GREYCASTLE

GreyCastle Life Reinsurance (SAC) Ltd.
Financial Condition Report

For the Year Ended December 31, 2016

Issued: April 27, 2017

Contents

INTRODUCTION

On 30 May 2014, GreyCastle Holdings Ltd. purchased XL Life Reinsurance (SAC) Ltd. from the XL Group. XL Life Reinsurance (SAC) Ltd. was a Bermuda based company that wrote life retrocession business ceded from several XL entities. On 4 June 2014, XL Life Reinsurance (SAC) Ltd. was renamed GreyCastle Life Reinsurance (SAC) Ltd ("The Company"). The Company is licensed as a Class C insurer and was registered under the Segregated Accounts Act 2000.

On 30 April 2014 GreyCastle Holdings Ltd. established a wholly owned subsidiary in the United Kingdom, GreyCastle Services Limited ("GSL"). GSL has entered into arrangements with the Company and various XL entities to provide accounting, administration, actuarial and claims services.

This document is the Financial Condition Report for the Company for the period ending 31 December 2016. The format of the report follows that used in the Bermuda Monetary Authority's Financial Condition Report template.

i) BUSINESS AND PERFORMANCE

a) Name of Insurer
GreyCastle Life Reinsurance (SAC) Ltd.

b) Supervisors
Insurance Supervisor

Name	Patience Maina
Jurisdiction	Bermuda
Email	pmaina@bma.bm
Phone	001 441 278 0363

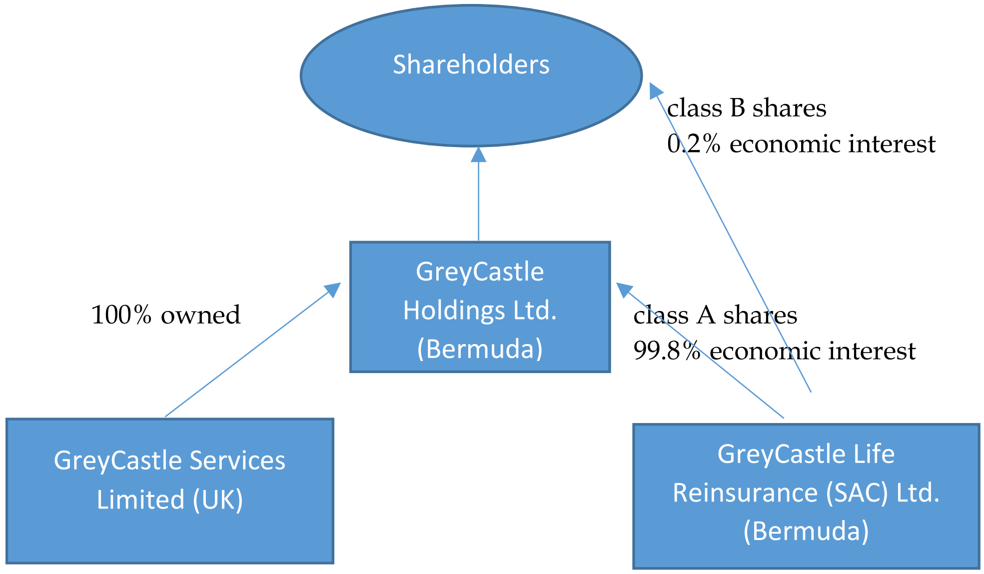
Group Supervisor
Not applicable

c) Approved Auditor

Organisation	Pricewaterhouse Coopers
Name	Stewart Ritchie
Jurisdiction	Bermuda
Email	stewart.ritchie@bm.pwc.com
Phone	001 441 299 7262

d) Ownership Details
GreyCastle Holdings Ltd. owns 99.8% of the economic interest in the Company and GreyCastle Holdings Ltd.'s shareholders own a 0.2% economic interest in the Company.

e) Group Structure



f) Insurance Business written by line of business and geographical region

The Company predominantly writes life reinsurance business in the UK and Ireland, focusing on annuity products (including longevity swaps) and term assurance business (mortality and critical illness business). The Company writes several smaller lines of business including Variable Annuity business originating mainly from the US, and covers on Insurance products written in Continental Europe.

Premium written by product line for the year ending 2016

Line of Business	Gross Premium Written USD 000's	Net Written Premium USD 000's
Mortality	52,782	52,782
Critical Illness	27,294	27,294
Longevity	98,885	98,885
Variable Annuity	5,874	5,874
Total	184,835	184,835

Gross Premium written by geographical location for the year ending 2016

Geographical Location	Gross Premium Written USD 000's
Central & Western Asia	425
Northern Europe	176,429
Southern Europe	990
Western Europe	5,669
Mid-West United States	1,322
Total	184,835

g) Performance of Investments and Material Income and Expenses for year ending 2016

The assets backing the Company's reserves are held on its cedants (various XL entities) balance sheets.

The Company has appointed investment managers to manage these assets, operating within guidelines agreed with its cedants. The table below shows the market values of these assets and the average gross redemption yields at the end of the reporting period.

Product Line	Market Value of Invested Assets (USD 000's)	Gross Redemption Yield at 31 Dec 2016 (%)
Single Premium Annuity (GBP)	2,488,245	2.68
Single Premium Annuity (Euro)	1,230,120	1.90
Other business	396,867	1.76

The Company's other assets (referred to as "Balance Sheet assets") are invested in high quality fixed interest securities. The table below shows the market values of these fixed interest securities split by type of investment at the end of the reporting period.

Fixed Interest Securities	Market Value at 31 Dec 2016 (USD 000's)
US Government (Federal)	81,397
Non US Government	25,744
Corporate (non US Govt backed)	2,163
Corporate (other)	28,318
Mortgage backed (Commercial)	6,900
Total	144,522

The Company's main source of income was premiums written on longevity swap and term assurance products. The major expenses relate to claim payments written on single premium longevity, longevity swap and term assurance products.

USD 000's	2015	2016
Income		
Premiums – life	101,753	85,950
Premiums – annuity	114,163	98,885
Total income	215,916	184,835
Expenses		
Claims – life	72,163	75,394
Claims - annuity	423,206	374,455
Commission (inc other)	5,944	3,106
Operating expenses	19,556	14,351
Total expenses	520,869	467,306

In US dollar terms the premiums and claims were lower in 2016, when compared to 2015, through the depreciation of sterling and the euro against the US dollar, and also the natural run-off of the business. Operational expenses were higher in 2015 than in 2016, mainly because the 2015 expense base includes some one-off costs incurred in setting up the Company, although movements in exchange rates also explain some of the difference.

h) Any Other Material Information

There is no other material information.

ii) GOVERNANCE STRUCTURE

a) Board and Senior Executive

i) *Directors and Officers, and responsibilities*

The directors and officers of the Company are detailed in the table below:

Directors	Position
Lord James Blyth	Chairman of Board
Willis T. King	Director (Independent)
Raymond Brooks	Director and Chief Executive Officer
Andrew Cook	Director (Independent)
Officers	
Beth Schneider-DeGroat	Human Resources and Administration
Neil Russell	Approved Actuary
John Cordey	Chief Risk Officer
Garth Fleming	Principal Representative

The ultimate responsibility for sound and prudent management of the Company rests with the Board of Directors (the "Board"). The Board is responsible for ensuring that corporate governance policies and practices are developed and applied in a prudent manner. The Board has delegated its authority (under its oversight) to the following committees to assist it in discharging its responsibilities:

- Risk Committee – includes the oversight of risk management, integrity of financial statements, and oversight of internal controls.
- Investment Committee – includes the oversight of investment activity and strategy.
- Compensation Committee – includes the determination and agreement of compensation policy.

ii) *Description of Remuneration Policy*

The Independent Directors are paid a fixed retainer for their Board services, which includes attendance at Board meetings. Senior management receive a basic salary, a standard benefits package and an annual cash bonus based on Company and individual performance measures.

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

GreyCastle provides all employees with pension benefits through defined contribution schemes. There are no supplementary pension or early retirement schemes.

iv) *Details of any material transactions with Shareholder Controllers, Persons who exercise significant influence, the Board and Senior Executive*

Not applicable.

b) Fitness and Propriety Requirements

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

The Board and the respective Committees of the Board are governed by charters that prescribe the periodic (generally annual) self and peer assessment of each Director's contribution to the Company.

Directors are elected each year at the Annual General Meeting.

Senior employees are subject to regular appraisal.

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

Board members and senior employees have appropriate academic and professional qualifications and significant industry experience, and are generally considered to be experts in their fields.

c) <u>Risk Management and Solvency Self-Assessment</u>

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

The Company has developed a Risk Management Framework ("RMF") to support and sustain risk management activity throughout the Company. Risks are identified, defined and measured through a Risk Register that is reviewed and updated at least annually. The risks are managed in a number of ways including: review of experience for insurance risks; asset liability management and analysis of credit exposures for investment risks; and internal controls for operational risks. Risks are reported to Senior Management and the Board through a variety of regular reports.

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

The Company's RMF is implemented into its day to day operations through its systems, processes and controls that are detailed in the Company's Controls Manuals. The Company's risk management systems are used to make the following assessments of the solvency:

- Regulatory solvency is assessed on a quarterly basis to ensure the Company can meet its statutory requirements.

- Management assess capital requirements using a "Solvency Self-Assessment" model. The model has been developed and the initial results will relate to this 31 December 2016 valuation. It is envisaged that the model will be run on a quarterly basis when it is fully operational.

- Operational Planning is carried out twice a year (see (iii) *Relationship between Solvency Self-Assessment, Solvency Needs and Capital, and Risk Management*), and includes a projection of likely distributions to the Company's shareholders over the lifetime of the business.

iii) *Relationship between Solvency Self-Assessment, Solvency Needs and Capital, and Risk Management Systems*

The Company's Risk Management and Solvency Self-Assessment systems also drive projections of assets, liabilities and solvency requirements. These projections are produced twice yearly and form the Company's Operating Plan (produced in April following the year end) and Reforecast (a 6 monthly update produced in September). Income statements, balance sheets and distributions are projected over the lifetime of the business, along with an analysis of change. The Operating Plan and Reforecast are both reviewed and approved by the Board.

iv) *Solvency Self-Assessment Approval Process*

As the Solvency Self-Assessment becomes embedded in the Company's risk management processes, it will be regularly reviewed by the Company's Senior Management team, and the Board.

d) Internal Controls

i) *Internal Control System*

Whilst responsibility for the Company's internal controls rests with the Board, the Board delegates its authority to various committees of the Board. Day to day responsibility for the control environment is delegated to management, who ensure its smooth operation through the Controls Manuals.

ii) *Compliance Function*

Oversight on compliance is delegated to Conyers, Dill and Pearman who also provide legal services.

e) Internal Audit

Independent verification of the adequacy and effectiveness of the internal controls will be provided by the internal audit function, supported by the Audit Committee of the Board of GreyCastle Holdings Ltd. The Company has not yet established an internal audit function, but it is expected that this will be filled by an external service provider.

f) Actuarial Function

The Actuarial Function is outsourced to GSL. The Actuarial Function is managed by the Chief Actuary of GSL, and the team consists of (i) a reserving and financial reporting team and (ii) a risk management team whose duties also include the review of experience and valuation bases. The Actuarial Function works closely with the Approved Actuary of the Company.

g) Outsourcing

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

All outsourcing decisions are taken by the Board, with advice provided by management. The Company has engaged various third party service providers: (i) GreyCastle Services Limited ("GSL") provide actuarial, accounting, treaty administration and claims services; (ii) Conyers, Dill and Pearman provide legal and compliance services; (iii) Aon Insurance Managers (Bermuda) Limited and Harbour HR provide payroll services; (iv) Blackrock Solutions Limited provide Chief Investment Officer Services; (v) Blackrock Asset Management, Western Asset Management and JP Morgan Assessment Management provide asset management services; and (vi) HSBC Bank of Bermuda, the Bank of N.T. Butterfield and Son, and JP Morgan Chase Bank N.A. provide banking services.

ii) *Material Intra Group Outsourcing*

The Company outsources actuarial, accounting, treaty administration and claims services to GSL, which is wholly owned by GreyCastle Holdings Ltd.

h) Other Material Information

There is no other material information.

iii) RISK PROFILE

a) <u>Material Risks that the Insurer is exposed to during the Reporting Period</u>

The Company is exposed to the following risks:

- Insurance Risk – the adverse impact arising from fluctuations in the timing, frequency and severity of insured events, relative to the expectations of the Company at the time of underwriting or subsequent reassessment at the time of reserving.

- Investment, Liquidity and Concentration Risk – the adverse impact arising from a lack of sufficient financial resources available to meet obligations as they fall due or because such resources can only be secured at excessive cost.

- Market risk – the adverse impact arising from the uncertainty in the valuation arising from changes in interest rate risk, foreign exchange, equities and or macroeconomic factors.

- Credit Risk – the adverse impact arising from the failure of counterparties to make full and timely payments on their financial obligations or from the change in the market value of assets due to deterioration of the counterparty's creditworthiness.

- Operational Risk – the adverse impact arising from inadequate or failed internal processes, people and systems, or from external events.

- Strategic Risk – the adverse impact from internal or external factors which threaten the ability of the Company to execute its overall organisational strategy.

- Legal Risk – the adverse impact arising from external events, actions or changing conditions in the legal environment.

- Emerging Risk – the adverse impact arising from external events, actions or changing conditions in the business environment.

The Company measures these risks using a combination of proprietary and third party models, where quantifiable. There were no material changes to the risks during the reporting period, although the Company increased its monitoring of its investment risks due to a number of geopolitical events (e.g. EU referendum in the United Kingdom, US Presidential elections, etc.)

b) <u>Risk Mitigation in the Organisation</u>

The Company has an appetite for the insurance and credit risks that are written. Risks are managed through the RMF (for more detail see (ii) GOVERNANCE STRUCTURE (c) *Risk Management and Solvency Self-Assessment*)

c) <u>Material Risk Concentrations</u>

The most material insurance risk concentration is longevity risk which the Company has actively sought, and this risk is managed through the processes discussed in previous sections. The Company has policies to limit concentrations of investment risk in relation to counterparties, credit quality and mismatches in duration between its assets and liabilities.

d) Investment in Assets in Accordance with the Prudent Person Principles of the Code of Conduct

Investments are managed within strict investment guidelines that ensure that assets are invested in accordance with the prudent person principle defined in Paragraph 5.1.2 of the Insurance Code of Conduct. The purpose of the guidelines is (i) to establish the investment objectives and performance standards of the portfolio; (ii) to ensure that the respective portfolios are structured to meet the objectives of GreyCastle and its cedants; and (iii) to prevent exposure to excessive risk aggregation.

e) Stress Testing and Sensitivity Analysis to assess material risks

The Company performs regular stress and scenario testing to ensure that regulatory requirements can be met. For certain scenarios, these analyses have been extended to investigate the dividend paying ability of the Company under these scenarios.

The Company uses a combination of simple deterministic analysis, and more complex stochastic techniques to model its key risks. The tests consider the immediate impact on regulatory requirements, and also longer term impacts on dividend paying ability.

f) Any other material information

There is no other material information.

iv) SOLVENCY VALUATION

a) Valuation bases, assumptions and methods used to derive the value of each asset class

The Company has used the valuation principles outlined by the Bermuda Monetary Authority's "Guidance note for Statutory Reporting Regime" dated 30 November 2016 for the reporting period's regulatory filing. The economic valuation principles are to measure assets and liabilities on a fair value basis. The fair value principles used for the assets are as follows:

- Cash and cash equivalents – the fair value of these holdings is determined using a mark to market valuation.
- Fixed income securities – these are valued using quoted market prices.
- Premium receivable – this is recorded at fair value. Any balances owing for more than 12 months are eliminated.
- Derivative instruments – these are valued using quoted market prices.

b) Valuation bases, assumptions and methods used to derive the value of technical provisions

Insurance technical provisions are valued using best estimate cashflows, which are discounted using a risk free discount rate term structure with an appropriate illiquidity adjustment which is assessed as follows:

- Single Premium Annuity business – a "scenario based approach" is used which reflects the assets that are held to back each portfolio, and the extent to which they are duration and cashflow matched, using tests prescribed by the Bermuda Monetary Authority ("BMA").
- Other business – a "standard approach" is used, using an adjustment provided by the BMA.

A risk margin is also established to reflect the inherent uncertainty in the underlying cashflows using a cost of capital approach and a risk free discount rate term structure.

The best estimate assumptions used to derive the cashflows are based on detailed historic experience investigations, and expectations of future experience.

c) Description of recoverables from reinsurance contracts

The Company does not use reinsurance or any other risk transfer mechanisms.

d) Valuation bases, assumptions and methods used to derive the value of other liabilities

Other liabilities are valued using generally accepted accounting principles.

e) Any other material information

There is no other material information.

v) CAPITAL MANAGEMENT

a) Eligible Capital

i) *Capital management policy and process for capital needs*

The Company holds capital equivalent to a Standard & Poors "AA" rated level. This level of capital and reserves is tested against the regulatory level quarterly. There have been no material changes in the approach in the reporting period.

ii) *Eligible Capital categorised by tiers in accordance with the eligible capital rules*

At the end of the reporting period all of the Company's Eligible Capital was categorised as Tier 1:

USD 000's	Eligible Capital
Tier 1	786,782
Tier 2	-
Tier 3	-
Total	786,782

iii) *Eligible Capital by tiers, used to meet ECR and MSM requirements*

At the end of the reporting period, all of the Company's Eligible Capital for its Minimum Margin of Solvency ("MSM") and Enhanced Capital Requirement ("ECR") was categorised as Tier 1:

USD 000's	Minimum Margin of Solvency	Enhanced Capital Requirement
Tier 1	786,782	786,782
Tier 2	-	-
Tier 3	-	-
Total	786,782	786,782

iii) *Confirmation of Eligible Capital that is subject to transitional arrangements*

None of the eligible capital is subject to transitional arrangements.

v) *Identification of any factors affecting the encumbrances affecting the availability and transferability of capital to meet the ECR*

There are no policyholder liabilities that sit outside the pledged accounts, so all capital is classified as Tier 1.

vi) *Identification of Ancillary Capital Instruments that have been approved by the Authority*

The Company has no Ancillary Capital Instruments.

vii) *Identification of differences in Shareholder's Equity as stated in the financial statements versus the available statutory capital and surplus*

The major differences between the shareholder's equity in the accounts and the statutory capital and surplus relate to differences in the accounting approach. The financial statements are prepared using "US

GAAP" accounting rules, whereas the statutory capital and surplus is prepared using the BMA's Economic Balance Sheet rules. The major differences relate to:

- Inclusion of the "Value of Business Acquired" asset in the US GAAP financial statements.

- Use of a market rate of interest (using risk free yields plus an illiquidity premium) for the derivation of the valuation interest rate used in the reserve calculations in the statutory capital and surplus, as opposed to a "locked in" valuation interest rate in the US GAAP financial statements.

- Use of best estimate assumptions for decrements in the statutory capital and surplus, as opposed to "locked in" assumptions in the US GAAP financial statements.

b) <u>Regulatory Capital Requirements</u>

i) *ECR and MSM requirements at the end of the reporting period*

At the end of the reporting period, the Company's regulatory capital requirements were as follows:

	Amount in USD 000's	Coverage Ratio
Minimum Margin of Solvency	64,518	1,219%
Enhanced Capital Requirement	239,290	329%

ii) *Identification of any non-compliance with the MSM and the ECR*

The Company was compliant with the MSM and the ECR during the year ending December 31, 2016 and remains compliant at the date of the report.

iii) *Description of the amount and circumstances surrounding the non-compliance, the remedial measures taken and their effectiveness*

Not applicable

iv) *Where the non-compliance has not been resolved, description of the amount of non-compliance at the end of the reporting period*

Not applicable

c) <u>Approved Internal Capital Model</u>

i) *Description of the purpose and scope of the business and risk areas where the Internal Model is used*

Not applicable

ii) *Where a Partial Internal Model is used, description of the integration with the BSCR Model*

Not applicable

iii) *Description of the methods used in the Internal Model to calculate the ECR*

Not applicable

iv) *Description of the aggregation methodologies and diversification effects*

Not applicable

v) *Description of the main differences in the methods and assumptions used for the risk areas in the Internal Model versus the BSCR Model*

Not applicable

vi) *Description of the nature and suitability of the data used in the Internal Model*

Not applicable

vii) *Any other material information*

There is no other material information.

vi) SIGNIFICANT EVENTS

a) Description of the significant event

There are no significant events either in the reporting period, or that have occurred between the end of the reporting period and the date of signing the return.

b) Approximate date(s) or proposed timings of the significant event

Not applicable

c) Confirmation of how the significant event has impacted or will impact any information provided in the most recent financial condition report filed with the Authority

Not applicable

d) Any other material information

Not applicable