	10.0	149,665	9.0
Total	\$542,995	100.0	\$538,994	100.0	\$1,594,065	100.0	\$1,663,478	100.0

2015 Third Quarter versus 2014 Third Quarter. Gross premiums written by the insurance segment in the 2015 third quarter were 3.5% higher than in the 2014 third quarter, while net premiums written were 0.7% higher than in the 2014 third quarter. Changes in foreign currency rates resulted in a decrease in net premiums written in the 2015 third quarter of approximately \$11 million, or 2.1%, compared to the 2014 third quarter. The higher level of net premiums written reflected growth in construction, alternative markets and travel, accident and health business, partially offset by a reduction in program business. The growth in construction business primarily reflected an increase in new projects and audit premiums, while the increase in alternative markets primarily resulted from changes in renewal dates on business acquired as part of the renewal rights agreement entered into in the 2014 second quarter. The higher level of travel, accident and health business reflected growth in U.S. travel along with international medical small and medium accounts, while the reduction in program business reflected underwriting decisions.

Nine Months Ended September 30, 2015 versus 2014. Gross premiums written by the insurance segment for the nine months ended September 30, 2015 were 2.0% lower than in the 2014 period, while net premiums written were 4.2% lower than in the 2014 period. The differential in gross versus net premiums written primarily resulted from growth in alternative markets business which is subject to a high level of cessions, primarily to captives. The lower level of net premiums written reflected the impact of changes in foreign currency rates compared to the 2014 periods and reductions in programs, property, energy and marine business and professional lines. The decrease in program business reflected underwriting decisions while the reduction in property, energy and marine business reflected rate decreases and strategic reductions in certain lines. The decline in professional lines was primarily related to the timing of premiums on renewal accounts.

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Net Premiums Earned.

The following table sets forth our insurance segment's net premiums earned by major line of business:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2015		2014		2015		2014	
	Amount	%	Amount	%	Amount	%	Amount	%
Programs	\$115,502	22.1	\$118,087	22.7	\$344,408	22.4	\$341,311	22.7
Professional lines	106,283	20.3	118,204	22.8	321,575	20.9	346,979	23.1
Construction and national accounts	75,256	14.4	68,229	13.1	219,066	14.2	209,282	13.9
Property, energy, marine and aviation	55,106	10.5	59,432	11.4	164,012	10.6	187,242	12.4
Excess and surplus casualty	53,366	10.2	48,716	9.4	157,422	10.2	131,423	8.7
Travel, accident and health	39,918	7.6	34,991	6.7	113,629	7.4	93,701	6.2
Lenders products	23,956	4.6	23,591	4.5	68,074	4.4	70,186	4.7
Other	53,157	10.2	48,137	9.3	152,097	9.9	124,476	8.3
Total	\$522,544	100.0	\$519,387	100.0	\$1,540,283	100.0	\$1,504,600	100.0

Net premiums written are primarily earned on a pro rata basis over the terms of the policies for all products, usually 12 months. Net premiums earned in the 2015 third quarter were 0.6% higher than in the 2014 third quarter and 2.4% higher for the nine months ended September 30, 2015 than in the 2014 period. Net premiums earned reflect changes in net premiums written over the previous five quarters.

Losses and Loss Adjustment Expenses.

The table below shows the components of the insurance segment's loss ratio:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2015		2014		2015		2014	
		%		%		%		%
Current year	66.9	%	67.3	%	65.9	%	65.4	%
Prior period reserve development	(1.9)	)%	(2.2)	)%	(2.4)	)%	(3.1))%
Loss ratio	65.0	%	65.1	%	63.5	%	62.3	%

Current Year Loss Ratio.

The insurance segment's current year loss ratio in the 2015 third quarter was 0.4 points lower than in the 2014 third quarter and 0.5 points higher for the nine months ended September 30, 2015 than in the 2014 period. The 2015 third quarter loss ratio reflected 1.6 points of current year catastrophic activity, compared to 0.4 points in the 2014 third quarter. The loss ratio for the nine months ended September 30, 2015 reflected 1.2 points of current year catastrophic activity, compared to 0.6 points for the 2014 period. The balance of the change in the 2015 periods primarily resulted from a lower level of attritional large loss activity relative to the 2014 periods and changes in the mix of business.

Prior Period Reserve Development.

2015 Third Quarter: The insurance segment's net favorable development of \$9.9 million, or 1.9 points, consisted of \$12.9 million of net favorable development in medium-tailed and long-tailed lines, partially offset by \$3.0 million of net adverse development in short-tailed lines. Net favorable development in medium-tailed and long-tailed lines

reflected favorable development in professional lines of \$14.5 million, which included \$10.8 million of favorable development in executive assurance reserves primarily from the 2007 to 2012 accident years (i.e., the year in which a loss occurred) with the remainder in professional liability and healthcare reserves. Such amounts were partially offset by \$2.4 million of adverse development in programs, primarily from the 2014 accident year. Adverse development in short-tailed lines primarily resulted from travel, accident and health business in the 2014 accident year, partially offset by a reduction in property (including special risk other than marine) reserves from the 2012 to 2014 accident years. Development on the 2005 to 2014 named catastrophic events was adverse by \$0.6 million in the quarter.

2014 Third Quarter: The insurance segment's net favorable development of \$11.4 million, or 2.2 points, consisted of \$15.3 million of net favorable development in short-tailed lines and \$3.9 million of net adverse development in medium-tailed and long-tailed lines. Favorable development in short-tailed lines primarily consisted of reductions in property (including special risk other than marine) reserves from the 2011 to 2013 accident years, primarily due to varying levels of reported claims

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activity. Development on the 2005 to 2013 named catastrophic events was favorable by \$2.1 million in the quarter. Net adverse development in medium-tailed and long-tailed lines reflected increases in construction reserves of \$8.4 million, primarily resulting from higher reported losses in the 2009 to 2011 accident years, and increases in program reserves of \$7.5 million, reflecting higher reported losses in the 2011 and 2012 accident years. In addition, the insurance segment results reflected favorable development in professional lines of \$6.9 million and in marine and other of \$5.1 million.

Nine Months Ended September 30, 2015: The insurance segment's net favorable development of \$37.2 million, or 2.4 points, consisted of \$22.6 million of net favorable development in short-tailed lines and \$14.6 million of net favorable development in medium-tailed and long-tailed lines. Favorable development in short-tailed lines primarily consisted of reductions in property (including special risk other than marine) reserves from the 2011 to 2014 accident years, primarily due to varying levels of reported claims activity. Development on the 2005 to 2014 named catastrophic events was favorable by \$2.3 million for the 2015 period. Net favorable development in medium-tailed and long-tailed lines reflected favorable development in marine reserves, primarily from the 2010 to 2014 accident years, and in surety reserves, primarily from the 2013 to 2014 accident years. In addition, the insurance segment's results reflected net favorable development in professional lines of \$17.5 million, including favorable development in healthcare reserves, primarily from the 2005 to 2011 accident years, and in executive assurance reserves, primarily from the 2010 to 2012 accident years, partially offset by an increase in reserves on professional liability reserves, primarily in the 2011 and 2012 accident years. In addition, the insurance segment's results reflected net adverse development in programs of \$13.4 million, primarily from the 2014 accident year.

Nine Months Ended September 30, 2014: The insurance segment's net favorable development of \$46.4 million, or 3.1 points, consisted of \$56.0 million of net favorable development in short-tailed lines and \$9.6 million of net adverse development in medium-tailed and long-tailed lines. Favorable development in short-tailed lines primarily consisted of reductions in property (including special risk other than marine) reserves from the 2008 to 2013 accident years, primarily due to varying levels of reported claims activity. Development on the 2005 to 2013 named catastrophic events was favorable by \$8.3 million for the 2014 period. Net adverse development in medium-tailed and long-tailed lines reflected increases in construction reserves of \$22.4 million, reflecting higher reported losses in the 2009 to 2012 accident years, and in program reserves of \$21.3 million, reflecting higher reported losses in the 2011 to 2013 accident years. In addition, the insurance segment results reflected favorable development in professional lines of \$18.8 million and in marine and other of \$15.3 million.

Underwriting Expenses.

2015 Third Quarter versus 2014 Third Quarter: The insurance segment's underwriting expense ratio was 31.0% in the 2015 third quarter, compared to 31.7% in the 2014 third quarter. The acquisition expense ratio was 14.8% in the 2015 third quarter, compared to 15.7% in the 2014 third quarter. The lower 2015 third quarter ratio primarily resulted from changes in the mix of business. The other operating expense ratio was 16.2% for the 2015 third quarter, compared to 16.0% for the 2014 third quarter.

Nine Months Ended September 30, 2015 versus 2014: The insurance segment's underwriting expense ratio was 31.9% for the nine months ended September 30, 2015, compared to 32.2% in the 2014 period. The acquisition expense ratio was 14.9% for the nine months ended September 30, 2015, compared to 15.6% in the 2014 period. The lower ratio for the nine months ended September 30, 2015 reflected an increase in ceding commission rates and changes in the mix of business. The other operating expense ratio was 17.0% for the nine months ended September 30, 2015, compared to 16.6% for the 2014 period, reflecting a higher level of aggregate expenses.

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Reinsurance Segment

The following table sets forth our reinsurance segment's underwriting results:

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2015	2014	% Change	2015	2014	% Change
Gross premiums written	\$329,327	\$345,747	(4.7)	\$1,156,540	\$1,212,641	(4.6)
Premiums ceded	(92,182)	(83,502)		(318,197)	(215,623)	
Net premiums written	237,145	262,245	(9.6)	838,343	997,018	(15.9)
Change in unearned premiums	23,286	34,303		(24,230)	(23,495)	
Net premiums earned	260,431	296,548	(12.2)	814,113	973,523	(16.4)
Other underwriting income	2,783	215		6,870	834	
Losses and loss adjustment expenses	(115,780)	(123,784)		(339,495)	(413,745)	
Acquisition expenses, net	(55,416)	(60,205)		(170,380)	(199,673)	
Other operating expenses	(37,131)	(36,337)		(114,182)	(110,198)	
Underwriting income	\$54,887	\$76,437	(28.2)	\$196,926	\$250,741	(21.5)
Underwriting Ratios			% Point Change			% Point Change
Loss ratio	44.5	% 41.7	% 2.8	41.7	% 42.5	% (0.8)
Acquisition expense ratio	21.3	% 20.3	% 1.0	20.9	% 20.5	% 0.4
Other operating expense ratio	14.3	% 12.3	% 2.0	14.0	% 11.3	% 2.7
Combined ratio	80.1	% 74.3	% 5.8	76.6	% 74.3	% 2.3

The reinsurance segment consists of our reinsurance underwriting units which offer specialty product lines on a worldwide basis. Product lines include:

Casualty: provides coverage to ceding company clients on third party liability and workers' compensation exposures from ceding company clients, primarily on a treaty basis. Exposures include, among others, executive assurance, professional liability, workers' compensation, excess and umbrella liability, excess motor and healthcare business.

Marine and aviation: provides coverage for energy, hull, cargo, specie, liability and transit, and aviation business, including airline and general aviation risks. Business written may also include space business, which includes coverages for satellite assembly, launch and operation for commercial space programs.

Other specialty: provides coverage to ceding company clients for proportional motor and other lines including surety, accident and health, workers' compensation catastrophe, agriculture, trade credit and political risk.

Property catastrophe: provides protection for most catastrophic losses that are covered in the underlying policies written by reinsureds, including hurricane, earthquake, flood, tornado, hail and fire, and coverage for other perils on a case-by-case basis. Property catastrophe reinsurance provides coverage on an excess of loss basis when aggregate losses and loss adjustment expense from a single occurrence of a covered peril exceed the retention specified in the contract.

Property excluding property catastrophe: provides coverage for both personal lines and commercial property exposures and principally covers buildings, structures, equipment and contents. The primary perils in this business include fire, explosion, collapse, riot, vandalism, wind, tornado, flood and earthquake. Business is assumed on both a proportional and excess of loss basis. In addition, facultative business is written which focuses on commercial property risks on an excess of loss basis.

Other. includes life reinsurance business on both a proportional and non-proportional basis, casualty clash business and, in limited instances, non-traditional business which is intended to provide insurers with risk management solutions that complement traditional reinsurance.

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Premiums Written.

The following table sets forth our reinsurance segment's net premiums written by major line of business:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2015		2014		2015		2014	
	Amount	%	Amount	%	Amount	%	Amount	%
Casualty	\$63,395	26.7	\$64,048	24.4	\$246,031	29.3	\$258,584	25.9
Other specialty	63,293	26.7	84,702	32.3	236,575	28.2	338,032	33.9
Property excluding property catastrophe	72,456	30.6	77,186	29.4	219,385	26.2	227,200	22.8
Property catastrophe	21,366	9.0	24,056	9.2	82,855	9.9	130,554	13.1
Marine and aviation	12,221	5.2	9,767	3.7	42,526	5.1	33,558	3.4
Other	4,414	1.9	2,486	0.9	10,971	1.3	9,090	0.9
Total	\$237,145	100.0	\$262,245	100.0	\$838,343	100.0	\$997,018	100.0
Pro rata	\$138,367	58.3	\$160,472	61.2	\$397,578	47.4	\$458,332	46.0
Excess of loss	98,778	41.7	101,773	38.8	440,765	52.6	538,686	54.0
Total	\$237,145	100.0	\$262,245	100.0	\$838,343	100.0	\$997,018	100.0

2015 Third Quarter versus 2014 Third Quarter. Gross premiums written by the reinsurance segment in the 2015 third quarter were 4.7% lower than in the 2014 third quarter, while net premiums written were 9.6% lower than in the 2014 third quarter. Changes in foreign currency rates resulted in a decrease in net premiums written in the 2015 third quarter of approximately \$9 million, or 3.4%, compared to the 2014 third quarter. The difference in gross versus net premiums written primarily reflects an increase in cessions to Watford Re in the 2015 third quarter compared to the 2014 third quarter. The lower level of net premiums written reflected decreases in other specialty and property lines. The decrease in other specialty reflected non-renewals and share decreases in response to current market conditions, primarily in proportional motor contracts. The lower level of property business reflected share decreases and timing of renewals.

Nine Months Ended September 30, 2015 versus 2014. Gross premiums written by the reinsurance segment for the nine months ended September 30, 2015 were 4.6% lower than in the 2014 period, while net premiums written were 15.9% lower than in the 2014 period. The differential in gross versus net premiums written primarily reflects an increase in cessions of premiums to Watford Re for the nine months ended September 30, 2015 compared to the 2014 period. The lower level of net premiums written reflected the impact of changes in foreign currency rates compared to the 2014 periods and decreases in other specialty and property catastrophe business. The decrease in other specialty reflected non-renewals and share decreases in response to current market conditions, primarily in proportional motor contracts. The lower level of property catastrophe business reflected non-renewals and share decreases, also in response to current market conditions.

Net Premiums Earned.

The following table sets forth our reinsurance segment's net premiums earned by major line of business:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2015		2014		2015		2014	
	Amount	%	Amount	%	Amount	%	Amount	%
Casualty	\$75,061	28.8	\$79,477	26.8	\$231,628	28.5	\$248,399	25.5
Other specialty	72,337	27.8	97,337	32.8	236,391	29.0	330,779	34.0
Property excluding property catastrophe	72,267	27.7	71,663	24.2	221,631	27.2	216,209	22.2

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Property catastrophe	23,325	9.0	32,423	10.9	74,920	9.2	122,087	12.5
Marine and aviation	13,708	5.3	13,110	4.4	39,744	4.9	47,264	4.9
Other	3,733	1.4	2,538	0.9	9,799	1.2	8,785	0.9
Total	\$260,431	100.0	\$296,548	100.0	\$814,113	100.0	\$973,523	100.0
Pro rata	\$132,090	50.7	\$156,830	52.9	\$429,440	52.7	\$522,611	53.7
Excess of loss	128,341	49.3	139,718	47.1	384,673	47.3	450,912	46.3
Total	\$260,431	100.0	\$296,548	100.0	\$814,113	100.0	\$973,523	100.0

Net premiums written, irrespective of the class of business, are generally earned on a pro rata basis over the terms of the underlying policies or reinsurance contracts. Net premiums earned for the 2015 third quarter were 12.2% lower than in the 2014 third quarter and 16.4% lower for the nine months ended September 30, 2015 than in the 2014 period. Net premiums earned reflect changes in net premiums written over the previous five quarters.

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Losses and Loss Adjustment Expenses.

The table below shows the components of the reinsurance segment's loss ratio:

	Three Months Ended September 30,		Nine Months Ended September 30,			
	2015	2014	2015	2014	2015	2014
Current year	63.7	% 62.3	% 62.1	% 63.1	%	%
Prior period reserve development	(19.2	)% (20.6	)% (20.4	)% (20.6)%)%
Loss ratio	44.5	% 41.7	% 41.7	% 42.5	%	%

Current Year Loss Ratio.

The reinsurance segment's current year loss ratio in the 2015 third quarter was 1.4 points higher than in the 2014 third quarter and 1.0 points lower for the nine months ended September 30, 2015 than in the 2014 period. The 2015 third quarter loss ratio reflected 4.2 points of current year catastrophic activity, compared to 4.6 points in the 2014 third quarter. The loss ratio for the nine months ended September 30, 2015 reflected 2.8 points of current year catastrophic activity, compared to 3.2 points for the 2014 period. The current year loss ratio for the 2015 third quarter reflected a higher level of attritional large loss activity, while the current year loss ratio for both 2015 periods reflected changes in the mix of business earned due, in part, to a lower contribution from property catastrophe business.

Prior Period Reserve Development.

2015 Third Quarter: The reinsurance segment's net favorable development of \$49.9 million, or 19.2 points, consisted of \$19.2 million from short-tailed lines and \$30.7 million from long-tailed and medium-tailed lines. Favorable development in short-tailed lines included \$15.6 million from property catastrophe and property other than property catastrophe reserves, primarily from the 2012 to 2014 underwriting years (i.e., all premiums and losses attributable to contracts having an inception or renewal date within the given twelve-month period). Development from the 2005 to 2014 named catastrophic events was negligible in the 2015 third quarter. The net reduction of loss estimates for the reinsurance segment's short-tailed lines primarily resulted from varying levels of reported and paid claims activity than previously anticipated which led to decreases in certain loss ratio selections during the period. Favorable development in long-tailed lines reflected reductions in casualty reserves of \$26.2 million based on varying levels of reported and paid claims activity, primarily from the 2003 to 2009 underwriting years.

2014 Third Quarter: The reinsurance segment's net favorable development of \$61.0 million, or 20.6 points, consisted of \$26.1 million from short-tailed lines and \$34.9 million from long-tailed and medium-tailed lines. Favorable development in short-tailed lines included \$18.5 million from property catastrophe and property other than property catastrophe reserves, primarily from the 2011 to 2013 underwriting years. Contained within this release was favorable development from the 2005 to 2013 named catastrophic events of \$3.5 million. The net reduction of loss estimates for the reinsurance segment's short-tailed lines primarily resulted from varying levels of reported and paid claims activity than previously anticipated which led to decreases in certain loss ratio selections during the period. Favorable development in long-tailed lines reflected reductions in casualty reserves of \$29.8 million, primarily from the 2005 to 2010 underwriting years based on varying levels of reported and paid claims activity, and a reduction of \$4.8 million in marine and aviation reserves, across all underwriting years.

Nine Months Ended September 30, 2015: The reinsurance segment's net favorable development of \$165.8 million, or 20.4 points, consisted of \$80.0 million from short-tailed lines and \$85.8 million from long-tailed and medium-tailed lines. Favorable development in short-tailed lines included \$61.5 million from property catastrophe and property other than property catastrophe reserves, primarily from the 2012 to 2014 underwriting years. Contained within this release was favorable development from the 2005 to 2014 named catastrophic events of \$10.3 million. The net reduction of loss estimates for the reinsurance segment's short-tailed lines primarily resulted from varying levels of reported and paid claims activity than previously anticipated which led to decreases in certain loss ratio selections during the period. Favorable development in long-tailed lines reflected reductions in casualty reserves of \$74.7 million, primarily from the 2003 to 2009 underwriting years based on varying levels of reported and paid claims activity, and a reduction of \$6.8 million in marine and aviation reserves, across most underwriting years.

Nine Months Ended September 30, 2014: The reinsurance segment's net favorable development of \$200.5 million, or 20.6 points, consisted of \$114.5 million from short-tailed lines and \$86.0 million from long-tailed and medium-tailed lines. Favorable development in short-tailed lines included \$86.5 million from property catastrophe and property other than property catastrophe reserves, primarily from the 2011 to 2013 underwriting years. Contained within this release was favorable

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development from the 2005 to 2013 named catastrophic events of \$12.2 million. The net reduction of loss estimates for the reinsurance segment's short-tailed lines primarily resulted from varying levels of reported and paid claims activity than previously anticipated which led to decreases in certain loss ratio selections during the period. Favorable development in long-tailed lines reflected reductions in casualty reserves of \$69.9 million, primarily from the 2003 to 2010 underwriting years based on varying levels of reported and paid claims activity, and a reduction of \$13.4 million in marine and aviation reserves, across all underwriting years.

Underwriting Expenses.

2015 Third Quarter versus 2014 Third Quarter: The underwriting expense ratio for the reinsurance segment was 35.6% in the 2015 third quarter, compared to 32.6% in the 2014 third quarter. The acquisition expense ratio for the 2015 third quarter was 21.3%, compared to 20.3% for the 2014 third quarter. The comparison of the acquisition expense ratios in each period is influenced by, among other things, the mix and type of business written and earned, including a lower contribution from property catastrophe business than in the 2014 third quarter, and an increase in the level of ceding commissions. The operating expense ratio for the 2015 third quarter was 14.3%, compared to 12.3% in the 2014 third quarter, primarily reflecting the lower level of net premiums earned.

Nine Months Ended September 30, 2015 versus 2014: The underwriting expense ratio for the reinsurance segment was 34.9% for the nine months ended September 30, 2015, compared to 31.8% in the 2014 period. The acquisition expense ratio was 20.9% for the nine months ended September 30, 2015, compared to 20.5% in the 2014 period. The comparison of the acquisition expense ratios in each period is influenced by, among other things, the mix and type of business written and earned, including a lower contribution from property catastrophe business than in the 2014 period. The operating expense ratio for the nine months ended September 30, 2015 was 14.0%, compared to 11.3% in the 2014 period, primarily reflecting the lower level of net premiums earned.

Mortgage Segment

The following table sets forth our mortgage segment's underwriting results:

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2015	2014	% Change	2015	2014	% Change
Gross premiums written	\$74,657	\$66,389	12.5	\$203,770	\$169,772	20.0
Premiums ceded	(7,832)	(7,904)		(23,404)	(17,622)	
Net premiums written	66,825	58,485	14.3	180,366	152,150	18.5
Change in unearned premiums	(12,277)	(5,539)		(22,992)	(9,606)	
Net premiums earned	54,548	52,946	3.0	157,374	142,544	10.4
Other underwriting income	3,565	988		14,969	2,970	
Losses and loss adjustment expenses	(9,562)	(15,987)		(33,010)	(39,938)	
Acquisition expenses, net	(10,428)	(11,958)		(31,046)	(32,593)	
Other operating expenses	(21,048)	(17,913)		(61,096)	(48,077)	
Underwriting income	\$17,075	\$8,076	111.4	\$47,191	\$24,906	89.5

Underwriting Ratios	% Point Change			% Point Change		
Loss ratio	17.5	% 30.2	% (12.7)	21.0	% 28.0	% (7.0)
Acquisition expense ratio	19.1	% 22.6	% (3.5)	19.7	% 22.9	% (3.2)
Other operating expense ratio	38.6	% 33.8	% 4.8	38.8	% 33.7	% 5.1
Combined ratio	75.2	% 86.6	% (11.4)	79.5	% 84.6	% (5.1)

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Premiums Written.

The following table sets forth our mortgage segment's net premiums written by client location and underwriting location (i.e., where the business is underwritten):

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2015		2014		2015		2014	
	Amount	%	Amount	%	Amount	%	Amount	%
Net premiums written by client location:								
United States	\$48,611	72.7	\$54,639	93.4	141,893	78.7	137,306	90.2
Other	18,214	27.3	3,846	6.6	38,473	21.3	14,844	9.8
Total	\$66,825	100.0	\$58,485	100.0	\$180,366	100.0	\$152,150	100.0
Net premiums written by underwriting location:								
United States	\$33,298	49.8	\$32,229	55.1	\$91,843	50.9	\$73,554	48.3
Other	33,527	50.2	26,256	44.9	88,523	49.1	78,596	51.7
Total	\$66,825	100.0	\$58,485	100.0	\$180,366	100.0	\$152,150	100.0

2015 Third Quarter versus 2014 Third Quarter. Net premiums written for the 2015 third quarter were 14.3% higher than in the 2014 third quarter and included \$31.2 million of business underwritten by Arch MI U.S., compared to \$32.2 million in the 2014 third quarter. The 2015 third quarter amount reflected \$23.7 million from credit union clients and \$7.5 million from banks and other mortgage originators, compared to \$24.6 million from credit union clients and \$7.6 million from banks and other mortgage originators in the 2014 third quarter. Premiums written on reinsurance treaties were higher by \$9.4 million compared to the 2014 third quarter, primarily reflecting growth in single premium Australian business. The persistency rate, which represents the percentage of mortgage insurance in force at the beginning of a 12-month period that remains in force at the end of such period, of the Arch MI U.S. portfolio of mortgage loans was 76.0% at September 30, 2015, compared to 80.9% at December 31, 2014. The decline in persistency was due to policy terminations reflecting mortgage refinance activity and the continuing low interest rate environment.

Nine Months Ended September 30, 2015 versus 2014. Net premiums written for the nine months ended September 30, 2015 included \$89.7 million of business underwritten by Arch MI U.S., compared to \$73.6 million for the 2014 period. The 2015 amount reflected \$71.1 million from credit union clients and \$18.6 million from banks and other originators, compared to \$65.7 million from credit union clients and \$7.9 million from banks and other mortgage originators for the 2014 period. The 2014 period reflected eight months of activity for Arch MI U.S. due to the acquisition date of January 30, 2014.

Arch MI U.S. generated \$3.18 billion of new insurance written ("NIW") during the 2015 third quarter, of which approximately 57% was from banks and other non-credit union mortgage originators. NIW represents the original principal balance of all loans that received coverage during the period.

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The following table provides details on the NIW generated by Arch MI U.S.:

(U.S. Dollars in millions)	Three Months Ended								Nine Months Ended	
	September 30, 2015		June 30, 2015		March 31, 2015		December 31, 2014		September 30, 2015	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Total new insurance written (NIW)	\$3,179		\$2,709		\$1,808		\$1,359		\$7,696	
Total NIW by credit quality (FICO score):										
>=740	\$1,973	62.1	\$1,723	63.6	\$1,064	58.8	\$730	53.7	\$4,760	61.9
680-739	976	30.7	842	31.1	602	33.3	480	35.3	2,420	31.4
620-679	230	7.2	143	5.3	142	7.9	149	11.0	515	6.7
<620	—	—	1	—	—	—	\$—	—	1	—
Total	\$3,179	100.0	\$2,709	100.0	\$1,808	100.0	\$1,359	100.0	\$7,696	100.0
Total NIW by LTV:										
95.01% and above	\$219	6.9	\$165	6.1	\$86	4.8	\$79	5.8	\$470	6.1
90.01% to 95.00%	1,458	45.9	1,227	45.3	682	37.7	620	45.6	3,367	43.8
85.01% to 90.00%	1,054	33.2	908	33.5	583	32.2	389	28.6	2,545	33.1
85.01% and below	448	14.1	409	15.1	457	25.3	271	19.9	1,314	17.1
Total	\$3,179	100.0	\$2,709	100.0	\$1,808	100.0	\$1,359	100.0	\$7,696	100.0
Total NIW purchase vs. refinance:										
Purchase	\$2,483	78.1	\$1,830	67.6	\$918	50.8	\$950	69.9	\$5,231	68.0
Refinance	696	21.9	879	32.4	890	49.2	409	30.1	2,465	32.0
Total	\$3,179	100.0	\$2,709	100.0	\$1,808	100.0	\$1,359	100.0	\$7,696	100.0

Net Premiums Earned.

The following table sets forth our mortgage segment's net premiums earned by underwriting location:

Net premiums earned by underwriting location:	Three Months Ended September 30, 2015				Nine Months Ended September 30, 2014			
	2015		2014		2015		2014	
	Amount	%	Amount	%	Amount	%	Amount	%
United States	\$29,620	54.3	\$25,569	48.3	\$82,589	52.5	\$67,244	47.2
Other	24,928	45.7	27,377	51.7	74,785	47.5	75,300	