# Engaged governance and a dynamic culture

**Peter Clarke**
Non-Executive Chairman

**"Lancashire's dynamic and successful business culture is based on a common understanding of strategic goals across the Board and the business fostered by effective, direct and reciprocal communication."**

In my opening statement, I discussed the way in which our business and Board responded to the strategic challenges of 2018. The following section focuses on the work carried out by the Board and its Committees in providing responsive challenge and support to the business in the articulation and delivery of strategy and in exercising effective oversight.

## How does the Board manage and implement the governance arrangements for the Group?

Lancashire is a premium-listed company on the LSE, which measures its corporate governance compliance against the requirements of the UK Corporate Governance Code published by the UK FRC. The FCA requires each company with a premium listing to 'comply or explain' against the Code (i.e. to disclose how it has complied with Code provisions or, if the Code provisions have not been complied with, provide an explanation for the non-compliance). The Group monitors its compliance with the Code on at least a quarterly basis.

In this corporate governance section and throughout the Annual Report and Accounts for the 2018 financial year, areas of corporate governance compliance are explained by reference to the Code. The Company also monitors its compliance with applicable corporate governance requirements under both Bermuda law and regulations and, during 2018, with the requirements of the PRA and the UK's Solvency II regime.

Once again I am pleased to report that, in the judgement of the Board, the Company has complied with the principles and provisions as set out in the Code throughout the year ended 31 December 2018. The Board and business seek to ensure that the formal consideration of governance and regulatory requirements are used as a proactive and constructive exercise to foster the dynamic and successful business culture which has been a hallmark of the Group's success over many years.

## How has the Board managed its Group regulatory status during the year?

In 2012, the Company established its head office and conducted the majority of its Board business in the UK. Prior to this it was in Bermuda. Between 2016 and 2018, the PRA has operated as the Group's supervisory regulator and the Group has been subject to the requirements of the UK's Solvency II regime. During 2018, the Board held detailed discussions about the most suitable Group insurance supervisory and tax domicile for the Company and initiated engagement with the PRA, the BMA and the UK's HMRC, further to which it was agreed that, with effect from 1 January 2019, the Company should re-establish its Group supervisory and tax domiciles in Bermuda. This will not affect the regulation of the Group's UK insurance entities, which will continue to be regulated by the PRA, and the FCA, and in the case of CUL and Syndicates 2010 and 3010, Lloyd's. On balance the Board felt that the transition of Group supervision to Bermuda and the BMA would assist in ensuring a continuing strategic focus on the growth and development opportunities in the U.S. specialty and catastrophe markets.

## In the light of changes to the UK Corporate Governance Code how does the Board expect to develop Lancashire's stakeholder engagement in promoting the success of the business?

The FRC published a revised UK Corporate Governance Code during 2018, and our Board has been tracking these developments principally through the work of our Nomination and Corporate Governance Committee (see page 63 for the Committee report). Whilst we will be taking steps during 2019 to track and implement the upcoming requirements of the revised Code, we anticipate that the Board and business are well placed to meet the expectations articulated in the Code with regard to stakeholder engagement. Indeed, it is my view that the Company already has, and will continue to operate, a strong culture of proactive and constructive stakeholder engagement. Readers will note a more detailed account of the way in which the Company engages with its stakeholders in the engagement and sustainability section of this report on pages 40 to 44.

In the area of 'workforce' engagement, the Board plans to address the expectations of the revised UK Code during 2019 by making arrangements for the direct involvement of one or more of our Non-Executive Directors in current 'town hall' staff meetings which, for a number of years, Alex Maloney has held on a quarterly basis with all our staff in the UK and Bermuda. I will be attending some of these sessions during 2019 and the Board will also be exploring other ways and means to facilitate constructive two-way feedback between the Board and the Group's employees. In this regard I would also add that we have the great advantage of having an employee headcount of a little over 200 people, so all our employees are known personally by our Group CEO or the other members of the Group's executive management team and most of our Non-Executive Directors have regular opportunities to meet members of staff both as part of the formal business of the Board and informally outside Board meetings.

## How has Board membership and succession planning evolved during the year?

At the end of the first quarter of 2018, Tom Milligan stepped down from our Board, after having completed three years' service, to explore other opportunities in the insurance sector. I would like to thank Tom for his contribution to our business and insight as a member of our Board and wish him well for the future. After careful consideration of a diverse range of candidates, I was delighted that in July 2018 we were able to confirm the appointment of Sally Williams as a Non-Executive Director, who joined us in January 2019. In the light of Sally's recent employment as a senior executive and director within the Marsh Group, a global insurance brokerage which provides certain services to the Group, each of our Directors met individually with Sally prior to her appointment. The Board gave careful consideration to the question of Sally's independence of character and judgement in the light of her employment with an organisation which has had regular business dealings with the wider Group and its subsidiaries and which requires special consideration under the terms of the UK Corporate Governance Code (see page 55 for further details). I am delighted to report that after a detailed and thorough discussion the Board was unanimous in deciding that it should exercise its discretion to determine that Sally Williams should be considered independent on her appointment. I look forward to working with Sally in the coming years. In particular, Sally's experience (see page 51 for details) will help make her a valuable new member of our Audit Committee.

## Are the Board and its Committees operating effectively?

During 2018 our Board once again carried out a review of its effectiveness, which was facilitated by Lintstock Ltd. A summary report was discussed by the full Board and we concluded that the Board, its members and each of its Committees have a balance of experience and talents that serves the Group well and have the culture and competencies necessary to meet the strategic challenges of the business effectively. I have throughout 2018 continued to meet regularly with the chairs of each of our principal subsidiary boards and our performance evaluation also concluded that the relationship between the main Lancashire Board and the subsidiary boards continues to operate effectively.

We have identified various strategic areas of focus and enhancements to the ways we operate and have identified certain specific areas for training and learning during the coming year (see page 56 for further details). I would like to thank all of our Directors, our management team and all our employees for their hard work during the year.

**Peter Clarke**
Non-Executive Chairman

# A balanced board

**Peter Clarke** (B) (I) (N) (R)
Non-Executive Chairman

**Date of appointment to the Board:**
**9 June 2014**

**Board meeting attendance: 5/5**

**Skills, experience and qualifications:**

Peter Clarke was Group Chief Executive of Man Group plc between April 2007 and February 2013. In 1993, Mr Clarke joined Man Group plc, a leading global provider of alternative investment products and solutions as well as one of the world's largest futures brokers. He was appointed to the board in 1997 and served in a variety of roles, including Head of Corporate Finance and Corporate Affairs and Group Company Secretary, before becoming the Group Finance Director in 2000. During this period he was responsible for investing in and developing one of the leading providers of third-party capital insurance and reinsurance products. In November 2005, he was given the additional title of Group Deputy CEO. Mr Clarke has previously served as the Chairman of the National Teaching Awards Trust. Mr Clarke took a first in Law at Queens' College, Cambridge and is a qualified solicitor, having practised at Slaughter and May, and has experience in the investment banking industry, working at Morgan Grenfell and Citibank.

**External appointments/Other roles:**

Mr Clarke is currently a Non-Executive Director of RWC Partners Limited, Lombard Odier Asset Management and Sainsbury's Bank plc. He is a member of the Treasury Committee of King's College London.

**Alex Maloney** (B) (U)
Chief Executive Officer

**Date of appointment to the Board:**
**5 November 2010**

**Board meeting attendance: 5/5**

**Skills, experience and qualifications:**

Alex Maloney joined Lancashire in December 2005 and was appointed Group Chief Executive Officer in April 2014. On joining, Mr Maloney was responsible for establishing and building the energy underwriting team and account and, in May 2009, was appointed Group Chief Underwriting Officer. Since November 2010, Mr Maloney has served as a member of the Board. Mr Maloney has also been closely involved in the development of the Group's Lloyd's strategy. Mr Maloney has over 20 years' underwriting experience and has also worked in the New York and Bermuda markets.

**Elaine Whelan** (B) (I)
Chief Financial Officer

**Date of appointment to the Board:**
**1 January 2013**

**Board meeting attendance: 5/5**

**Skills, experience and qualifications:**

Elaine Whelan joined Lancashire in March 2006 and leads both the Group finance function and the Bermuda subsidiary, reporting to the Group Chief Executive Officer. Ms Whelan was previously Chief Accounting Officer of Zurich Insurance Company, Bermuda Branch. Prior to joining Zurich, Ms Whelan was an Audit Manager at PricewaterhouseCoopers, Bermuda, where she managed a portfolio of predominantly (re)insurance and captive insurance clients. Ms Whelan graduated from the University of Strathclyde in 1994 with a BA in Accounting and Economics and gained her Chartered Accountancy qualification from the Institute of Chartered Accountants of Scotland in 1997.

**Michael Dawson** (B) (N) (R) (U)
Non-Executive Director

**Date of appointment to the Board:**
**3 November 2016**

**Board meeting attendance: 5/5**

**Skills, experience and qualifications:**

Michael Dawson has more than 35 years' experience in the insurance industry, having started his career at Lloyd's in 1979. He joined Cox Insurance in 1986 where he was the Chief Executive from 1995 to 2002. In 1991, Mr Dawson formed and became the underwriter of Cox's and subsequently Chaucer's specialist nuclear syndicate 1176. Between 2005 and 2008, Mr Dawson was appointed Chief Executive of Goshawk Insurance Holdings PLC and its subsidiary Rosemont Re, a Bermuda reinsurer. Mr Dawson served on the Council of Lloyd's from 1998 to 2001 and on the Lloyd's Market Board from 1998 to 2002.

**External appointments/Other roles:**

Mr Dawson is a Non-Executive Director of Pool Re (Nuclear) Limited and Deputy Chairman of the management committee of Nuclear Risk Insurers Limited.

## Board and Committee membership key

- ● Chair
- (B) Board of Directors
- (A) Audit Committee
- (I) Investment Committee
- (N) Nomination and Corporate Governance Committee
- (R) Remuneration Committee
- (U) Underwriting and Underwriting Risk Committee

* Tom Milligan retired as a Non-Executive Director with effect from 31 March 2018. He attended the Board and Committee meetings for the fourth quarter 2017.

**Simon Fraser** (B) (A) (R)
Senior Independent Non-Executive Director

**Date of appointment to the Board: 5 November 2013**

**Board meeting attendance: 5/5**

**Skills, experience and qualifications:**

Simon Fraser was Head of Corporate Broking at Merrill Lynch and subsequently Bank of America Merrill Lynch until his retirement in 2011. He began his career in the City in 1986 with BZW and joined Merrill Lynch in 1997. He led initial public offerings, rights issues, placings, demergers and mergers and acquisitions transactions during his career and advised many UK companies on stock market and LSE issues. Mr Fraser has an MA degree in Modern History from the University of St Andrews.

**External appointments/ Other roles:**

Mr Fraser is also a Non-Executive Director of Legal and General Investment Management (Holdings) Limited and Senior Independent Director of Derwent London plc, where he sits on the Remuneration, Audit and Nominations Committees. Mr Fraser also serves as a Non-Executive Director of CUL.

**Samantha Hoe-Richardson** (B) (A) (N)
Non-Executive Director

**Date of appointment to the Board: 20 February 2013**

**Board meeting attendance: 5/5**

**Skills, experience and qualifications:**

Samantha Hoe-Richardson has been Chairman of the Audit Committee since 2014. She was Head of Environment & Sustainability for Network Rail and prior to that Head of Environment for Anglo American plc, one of the world's leading mining and natural resources companies. She was also a director and founder of Anglo American Zimele Green Fund (Pty) Ltd, which supports entrepreneurs in South Africa. Prior to her role with Anglo American, Ms Hoe-Richardson worked in investment banking and audit and she holds a masters degree in Nuclear and Electrical Engineering from the University of Cambridge. She also has a Chartered Accountancy qualification.

**External appointments/ Other roles:**

Ms Hoe-Richardson is a Non-Executive Director of Unum Ltd and Unum European Holding Company Ltd. Unum is one of the UK's leading employee benefits providers through the workplace. Ms Hoe-Richardson is also a Non-Executive Director of LUK.

**Robert Lusardi** (B) (A) (I) (R)
Non-Executive Director

**Date of appointment to the Board: 8 July 2016**

**Board meeting attendance: 5/5**

**Skills, experience and qualifications:**

Robert Lusardi spent the first phase of his career as a senior investment banker specialising in the insurance and asset management industries. From 1998 until 2005 he was a member of the Executive Management Board of XL Group plc, first as Group CFO then as a segment CEO; from 2005 until 2010 he was an EVP of White Mountains (an insurance merchant bank) and CEO of certain subsidiaries; and from 2010 to 2015 he was CEO of PremieRe Holdings LLC (a private insurance entity). He has been a director of ten insurance-related entities. He received his BA and MA degrees in Engineering and Economics from Oxford University and his MBA from Harvard University.

**External appointments/ Other roles:**

Mr Lusardi is currently a private investor and has spent his career as a senior executive in the financial services industry. He is also on the boards of Symetra Financial Holdings, Inc., a life insurer, and Oxford University's 501(c)3 charitable organisation.

**Sally Williams** (B) (A) (N)
Non-Executive Director

**Date of appointment to the Board: 14 January 2019**

**Board meeting attendance: N/A**

**Skills, experience and qualifications:**

Sally Williams joined the Marsh Group in 2015 where she served on the board of Marsh Ltd as a director with responsibility for Risk and Governance acting as the main business interface for Marsh Ltd with the FCA. She resigned from her directorships at Marsh with effect from 21 December 2018 and assumed her Non-Executive Directorship of LHL on 14 January 2019.

Ms Williams joined Marsh from National Australia Bank and previously held senior risk positions with Aviva. Ms Williams is a chartered accountant and spent the first 15 years of her career with PricewaterhouseCoopers (PwC), where she was a director specialising in financial services risk management and regulatory relationships. She also undertook a two year secondment from PwC to the Supervision and Surveillance Department at the Bank of England.

**External appointments/ Other roles:**

Ms Williams is a Non-Executive Director of OneFamily, where she is a member of the Audit Committee, Risk Committee and Nominations Committee.

**Christopher Head**
Company Secretary

**Board meeting attendance: N/A**

**Skills, experience and qualifications:**

Christopher Head joined Lancashire in September 2010. He was appointed Company Secretary of LHL in 2012 and advises on issues of corporate governance and generally on legal affairs for the Group. He also advises on the structuring of Lancashire's third-party capital underwriting initiatives which have included the Accordion and Kinesis facilities. Prior to joining Lancashire, he was in-house Counsel with the Imagine Insurance Group, advising specifically on the structuring of reinsurance transactions. He transferred to Max at Lloyd's in 2008 as Lloyd's and London Counsel. Between 1998 and 2006, Mr Head was Legal Counsel at KWELM Management Services Limited, where he managed an intensive programme of reinsurance arbitration and litigation for insolvent members of the HS Weavers underwriting pool. Mr Head is a qualified solicitor having worked until 1998 at Barlow Lyde & Gilbert in the Reinsurance and International Risk Team. Mr Head has a History MA and legal qualification from Cambridge University.

# Our focus during 2018

## Strategy and Capital Management

### February 2018

- Discussion of strategic underwriter recruitment and development initiatives which during the year resulted in the addition of a power team, an onshore energy underwriter and aviation deductible business (see page 23);
- Discussion and approval of the Group's 2018 business plan that had been updated in light of the 1 January 2018 renewals and market conditions; and
- Capital management review and declaration of a final ordinary dividend of $0.10 per common share in respect of the year ended 31 December 2017.

### May 2018

- Review and approval of the Group's UK tax strategy for the year ended 31 December 2018;
- Review and approval of modifications to the Group's investment strategy for 2018/2019;
- Review and discussion of the Group's capital support structures and options; and
- Dedicated strategy sessions (see case study – focus on strategy).

### July 2018

- Consideration and approval of the Group's three-year (2018-2021) strategic plan (see case study – focus on strategy);
- Consideration and approval of the Group's 2018 reforecast business plan in light of actual experience to 30 June 2018;
- Consideration and approval of a modification to the description of the Group's strategic RoE target key performance indicator (see page 11); and
- Capital management review and declaration of an interim dividend of $0.05 per common share.

### October 2018

- Consideration and approval of the Group's 2019 business plan; and
- Capital management review and declaration of a special dividend of $0.20 per common share.

### Case Study – Focus on strategy

The objective of the 2018 strategy sessions held in May 2018 was to consider the key decisions to be made in the preparation of the Group's three-year strategic plan. The issues discussed included:

- review of the current strategy;
- consideration of its continued relevance and the views of shareholders;
- review of the Group's underwriting lines of business and potential options and opportunities;
- consideration of areas of opportunity in particular in international and specialty markets;
- analysis of the structures and tools used within the third-party reinsurance capital sector and related strategic opportunities;
- review of the Group's investment strategy and options;
- consideration of the Group's regulatory domicile and its interaction with strategic initiatives; and
- review of the business's resourcing and training needs.

At its July 2018 meetings the Board approved the Group's three-year strategic plan including the Group's risk appetites and capital and solvency appetites.

## Risk

### February 2018

- Review and approval of the revised anti-money laundering and financial crime, whistleblowing and conflicts of interest policies and procedures;
- Approval of the updated UK and U.S. regulatory and tax operating guidelines for the Group;
- Review and approval of the revised underwriting exposure risk tolerances (see page 33); and
- Consideration of risk reports from the Group CRO.

### May 2018

- Review and approval of the Solvency II submissions as at 31 December 2017 for submission to the PRA;
- Review and approval of the revised sanctions policy and procedures; and
- Consideration of risk reports from the Group CRO.

### July 2018

- Consideration of risk reports from the Group CRO; and
- Review and approval of the Group's risk, capital and solvency appetites as part of strategic planning.

### October 2018

- Consideration of risk reports from the Group CRO including special focus on Brexit planning and climate change risk management.

## Succession and Remuneration

### February 2018

- Consideration and approval of a range of changes and appointments to the boards and management teams of the operating businesses within the Group;
- Review and approval of the Group's 2018 framework for executive remuneration; and
- Approval of the Directors' Remuneration Report within the 2017 Annual Report and Accounts, for approval by shareholders at the 2018 AGM.

### May 2018

- Review and approval of the Group's succession plan and talent management and development programme for 2018/2019; and
- Consideration and approval of a range of changes and appointments to the boards and management teams of the operating businesses within the Group.

### July 2018

- Consideration and approval in principle of the appointment of Sally Williams as a Non-Executive Director of LHL to take effect during January 2019 further to a determination that she should be considered to be independent in character and judgement (see page 55); and
- Consideration and approval of a range of changes and appointments to the boards and management teams of the operating businesses within the Group.

### October 2018

- Consideration and approval of a modified Group Solvency II Identified Staff Remuneration policy;
- Consideration and approval of a resolution to issue up to 600,000 common shares in satisfaction of obligations under the RSS; and
- Consideration and approval of a range of changes and appointments to the boards and management teams of the operating businesses within the Group.

## Financial Reporting and Controls

### February 2018

- Review and approval of the fourth quarter 2017 financial supplement; and
- Approval of the 2017 Annual Report and Accounts further to the report from the Audit Committee.

### May 2018

- Review and approval of the first quarter 2018 financial supplement; and
- Discussion of the 2017 audit process and review of KPMG's 2018 audit plan.

### July 2018

- Review and approval upon recommendation by the Audit Committee of the interim consolidated financial statements; and
- Review and approval of the second quarter 2018 financial supplement.

### October 2018

- Approval of a press release in respect of the Group's preliminary loss estimates from marine account losses and the U.S. and Pacific windstorm losses; and
- Review and approval of the third quarter 2018 financial supplement.

## Stakeholder Engagement and Corporate Governance Matters

### February 2018

- Review and approval of the Group's disclosure procedures;
- Review and approval of an updated diversity policy statement, further to a recommendation from the Nomination and Corporate Governance Committee;
- Review and approval of an updated policy statement on anti-slavery and human trafficking;
- Formal consideration of the independence of all Non-Executive Directors prior to the 2018 AGM;
- Discussion of the 2017 year end Board and Committee performance appraisal feedback and recommendations; and
- Consideration and approval of the draft 2018 AGM notice and the matters to be put to shareholders.

### May 2018

- Review and approval of a modification to the Investment Committee Terms of Reference;
- Discussion of a presentation from the Group's corporate brokers;
- Approval of the appointment of a new Trustee to the Lancashire Foundation; and
- The Company's 2018 AGM was held at its London office on 2 May 2018. All resolutions were duly passed and approved by shareholders.

### July 2018

- Discussion of the PRA's 'Dear CEO' letter concerning a request to all boards operating within the insurance industry to explain the management of "soft market" risks;
- Review and discussion of the Group's regulatory supervision options; and
- Review and approval of an updated diversity policy statement, further to a recommendation from the Nomination and Corporate Governance Committee.

### October 2018

- Consideration and approval of the process for the annual performance evaluation of the Board and its Committees and individual Directors, to be facilitated by Lintstock; and
- Consideration and approval of a special purpose committee to facilitate the migration of Group insurance supervision and tax domicile to Bermuda to take effect on 1 January 2019.

### December 2018

- Review and approval by the migration special purpose committee of revised UK and U.S. tax and regulatory operating guidelines to be used by the Group with effect from 1 January 2019.

# Board Committees

## Board and Committee administration

The Board of Directors is responsible for the leadership and control and the long-term success of Lancashire's business. The Board has reserved a number of matters for its decision, including responsibility for setting the Group's values and standards, and approval of the Group's strategic aims and objectives. The Board has delegated certain matters to Committees of the Board, as described below. Copies of the Schedule of Board-Reserved Matters and Terms of Reference of the Board Committees are available on the Company's website at www.lancashiregroup.com.

The Board has approved and adopted a formal division of responsibilities between the Chairman and the CEO. The Chairman is responsible for the leadership and management of the Board and for providing appropriate support and advice to the CEO. The CEO is responsible for the management of the Group's business and for the development of the Group's strategy and commercial objectives. The CEO is responsible, along with the executive team, for implementing the Board's decisions.

The Board and its Committees meet on at least a quarterly basis. At the regular quarterly Board meetings, the Directors review all areas of the Group's business and receive reports from management on underwriting, reserving, finance, investments, capital management, internal audit, risk, legal and regulatory developments, compliance and other matters affecting the Group. Management provides the Board with the information necessary for it to fulfil its responsibilities. In addition, presentations are made by external advisers such as the independent actuary, the investment managers, the external auditors, the remuneration consultants and the corporate brokers. The Board Committees are authorised to seek independent professional advice at the Company's expense.

The Board also meets to discuss strategic planning matters in addition to the customary schedule of quarterly meetings. A dedicated Board strategic planning day was held in May 2018.

The Chairman holds regular meetings with the Non-Executive Directors, without the Executive Directors present, to discuss a broad range of matters affecting the Group.

## The Directors

Appointments to the Board are made on merit, against objective criteria and with due regard for the benefits of diversity on the Board, including gender. The Board considers all of the Non-Executive Directors to be independent within the meaning of the Code.

Michael Dawson, Simon Fraser, Samantha Hoe-Richardson and Robert Lusardi are independent, as each is independent in character and judgement and has no relationship or circumstance likely to affect his or her independence. Peter Clarke was independent upon his appointment as Chairman on 4 May 2016.

In relation to the determination of independence of Sally Williams, in a Board meeting held on 10 July 2018, the Directors considered that, by virtue of her directorships of Marsh Limited and certain other subsidiaries within the Marsh Group and her employment as a senior executive of the Marsh Group, these were circumstances which for purposes of the Code should be considered to be a 'material business relationship' requiring special consideration within the context of the determination of a Director's independence. The Board concluded that it was appropriate for the Directors to use their discretion in the light of these facts to determine whether Sally Williams was indeed independent in character and judgement. After lengthy and detailed discussion of these matters the Directors concluded that there was no question in their minds but that, subject to the service of her notice of resignation from the Marsh Group, which was confirmed on 19 July 2018, Sally Williams was to be considered as and would continue to be independent in character and judgement in her role as a Director of the Company. Sally Williams assumed her role as a Director of the Company on 14 January 2019.

At the Board meeting held on 13 February 2019, further to a recommendation by the Nomination and Corporate Governance Committee, the Board affirmed its judgement that five of the eight members of the Board are independent Non-Executive Directors. Therefore, in the Board's judgement, the Board's composition complies with the Code requirement that at least half the Board, excluding the Chairman, should comprise Non-Executive Directors determined by the Board to be independent.

In accordance with the provisions of the Company's Bye-laws and the Code, all the Directors are subject to re-election annually at each AGM.

## Information and training

On appointment, the Directors receive written information regarding their responsibilities as Directors and information about the Group. An induction process is tailored for each new Director in the light of his or her existing skill set and knowledge of the Group, and includes meeting with senior management and visiting the Group's operations. Information and advice regarding the Company's official listing, legal and regulatory obligations and on the Group's compliance with the requirements of the Code is also provided on a regular basis. An analysis of the Group's compliance with the Code is collated and summarised in quarterly reports together with a more general summary of corporate governance developments, which are prepared by the Group's legal and compliance department for consideration by the Nomination and Corporate Governance Committee. The Directors have access to the Company Secretary who is responsible for advising the Board on all legal and governance matters. The Directors also have access to the Group General Counsel and independent professional advice as required. Regular sessions are held between the Board and management as part of the Company's quarterly Board meetings, during which in-depth presentations covering areas of the Group's business are made. During these presentations the Directors have the opportunity to consider, challenge and help shape the Group's commercial strategy. The Directors are also encouraged to seek supplementary know-how training suitable to their roles offered by the many external providers of training pertinent to governance and in particular the roles of non-executive directors and to consider their training needs and priorities as part of the year end performance evaluation for the Board and Committees.

## Board performance evaluation

A formal performance evaluation of the Board, its Committees and individual Directors is undertaken on an annual basis and the process is initiated by the Nomination and Corporate Governance Committee. The aim of this work is to assess the effectiveness of the Board and its Committees in terms of performance and risk oversight, strategic development, composition, supporting processes and management of the Group. The evaluation is forward-looking in terms of identifying the strategic priorities as well as considering performance, training and development needs for the Directors within the context of the work of each Committee and that of the Board. The 2017 evaluation was conducted internally and facilitated by the Company Secretary and the Chairman and the 2018 performance evaluation process was facilitated by Lintstock Limited, a London-based corporate advisory firm with no other connection to the Group.

The 2018 evaluation process involved each Director as well as the Company Secretary, the Group CRO, Group General Counsel and other members of senior management completing a questionnaire designed, in consultation with Lintstock, by the LHL Chairman and the Company Secretary with input from the Chairs of each of the relevant Committees. Responses to the completed questionnaires were collated by Lintstock, which then held a series of individual interviews with each of the Directors, the Company Secretary, the Group General Counsel and the Group CRO to explore emerging themes. Lintstock then prepared a suite of anonymised summary reports that were discussed in draft with the Board Chairman and Committee Chairs before being distributed to each of the Directors.

In February 2019, the performance evaluation reports were discussed at meetings of the Nomination and Corporate Governance Committee and the Board, and each of the other Committees discussed the report pertinent to its own operation and performance. The Board discussions were led by the Chairman and focused on such matters as strategic oversight, succession planning, Board composition and training and priorities for 2019.

In summary, in the Board's consideration of the 2018 evaluation reports, the Board concluded that it operates effectively and has a good blend of insurance, financial and regulatory expertise. All Non-Executive Directors are committed to the continued success of the Group and to making the Board and its Committees work effectively. Attendance at Board meetings was found to be excellent. The Group CEO and the Group CFO, the Company's Executive Directors, were also found to be operating effectively.

Appropriate infrastructure, processes and governance mechanisms are in place to support the effective performance of the Board and its Committees. The Board is considered to manage risk effectively. The number of Directors on the Board is considered to be appropriate.

It was noted in the evaluation process that, in what had been another challenging year for the (re)insurance markets, the Board and Committee oversight of underwriting strategy and risk tolerances had operated effectively and within expectations. Engagement between the Board and the wider body of staff is considered to be generally strong and beneficial to the operation of the business. It was concluded that the Board discussion around the regulatory and tax domicile for the Group had been well focused and effective and had resulted in the implementation of the decision to move Group management and supervision to Bermuda in a timely manner. Looking ahead, the Board and Committees will, during the course of 2019, seek to ensure that the Group holds sufficient capital and utilises capital tools to ensure that the business is well-placed to be a leading (re)insurance market. The Board is also committed to underwriting those specialty insurance lines in which the business has expertise and to support management in the identification of new and complementary underwriting classes with a view to achieving controlled organic premium growth where this makes sense. The Board also highlighted a number of themes which will inform the business of the Board during 2019 including the attributes required for a future non-executive appointment to the Board and the ongoing need to ensure a strong succession plan to meet the requirements of the business. A number of practical steps to optimise the focus of Board and Committee meetings were also identified for action.

The Board will continue to review its procedures, training requirements, effectiveness and development during 2019.

The Chairman's performance appraisal was conducted by the Senior Independent Director, who consulted with the Non-Executive Directors with input from the Executive Directors during July 2018. The discussion and feedback were positive regarding the Chairman's performance. Particular reference was made to the strong lines of communication which the Chairman has fostered with the Chairs of the subsidiary boards and the executive team. The Chairman's insight and strategic and high-level leadership of the Board were also noted.

Following the year end, the Chairman met with the Group CEO, and the Group CEO met with the Group CFO, to conduct a performance appraisal in respect of 2018 and to set targets for 2019. The results of these performance evaluations were discussed by the Chairman and the Non-Executive Directors and are reported in the Directors' Remuneration Report commencing on page 70.

## Relations with shareholders

During 2018, the Group's Head of Investor Relations, usually accompanied by one or more of the Group CEO, the Group CUO, the Group CFO, the Chairman or a senior member of the underwriting team, made presentations to major shareholders, analysts and the investor community. Formal reports of these meetings were provided to the Board on at least a quarterly basis. During the year the Board oversaw the transition to the appointment of a new Head of Investor Relations. Jelena Bjelanovic assumed that role in October 2018 and made her first presentation to the Board at the third quarter 2018 Board meeting.

The Chairman of the Remuneration Committee conducted a consultation with the significant shareholders of the Group with regard to remuneration policy and practice in advance of the production of the Directors' Remuneration Report in the 2017 Annual Report and Accounts and the 2018 AGM and again during January 2019, to seek feedback on the Group's implementation of remuneration policy.

Conference calls with shareholders and analysts hosted by senior management are held quarterly following the announcement of the Group's quarterly financial results. The Group CEO, Group CUO and Group CFO are generally available to answer questions at these presentations.

Shareholders are invited to request meetings with the Chairman, the Senior Independent Director and/or the other Non-Executive Directors by contacting the Group Head of Investor Relations. All of the Directors are expected to be available to meet with shareholders at the Company's 2019 AGM.

The Company commissions regular independent shareholder analysis reports together with independent research on feedback from shareholders and analysts following the Company's results' announcements. This research, together with the analysts' notes, is made available to all Directors.

## Enterprise Risk Management

The Board is responsible for setting the Group's risk appetites, defining its risk tolerances, and setting and monitoring the Company's risk management and internal control systems including compliance with risk tolerances. During 2018 the Board carried out a robust assessment of the principal risks affecting the Group's business model, future performance, solvency and liquidity and the operation of internal control systems.

Further discussion of the risks affecting the Group and the policies in place to manage them can be found in the ERM section of this report on pages 33 to 39 and in the risk disclosures section on pages 111 to 133.

Each of the Committees is responsible for various elements of risk (see the various Committee reports from page 58 to page 69 for further detail). The Group CRO reports directly to the Group and subsidiary boards and facilitates the identification, evaluation, quantification and control of risks at a Group and subsidiary level. The Group CRO provides regular reports to the Group and subsidiary boards covering, amongst other things, actual risk levels against tolerances, emerging risks, any lessons learned from risk events and assurance provided over key risks. During 2018, the Directors participated in a number of training sessions addressing the Board's obligations under Solvency II and, in particular, with regard to the review and approval of the Solvency II submissions as at 31 December 2017 for submission to the PRA. The Board considers that a supportive ERM culture, established at the Board and embedded throughout the business, is of key importance. The facilitating and embedding of ERM and helping the Group to improve its ERM practices are a major responsibility assigned to the Group CRO. The Group CRO's remuneration is subject to annual review by the Remuneration Committee. The Board is satisfied that the Company's risk management and internal control systems have operated effectively for the year under review.

## Committees

The Board has established Audit, Investment, Nomination and Corporate Governance, Remuneration, and Underwriting and Underwriting Risk Committees. Each of the Committees has written Terms of Reference, which are reviewed regularly and are available on the Company's website. The Committees' Terms of Reference were reviewed by the Board during 2018 and were considered to be in line with current best practice. The Committees are generally scheduled to meet quarterly, although additional meetings and information updates are arranged as business requirements dictate. Director attendance at the 2018 Board meetings is set out on pages 50 to 51. A report from each of the Committees, which covers Committee attendance, is set out from page 58 to page 69.

# Audit Committee

**Samantha Hoe-Richardson**
Chairman of the Audit Committee

**"During 2018, the focus of the Committee has been on the adequacy of the Group's loss reserves, as well as monitoring the effectiveness of both the external auditors and the internal audit programme and ensuring the continued integrity of the Group's financial reporting. In particular, the Committee has monitored the Group's preparations for the implementation of the IFRS 17 ('Insurance Contracts') accounting standard."**

## Committee membership

The Audit Committee comprises four independent Non-Executive Directors and is chaired by Samantha Hoe-Richardson, a qualified accountant. The Board considers that the four independent Non-Executive Directors all have recent and relevant financial experience. The Audit Committee as a whole has competence in the specialty insurance and reinsurance sectors. The internal and external auditors have the right of direct access to the Audit Committee. The Audit Committee's detailed Terms of Reference are available on the Group's website.

| | Meetings attended |
|---|---|
| Samantha Hoe-Richardson (Chairman) | 4/4 |
| Simon Fraser | 4/4 |
| Robert Lusardi | 4/4 |
| Sally Williams[1] | n/a |

1. Sally Williams was appointed as a member of the Audit Committee with effect from 12 February 2019.

## Principal responsibilities of the Committee

- Financial reporting: monitors the integrity of the consolidated financial statements of the Group and any other formal statements relating to its financial performance, including the annual Solvency II Group reporting requirements. Reviews and reports to the Board on significant financial reporting issues and judgements that those statements contain. Reviews the Annual Report and Accounts and advises the Board on whether, taken as a whole, it is fair, balanced and understandable;
- External audit: oversees the relationship with the external auditors and is responsible for the annual assessment of their independence and objectivity. Makes a recommendation to the Board, to be put to shareholders for approval at the AGM, for the appointment of the Company's external auditors;
- Internal audit: monitors and reviews the effectiveness of the Group's internal audit function ensuring it has unrestricted scope, the necessary resources and access to information to enable it to fulfil its mandate in accordance with appropriate professional standards; and
- Internal controls and risk management systems: oversight of internal controls and risk management systems. Reviews the Group's 'whistleblowing' and other systems and controls for the prevention of fraud, bribery and money laundering.

## How the Committee discharged its responsibilities during 2018

### Financial reporting

| Committee responsibility | Committee activities |
|---|---|
| Monitors the integrity of the Group's consolidated financial statements, including its annual and half-yearly reports, annual Solvency II Group Pillar 3 reports, interim management statements and any other formal statements relating to the Group's financial performance. Reports to the Board on significant financial reporting issues and judgements contained in the consolidated financial statements. | At each quarterly meeting the Committee reviews the Group's quarterly consolidated financial statements for the purposes of recommending their approval by the Board. The Group's annual Solvency II Pillar 3 reports were reviewed at the April 2018 Audit Committee meeting prior to recommendation of their approval at the May 2018 Board meeting. The Committee also monitors the activities of the Company's Disclosure Committee and reviews the Group's quarterly financial press releases, which it recommends to the Board for approval. The Committee receives quarterly reports from management on:<br>• developments in accounting and financial reporting requirements;<br>• any new and/or significant accounting treatments/transactions in the quarter;<br>• the activities of LHL's subsidiary companies, including consideration of any risk issues;<br>• loss reserving (see page 107 for further details);<br>• the progress of the Group's IFRS 9 and IFRS 17 implementation project and the related enhancements to the Group's finance IT framework and move to a common Group general ledger; and<br>• the Committee also receives quarterly reports on the consolidated financial statements from the external auditors, including an interim review report and a year-end full audit report. These are discussed with the external auditors at the Committee meetings.<br><br>**Judgements and estimation in the consolidated financial statements**<br>An annual paper is presented by management to the Committee that details the areas of judgement and estimation in the preparation of the consolidated financial statements (see accounting policies (page 105) for the details of these areas). Of these, the most significant area of estimation and judgement considered by the Committee during 2018 was the estimation of ultimate loss reserves. The Audit Committee's quarterly review of the adequacy of the loss reserves is explained in detail on page 62.<br><br>The Group has two indefinite life intangible assets following the acquisition of Cathedral – goodwill and syndicate participation rights. Intangible assets with indefinite useful lives are subject to an impairment review at least annually, or sooner if there is an indication of impairment. Some of the key inputs in the impairment review are based on management judgement and/or estimation (see page 105 of the consolidated financial statements for further details). These inputs are reviewed by the Audit Committee annually and are considered reasonable. The Audit Committee also considers the Group's internal stress tests and what stress scenarios would have to occur to indicate an impairment of its intangible assets. As a result of these considerations the Audit Committee agreed with management and KPMG that there was no impairment of the Group's intangible assets.<br><br>In accordance with auditing guidance, KPMG's year-end audit report identified revenue recognition through the estimation of premium revenues as an area of significant risk. The Audit Committee considered this and concluded that, whilst some premiums are subject to estimation, revenues are unlikely to be materially different from initial estimates, particularly on a consolidated Group basis. |
| Reviews the content of the Annual Report and Accounts and advises the Board on whether, taken as a whole, it is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy. | The Chairman of the Committee reviewed the early drafts of the 2018 Annual Report and Accounts in order to keep apprised of its key themes and messages. The Committee reviewed the final draft of the Annual Report and Accounts at the February 2019 Audit Committee meeting together with the external auditor's report. The Committee advised the Board that, in its view, the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy. |

## External audit

| Committee responsibility | Committee activities |
|---|---|
| Oversees the relationship with the Group's external auditors, approves their remuneration and terms of engagement, and assesses annually their independence and objectivity taking into account relevant legal, regulatory and professional requirements and the Group's relationship with the external auditors as a whole. This includes an annual assessment of the qualifications, expertise and resources, and independence of the external auditors and the effectiveness of the external audit process. | The Committee approves the annual external audit plan and receives reports from the external auditors at each quarterly Committee meeting, including an ongoing assessment of the effective performance of the audit compared to the plan. The Committee Chairman conducts informal meetings with the external auditors and the Group CFO prior to, during, and after the review of the quarterly results. The Committee meets quarterly in executive session with the external auditors to discuss any issues arising from the audit, and with management to obtain feedback on the audit process. Following the completion of KPMG's first year of provision of external audit services for the financial year ending 31 December 2017, the Committee Chairman led a thorough and formal review process to consider the effectiveness of the external audit process. This sought constructive feedback from stakeholders across the organisation and included an assessment of the qualifications, expertise and resources, and independence of KPMG. The results of the review were discussed at the April 2018 meeting, where it was concluded that the external audit process was operating effectively both with respect to the service provided by KPMG and management's support of the audit process. Areas of the audit process identified as benefiting from further development included the overall audit planning process and more effective communication between KPMG and the Group finance team. At its February 2019 meeting, the Committee discussed with KPMG an Audit Quality Review (AQR) report produced by the FRC on KPMG's 2017 audit of the Group. The Committee discussed areas for process enhancements with KPMG in relation to the FRC AQR findings. It was the Committee's view that the issues raised by the FRC were procedural rather than substantive in nature. A further review of auditor independence was conducted in February 2019 and the Committee concluded that the external auditors are independent and objective. |
| The development and implementation of a formal policy on the provision of non-audit services by the external auditors, taking into consideration any threats to the independence and objectivity of the external auditors. | The Committee has approved and adopted a formal non-audit services policy that is reviewed on an annual basis and was last reviewed and approved in October 2018. The policy, which stipulates the approvals required for various types of non-audit services that may be provided by the external auditors, is on the Group's website. During 2018, KPMG provided non-audit services in relation to U.S. tax advisory work. Fees for non-audit services provided in 2018 totalled $15,000. The Committee gave careful consideration to the nature of the non-audit services provided and the level of fees charged, and has determined that they do not affect the independence and objectivity of KPMG as auditors. |
| Makes a recommendation to the Board, to be put to shareholders for approval at the AGM, in relation to the appointment, re-appointment or removal of the Group's external auditors. | Following a competitive external audit tender process undertaken during 2016, the appointment of KPMG as external auditors was first approved by shareholders at the 2017 AGM. Accordingly, the 2018 financial year was the second financial year in which KPMG acted as the Company's external auditors, following KPMG's re-appointment at the 2018 AGM further to a recommendation from the Committee and the full Board. The lead audit partner is Rees Aronson. The Committee and the Board are recommending the re-appointment of KPMG as external auditors at the 2019 AGM. The Committee has noted the reports from the Kingman review regarding the role of the FRC and related proposals for reform, and the UK Competition and Markets Authority report concerning the market for audit services, and will continue to monitor these, and related, developments. |

## Internal audit

| Committee responsibility | Committee activities |
|---|---|
| Monitors and reviews the effectiveness of the Group's internal audit function in the overall context of the Group's risk management system. | The Group's internal audit function reports directly to the Committee. Each year, the Group Head of Internal Audit presents an annual internal audit strategy and plan to the Committee for consideration and approval. In general, the most significant business risks and controls are usually considered for audit annually whilst less critical risks are audited periodically as part of a flexible multi-year programme. The findings of each audit are reported to the Committee at the quarterly meetings and the Committee reviews the actions taken by management to implement the recommendations of internal audit. The Committee meets in executive session with the Group Head of Internal Audit usually on a quarterly basis.<br><br>During 2018, the Committee reviewed and approved an updated Internal Audit Charter. This can be viewed on the Group's website. The Group CRO undertook an annual review of the implementation of the internal audit programme during 2018 to ensure its continued efficiency and appropriate standing within the Group and the effectiveness of the internal audit function. The Committee discussed the report and its findings with the Group CRO and the Group Head of Internal Audit and concluded that the internal audit function is operating effectively in the overall context of the Group's risk management system. The Committee Chairman oversaw the process for the appointment of a new Group Head of Internal Audit and the transitional internal audit management arrangements. Samantha Churchill joined the Group as the new Group Head of Internal Audit during January 2019. |

## Internal controls and risk management systems

| Committee responsibility | Committee activities |
|---|---|
| Reviews the adequacy and effectiveness of the Group's internal financial controls systems that identify, assess, manage and monitor financial risks, and other internal control and risk management systems; and reviews and approves the statements to be included in the Annual Report and Accounts concerning internal control, risk management and the viability statement. | The Board has ultimate responsibility for ensuring the maintenance by the Group of a robust framework of internal control and risk management systems, and has delegated the monitoring and review of these systems to the Committee. The system of internal controls is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss. The Committee receives from the Group CRO periodic reports detailing results of the quarterly risk and control affirmation review. The Committee receives from the Group Head of Internal Audit an annual assessment of the Group's governance, risk and control framework together with an analysis of themes and trends from the internal audit work and their impact on the Group's risk profile. In 2018, the Committee and Board were satisfied that the governance, risk and control framework remains effective and appropriate for the Lancashire Group. |
| Reviews for adequacy and security the Group's compliance, 'whistleblowing' and fraud controls. | During 2018, the Committee conducted an annual review of the Group's policies and procedures relevant to financial controls and recommended the adoption by the Board of updated policies and procedures in respect of anti-money laundering, bribery and financial crime (including fraud), conflicts of interest and whistleblowing. There were no suspicious transactions or whistleblowing reports made during the year (whether arising from suspected money laundering activity or knowledge of, suspicion or concern relating to suspected acts of bribery or any other type of financial crime, dishonesty or impropriety). The Committee also keeps under review the adequacy and effectiveness of the Group's legal and compliance function. |

## Significant area of judgement or estimation

### Loss reserves and expenses

As detailed on pages 117 to 118 of the consolidated financial statements, the estimation of ultimate loss reserves is a complex actuarial process that incorporates a significant amount of judgement. The Committee considers the adequacy of the Group's loss reserves at each Audit Committee meeting, for which purpose it receives quarterly reports from the Group's Reserving Actuary. KPMG conduct a high-level review of the Group's loss reserves as part of their first and third quarter review procedures. The Committee also receives estimates of the Group's ultimate loss reserves from an external independent actuary and from KPMG and compares these third-party estimates to those of the Group at its second and fourth quarter Audit Committee meetings. During 2018, the Committee focused its discussions around the Group's loss reserves on: the range of reasonable actuarial estimates and the difference between the Group's and the independent review from external actuaries (these differences being viewed by management, the external third parties and the Committee to be within a reasonable actuarial range); current and prior year loss development including 'back-testing' of the Group's prior year reserves; and reserving for each insurance operating subsidiary. Having reviewed and challenged these areas, the Committee concurred with management's valuation of the Group's loss reserves and the relevant disclosures around loss reserving in the Group's consolidated financial statements.

## Priorities for 2019

The Committee's key priorities for 2019 are:

- To ensure the continued effectiveness of the Group's control environment, the operation of the business's financial reporting systems and the integrity of external financial reporting; and
- To continue to monitor the preparation by the Group for the implementation of IFRS 9 and IFRS 17.

## IFRS 17, Insurance Contracts

In 2017 the IASB issued IFRS 17 ('Insurance Contracts'), which was to be mandatorily effective for annual reporting periods beginning on or after 1 January 2021. However, at its board meeting on 14 November 2018, the IASB tentatively decided to propose an amendment of the IFRS 17 effective date to reporting periods beginning on or after 1 January 2022. If the proposed deferral of IFRS 17 is accepted, the implementation of IFRS 9 ('Financial Instruments: Classification and Measurement'), will also be deferred to this date for companies whose prominent activity is the issuance of insurance contracts. During 2018, the Committee monitored on a quarterly basis the preparation by the Group for the implementation of IFRS 9 and IFRS 17. This project encompasses changes to the Group's finance IT framework and general ledger, as well as the presentation of the Group's financial statements on an IFRS 9 and IFRS 17 basis. The prospective deferral of the implementation date for the standard has not had a significant impact on the Group's implementation project timetable.

# Nomination and Corporate Governance Committee

**Peter Clarke**
Chairman of the Nomination and Corporate Governance Committee

**"During 2019, the Committee will keep under review the Group's corporate governance reporting to ensure that the Company is able to discharge effectively its governance responsibilities under the 2018 Code."**

## Committee membership

A majority of the members of the Nomination and Corporate Governance Committee are independent Non-Executive Directors. The Committee Chairman is Peter Clarke, who is the Chairman of the Board.

| | Meetings attended |
|---|---|
| Peter Clarke (Chairman) | 4/4 |
| Michael Dawson | 4/4 |
| Samantha Hoe-Richardson | 4/4 |
| Tom Milligan[1] | 1/1 |
| Sally Williams[2] | n/a |

1. Tom Milligan retired as a member of the Nomination and Corporate Governance Committee with effect from 31 March 2018.
2. Sally Williams was appointed as a member of the Nomination and Corporate Governance Committee with effect from 12 February 2019.

## Principal responsibilities of the Committee

- Reviews the structure, size and composition (including the skills, knowledge, independence, experience and diversity) of the Board;
- Considers succession planning for Directors and other senior executives;
- Nominates candidates to fill Board vacancies;
- Makes recommendations to the Board concerning Non-Executive Director independence, membership of Committees, suitable candidates for the role of Senior Independent Director, and the re-election of Directors by shareholders;
- Reviews the Company's corporate governance arrangements and compliance with the Code; and
- Makes recommendations to the Board concerning the charitable and corporate social responsibility activities of the Company and donations to the Lancashire Foundation.

## How the Committee discharged its responsibilities during 2018

### Board composition

The Committee reviewed the composition of the Board to ensure that the balance of skills, knowledge, independence, experience and diversity continues to be appropriate for the Group's business to meet its strategic objectives. The Committee also considered whether any additional skills and experience were needed to complement those already on the Board.

In this regard, the Committee engaged the Eliot Partnership, an executive search firm that has no other connection to the Group. They identified a number of potential candidates, including Sally Williams, who in July 2018 was appointed as a Non-Executive Director of the Company which took effect on 14 January 2019. In this regard, please see page 55 for a discussion relating to the Board process followed on the determination of the independence of Sally Williams. In accordance with the provisions of the Code, all of the Directors are subject to annual (re)election by shareholders. With the exception of Tom Milligan, who retired from the Board on 31 March 2018, all of the Directors were re-elected by shareholders at the 2018 AGM.

### Succession planning

The Committee reviewed and recommended the approval and adoption by the Board of the Company's succession plan and talent management and development programme 2018/2019. The Committee also continued to focus in its dialogue with management on training and development initiatives for key employees across the Group. During 2018, there were a number of planned promotions within the risk management, modelling and actuarial, and underwriting teams.

## Subsidiary boards

The Committee monitored the composition of subsidiary boards during 2018 and recommended appointments to the boards of CUL, LICL and KCML. The Committee also recommended the appointment of Simon Fraser as Chairman of the CUL Remuneration and Nomination Committee.

## Corporate governance

The Committee keeps under review the Company's corporate governance, particularly compliance with the Code, and is responsible for making recommendations to the Board concerning the process for conducting and facilitating the annual performance evaluation of the Board, its Committees and the individual Directors (see page 56).

During 2018, the Committee noted the publication by the FRC of the 2018 Code and reviewed with management the detailed changes made to the Code. The Committee will review the Company's compliance with the 2018 Code from the beginning of 2019 for the purpose of reporting in the Company's 2019 Annual Report and Accounts.

During 2018, the Company continued the practice of the Group CEO holding 'town hall' meetings with employees following the announcement of the Company's quarterly results. The Committee has discussed plans for certain of these meetings to be attended by the Chairman of the Board or another Non-Executive Director during 2019 and to further enhance arrangements for engagement between the Directors and members of the workforce.

During 2018, the Committee recommended the approval and adoption by the Board of amended and restated Terms of Reference of the Investment Committee, a copy of which is posted on the Company's website.

The Committee considered statistics relevant to the gender composition of the Board, Group management excluding LHL Non-Executive Directors, and overall Group employees. These statistics are shown opposite. The Committee also reviewed 2018 comparative pay data by gender within the Lancashire Group.

The Committee recommended approval by the Board of an updated diversity policy, which is posted on the Company's website. The Board remains of the view that the skills and experience needed to take the business of the Company forward are of paramount importance in selecting Board members and employees.

Lancashire's approach to recruitment and ensuring the benefits of a broad diversity throughout the business is discussed further on page 41 in the discussion of the workplace culture.

During 2018, the Committee recommended the approval by the Board of an updated Anti-Slavery and Human Trafficking statement, a copy of which is posted on the Company's website.

## The Lancashire Foundation

The Committee is responsible for monitoring and making recommendations to the Board in relation to the Company's charitable giving policy and the operation of, and reporting requirements for, the Lancashire Foundation. During 2018, the Committee received a report on the Foundation, including its objectives, governance, approach to funding for 2018 and beyond, investment strategy, donations policy and charitable activities, and considered the ways in which the Foundation engages with employees throughout the Group. The Committee made a recommendation to the Board that the Company make a donation to the Foundation of $0.5 million for 2019.

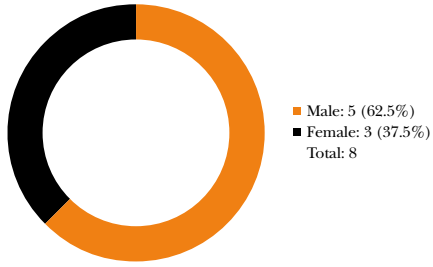
The Committee recommended the appointment by the Board of Emma Hill (a LUK Terrorism, War & Political Risks underwriter) as a Trustee of the Foundation. The Committee also recommended the approval by the Board of some amendments to the Foundation's Trust Deed.

## Priorities for 2019

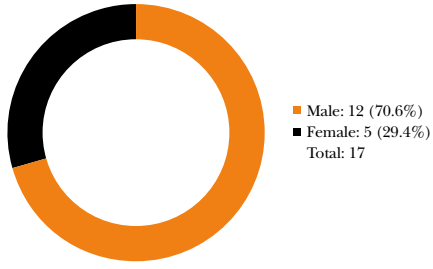
The Committee's key priorities for 2019 are:

- To ensure that the Company is able to discharge effectively its governance responsibilities under the 2018 Code;
- To continue to develop the succession plans for Directors and senior executives, in line with the Group's strategic objectives, and to support management in the development of the talent pipeline; and
- To monitor the Company's progress on gender diversity and other diversities.

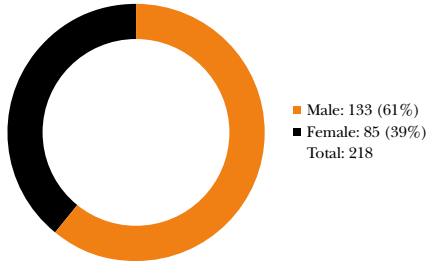
### LHL Board members




### Group management excluding LHL Non-Executive Directors




### Overall Group employees




The gender composition data reflecting LHL Board members is reported as at the date of this Annual Report and Accounts. The gender split of males to females on the LHL Board as at 31 December 2018 was five males (71.4 per cent)/two females (28.6 per cent). All other gender composition data is shown as at 31 December 2018.

# Investment Committee

**Robert Lusardi**
Chairman of the Investment Committee

**"Returns on Lancashire's investment portfolio are an integral part of the income generated for our shareholders. Our investment philosophy is designed to complement and support our underwriting strategy, reflect the current market conditions and include liquidity constraints based on PMLs and potential claim exposures. During 2018, the Group continued to maintain a defensive short duration profile during a year in which we have seen rising interest rates. We also seek to hold a diversified portfolio to manage and mitigate the effect of interest rate risk."**

## Committee membership

During 2018, the Terms of Reference of the Investment Committee were amended to provide that the Committee shall comprise at least two Non-Executive Directors (one of whom may be the Chairman of the Board) and the Group CFO and/or the Group CIO. Any Executive Director may also serve on the Committee. The Terms of Reference are posted on the Company's website.

The Investment Committee comprises one independent Non-Executive Director, the Chairman of the Board, one Executive Director (the Group CFO) and the Group CIO (who is not a Director).

| | Meetings attended |
|---|---|
| Robert Lusardi (Chairman) | 4/4 |
| Peter Clarke | 4/4 |
| Tom Milligan[1] | 1/1 |
| Elaine Whelan | 4/4 |
| Denise O'Donoghue | 4/4 |

1. Tom Milligan retired as a member of the Investment Committee with effect from 31 March 2018.

## Principal responsibilities of the Committee

- Recommends investment strategies, guidelines and policies to the Board and other members of the Group to approve annually;
- Recommends and sets risk asset definitions and risk tolerance levels;
- Recommends to the relevant boards the appointment of investment managers to manage the Group's investments;
- Monitors the performance of investment strategies within the risk framework; and
- Establishes and monitors compliance with investment operating guidelines relating to the custody of investments and the related internal controls.

## How the Committee discharged its responsibilities during 2018

The Committee regularly discussed and kept under review macro-economic, capital markets and global political developments during the year, in particular fiscal and political developments in the U.S. and the ongoing impact of the UK's Brexit negotiations on investment strategy and performance. The Committee also considered regular reports on the performance of the Group's investment portfolios, including asset allocation and compliance with pre-defined guidelines and tolerances; and recommended amendments to portfolio investment guidelines to the Board and operating boards of LICL, LUK and CUL. During the year the Committee received presentations from Goldman Sachs and PIMCO on the state of the investment markets and the Group's portfolio structure and performance.

The Committee's discussion of the investment strategy has been framed within the context of the Board's objective of ensuring appropriate connectivity with, and support for, the Group's underwriting operations. The Committee continued to prioritise the preservation of capital and seeks to ensure an appropriate balance between risk assets and core assets. The Committee aims to provide sufficient liquidity in the investment portfolio to meet the potential payout patterns on the Group's insurance business, and during the year the Committee modified the Group's liquidity rule to ensure that it appropriately recognises historic payout patterns.

The Committee also considered potential adjustments to the investment strategy in light of the decision to move the Company's group insurance regulatory supervision and tax residence from the UK to Bermuda.

## Priorities for 2019

The Committee's key priorities for 2019 are:

- To maintain a continued focus on a diversified portfolio, the preservation of capital, the maintenance of liquidity and the management of interest rate and other investment risks; and
- To continue to review the asset allocation strategy in light of the decision to move the Company's group insurance regulatory supervision and tax residence from the UK to Bermuda.

# Underwriting and Underwriting Risk Committee

**Alex Maloney**
Group Chief Executive Officer and Chairman of the Underwriting and Underwriting Risk Committee

**"The Committee provides a forum for discussing the Group's underwriting performance and developments in market pricing and coverage trends within the insurance and reinsurance lines in which we operate. The Committee's work in engaging with our underwriters and managers is an important discipline in helping manage the Group's (re)insurance risk exposures and in identifying areas of opportunity through the insurance cycle."**

## Committee membership

During 2018, the Underwriting and Underwriting Risk Committee comprised one Executive Director (the Group CEO) and one Non-Executive Director together with the Group CUO, the CUO of LICL, the CUO and Reinsurance Manager of LUK, the Active Underwriters for Syndicates 2010 and 3010, and the Deputy Group Chief Actuary (who are not Directors).

| | Meetings attended |
|---|---|
| Alex Maloney (Chairman) | 4/4 |
| Jon Barnes | 4/4 |
| Michael Dawson | 4/4 |
| Paul Gregory | 4/4 |
| Hayley Johnston | 4/4 |
| Sylvain Perrier[1] | 4/4 |
| Ben Readdy | 4/4 |
| John Spence | 4/4 |
| James Irvine[2] | 1/1 |
| Tom Milligan[3] | 1/1 |

1. Sylvain Perrier retired as a member of the Underwriting and Underwriting Risk Committee with effect from 31 December 2018.
2. James Irvine was appointed as a member of the Underwriting and Underwriting Risk Committee with effect from 30 October 2018.
3. Tom Milligan retired as a member of the Underwriting and Underwriting Risk Committee with effect from 31 March 2018.

## Principal responsibilities of the Committee

- Reviews Group underwriting strategy including consideration of new lines of business;
- Oversees the development of, and adherence to, underwriting guidelines by operating company CUOs;
- Reviews underwriting performance;
- Reviews significant changes in underwriting rules and policies;
- Establishes, reviews and maintains strict underwriting criteria and limits; and
- Monitors underwriting risk and its consistency with the Group's risk profile and risk appetite.

## How the Committee discharged its responsibilities during 2018

The Committee is actively engaged in the development of strategy and the formal underwriting risk tolerances, which are reviewed by the Committee and approved by the Board. Underwriting risk is the key risk faced by the Group. Specifically, the Committee receives quarterly risk data, tracking movements in the Group's exposures to modelled PMLs and RDSs.

The Committee monitors underwriting performance on a quarterly basis, and seeks to ensure that good risk selection and disciplined underwriting remain at the heart of the Group's underwriting strategy. The Committee reviewed

management reports on the structuring and pricing of the outwards reinsurance protections purchased across the Group. The Committee received quarterly update reports from the Active Underwriters of Syndicates 2010 and 3010, the CUOs for LUK and LICL and the CEO of KCML during 2018. The Committee also received quarterly reports of significant claims and related developments.

Regarding business development opportunities, the Committee reviewed and approved management plans for the recruitment of underwriters in onshore energy, power and aviation deductible lines of business as well as approving underwriting parameters for participating in transactional liability risk, underwritten on an agency basis.

During 2018, the Committee meetings were open to attendance by all of the Board members and provided a useful forum for the discussion of underwriting performance, the approval and management of risk tolerances and the development of strategic underwriting initiatives. The Committee and Board seek to match the Company's capital to the underwriting requirements of the business in all parts of the underwriting cycle.

A more detailed analysis of the Group's underwriting performance appears in the business review section of this Annual Report and Accounts on pages 26 to 32.

## Priorities for 2019

The Committee's key priorities for 2019 are:

- To continue to monitor the development and implementation of a forward-looking and disciplined underwriting strategy appropriate for the Group's underwriting platforms, within a framework of appropriate risk tolerances;
- To work actively with management in the identification, analysis and consideration of new underwriters and/or lines of business, with a particular focus on the managed development of growth in the U.S. specialty and catastrophe lines which are complementary to the Group's underwriting portfolio; and
- To continue to foster a nimble and responsive underwriting culture, capable of responding to the needs of clients, investors, employees and other stakeholders.

# Remuneration Committee

**Simon Fraser**
Chairman of the Remuneration Committee

**"The Committee seeks to support the recruitment and retention of the best people for our business. This requires achieving a balance between the need to ensure attractive and fair remuneration outcomes, which are linked to appropriately challenging yet realistic targets for Company and personal performance, and the need to avoid structures which might incentivise excessive risk-taking or a culture of short-termism."**

## Committee membership

The Remuneration Committee comprises three independent Non-Executive Directors and the Chairman of the Board.

| | Meetings attended |
|---|---|
| Simon Fraser (Chairman) | 4/4 |
| Peter Clarke | 4/4 |
| Michael Dawson | 4/4 |
| Robert Lusardi | 4/4 |

## Principal responsibilities of the Committee

- Sets the remuneration policy for, and determines the total individual remuneration packages, including pension arrangements of, the Company's Chairman, the Executive Directors, Company Secretary and other designated senior executives, to deliver long-term benefits to the Group;
- Agrees personal objectives for each Executive Director and the related performance and pay-out metrics for the performance element of the annual bonus;
- Determines each year whether awards will be made under the Group's RSS and, if so, the overall amount of such awards, the individual awards to Executive Directors and other designated senior executives, and the performance targets to be used;
- Ensures that contractual terms on termination or retirement, and any payments made, are fair to the individual and the Company; and
- Oversees any major changes in employee benefit structures throughout the Group.

## How the Committee discharged its responsibilities during 2018

During 2018, the Committee reviewed the Group incentive packages to ensure that remuneration is structured appropriately to promote the long-term success of the Company. The Committee also reviewed the RSS structure for Executive Directors to ensure that the performance metrics continue to align the interests of the Company with its investors and management. The Committee considered the salary and bonus awards for 2018 for Executive Directors and other designated senior executives. The Committee also approved the grant of awards under the Company's RSS.

The Committee reviewed Executive Directors' shareholdings in the context of the Company's share ownership guidelines for senior/key executives and discussed revisions to the guidelines to reflect more recent changes to the composition of the senior management team.

The Committee also reviewed the policy for Executive Directors' remuneration, which has a three-year life following its approval by shareholders at the 2017 AGM. The Committee considers the policy fit for purpose and does not propose any amendments at the 2019 AGM.

During 2018, the Committee recommended the approval and adoption by the Board of modifications to the Group Solvency II Identified Staff Remuneration policy principally to reflect changes within the staff population. The Committee continued to monitor progress made during the year on the alignment of remuneration practices across the Group.

The Committee also recommended changes to the companies comprising the Company's peer group for comparator purposes in light of recent M&A activity, albeit that with effect from the 2018 RSS awards the Group has decided to move away from a peer group approach in favour of absolute targets for both TSR and growth (see page 79 for further details).

The Committee considered a number of proposals relating to the treatment of RSS awards held by departing employees.

The Directors' Remuneration Policy and the Annual Report on Remuneration, for which the Committee is responsible, can be found on pages 70 to 89. The report contains a summary of the debate which has been had within the Committee and the Board on the alignment of remuneration and Group performance both in the current year and over a longer timeframe. It should be noted that following a shareholder consultation at the beginning of 2018, the Committee recommended a modification in the methodology for measurement of financial performance in the 2018 three-year RSS awards. The Committee noted and discussed the minority shareholder vote against the Annual Report on Remuneration at the 2018 AGM and, following a further consultation with shareholders at the beginning of 2019, the Committee has recommended to the Board the continued use of the measurement methodology for the 2019 three-year RSS awards (see page 79 for further details).

## Priorities for 2019

The Committee does not expect any change to the implementation of its policy in 2019. The Committee's key priorities for 2019 are:

- To review the ongoing appropriateness and relevance of the Group's remuneration structures, ensuring that they are in line with the Group's business strategy, risk profile, objectives, risk management practices and long-term interests;
- To ensure that remuneration across the wider Group meets the staffing needs and staff retention requirements of the business; and
- To conduct a full review of the 2017 Directors' Remuneration Policy, with any changes being put to shareholders for consideration at the 2020 AGM. As part of this review, the Committee will work with its independent advisers to keep abreast of compensation levels amongst the Group's Bermudian and other peers, and the latest compensation issues and market practices.

## Annual statement

Dear Shareholder,

I am pleased to present the 2018 Directors' Remuneration Report to shareholders.

### Shareholder engagement

Lancashire's Directors' Remuneration Policy was approved by shareholders at the May 2017 AGM. There were no changes to the Policy proposed at the 2018 AGM. At our 2018 AGM we received support from in excess of 80 per cent of shareholders that voted for our Annual Report on Remuneration. On behalf of the Committee I contacted various shareholders and proxy advisory agencies, both before and/or after the 2018 AGM vote, to explain and discuss the Committee's reasoning for the changes implemented in 2018. The Committee has debated the appropriate remuneration structures to be used in 2019 in some detail and (as I set out below) we have decided to follow the same structure for the remuneration of our Executive Directors as was used in 2018.

### Remuneration and strategy

The Group's goal continues to be to reward its employees fairly and responsibly by providing an appropriate balance between fixed remuneration and variable remuneration linked to the achievement of suitably challenging Group and individual performance measures.

There is a strong link between the Remuneration Policy and the business strategy. As highlighted elsewhere in this Annual Report and Accounts, our strategy focuses on the effective operation of the business necessary to maximise long-term RoE and the delivery of superior total shareholder returns on a risk-adjusted basis over the course of the insurance cycle. Our Remuneration Policy and the way it is implemented are closely aligned to this strategy.

The Board and management continue to believe that the insurance industry is cyclical in its fundamental characteristics. The Board's priorities at the current point in the pricing cycle are to achieve acceptable returns whilst moderating overall risk levels through underwriting discipline and prudent reinsurance planning and to ensure that throughout the softer part of the market cycle the business has continued to service the needs of its core clients and brokers.

### Performance outcomes for 2018 – another challenging year

The Group has produced an RoE of 2.4 per cent (see the strategy and performance reviews of this report on pages 16 to 21).

The Board and Committee were satisfied that in light of 2018 market loss events this performance represents an acceptable outcome for the year. Whilst this has been a year in which higher than average catastrophe loss activity has been experienced, the business has generated positive annual earnings and the Group remains vibrant and well-capitalised. The business is well-positioned to compete in the market as we enter 2019 in what we expect to be an improving phase of the insurance cycle. Our strategy is to continue exploring opportunities for organic growth, where this makes sense, whilst ensuring a rigorous focus on the balanced management of risk and reward.

Against the background described above there has been a decrease in total remuneration of 26 per cent for the CEO and 20 per cent for the CFO between 2017 and 2018 (see the comparison table for single figure remuneration on page 80). This movement is largely driven by an RoE of 2.4 per cent for 2018 and the negative 5.9 per cent for 2017, which taken together severely impacted the vesting levels on the 2016 RSS awards (see below and page 83 for further details).

The Executive Directors' annual bonus performance targets set at the beginning of 2018 for personal and financial performance were stretching. The financial element which made up 75 per cent of the annual bonus opportunity resulted in no annual bonus for that element given the Company's 2018 low return (as a result of the above average catastrophe loss environment). The Board did however consider that both the Executive Directors had performed strongly in managing risk within the business and in positioning the Group well for what we hope will be a better rating environment in 2019, therefore a bonus was awarded for the personal component in respect of 2018 performance. In summary, annual bonuses for our Executive Directors were achieved substantially below target level at 19 per cent of maximum bonus for both the CEO and the CFO (see page 82 for further details).

In relation to long-term incentives for Executive Directors and other senior management, the 2016 Performance RSS awards were 75 per cent based on absolute RoE targets and 25 per cent on relative TSR against specified peer group companies over the three-year period to 31 December 2018. Our TSR performance (in U.S. dollars) over this period ranked the Company below the median of the designated peer group of 11 companies, resulting in 0 per cent vesting for the TSR component.

Our average RoE performance over this three-year performance period was 3.3 per cent against a threshold target of the 13-week Treasury bill rate plus 6 per cent and a maximum pay out of the 13-week Treasury bill rate plus 15 per cent, resulting in 0 per cent of the RoE component of the 2016 Performance RSS awards vesting. Therefore overall, the 2016 Performance RSS awards vested at 0 per cent. This compared with the overall 22.5 per cent vesting of the 2015 Performance RSS awards due to 30.1 per cent vesting of the RoE portion of those awards and 0 per cent vesting of the TSR portion of the awards, which we reported last year.

The total remuneration received by our Executive Directors in 2018 was accordingly lower than that received in 2017 (see page 80 for the comparison data), as demonstrated by the table of Total Remuneration History for the CEO on page 88.

The Committee believes in setting challenging performance criteria and having a significant proportion of the overall package linked to Company performance. However, the Committee also continues to recognise the need to ensure that Executive Directors are appropriately remunerated and incentivised even in the more challenging phases of the insurance cycle, as at present.

It is also important that the Committee and the Board ensure that Executive Director compensation is structured in such a way as to discourage excessive risk to the business.

Overall, in light of the annual and three-year performance delivered, the Committee is satisfied that there has been a robust link between performance and reward for Executive Directors, albeit that the Group's performance has been substantially impacted by a series of above average catastrophe loss events to the global insurance markets, which are beyond the power of our Executive Directors to control, but which have been appropriately planned for. Lancashire will continue to ensure that there remains appropriate alignment between executive remuneration and Company performance, not only in loss-affected years, but also in those future years when the Group hopes to produce results more in line with its cross-cycle return expectations.

## Application of Remuneration Policy for 2019

The Remuneration Committee has reviewed the 2017 Directors' Remuneration Policy approved by shareholders and considers it to remain fit for purpose. The Remuneration Committee will be conducting a full review of the Policy in 2019, with any changes being put to shareholders for consideration at the 2020 AGM. The planned review will take into account changes introduced as a result of the FRC's revised 2018 UK Corporate Governance Code.

The final section of this report is the Annual Report on Remuneration, which provides detailed disclosure on how the Policy will be implemented for 2019 and how Directors have been paid in relation to 2018. The Board has decided to apply the targets for the annual bonus on substantially the same basis as agreed for 2018. In deciding to implement the three-year RSS awards for Executive Directors for 2019 on the same basis as the 2018 RSS awards, I wrote to our major shareholders and a number of the leading proxy voting advisory services and held a number of meetings to seek comments on our plans and the feedback given was largely supportive.

There has been some discussion within the investor community regarding post-employment holding periods for Executive Directors, which the Committee has discussed. The Committee does not propose to change the current policy at present, but will further debate this matter during the year and as part of the Remuneration Policy review, which is to take place in advance of the shareholder policy vote in 2020. The Committee notes that the current structure of the RSS awards requires a two-year holding period post vesting for awards held by Executive Directors. Should an Executive Director leave the business on agreed terms as a 'good leaver' it will ordinarily be a requirement that RSS awards vesting after the date of departure should be held for a period of two years post vesting. Accordingly, the Committee notes that in a managed exit for an Executive Director there is already a degree of post-employment shareholder alignment under the current arrangements.

The disclosures provide our shareholders with the information necessary to form a judgement as to the link between Company performance and how the Executive Directors are paid. This Annual Statement together with the Annual Report on Remuneration will be subject to an advisory vote and I hope that you will be able to support the resolution at the forthcoming AGM. The Committee is committed to maintaining an open and constructive dialogue with our shareholders on remuneration matters and I welcome any feedback you may have.

**Simon Fraser**
Chairman of the Remuneration Committee

## Directors' Remuneration Policy section

As a company incorporated in Bermuda, Lancashire is not bound by UK law or regulation in the area of Directors' remuneration to the same extent that it applies to UK incorporated companies. However, by virtue of the Company's premium listing on the LSE, and for the purposes of explaining its compliance against the requirements of the Code, the Board is committed to providing full information on Directors' remuneration to shareholders. In particular, the Committee has discussed the changes to the Code during 2018 for implementation during 2019, in particular with regard to the responsibilities of the Remuneration Committee and Board concerning the review and cognisance of workforce remuneration structures and the mechanisms for employees' engagement and feedback.

The Company's Remuneration Policy was approved by shareholders at the 2017 AGM and is effective for a period of three years from the 2017 AGM until the AGM in 2020 (or until amended by a decision of shareholders). The 2017 Remuneration Policy was developed taking into account the principles of the Code and the views of our major shareholders. As noted earlier, the Committee will be conducting a full review of the Remuneration Policy in 2019, with any changes put to shareholders for consideration at the 2020 AGM.

The 2017 Remuneration Policy contains details of the Company's policy to govern future payments that will be made to Directors.

The Annual Report on Remuneration also details the remuneration paid to Directors in respect of the 2018 financial year in accordance with the shareholder approved Policy.

### Governance and approach

The Company's Remuneration Policy is geared towards providing a level of remuneration which attracts, retains and motivates Executive Directors of the highest calibre to further the Company's interests and to optimise long-term shareholder value creation, within appropriate risk parameters. The Remuneration Policy also seeks to ensure that Executive Directors are provided with appropriate incentives to drive individual performance and to reward them fairly for their contribution to the successful performance of the Company.

The Remuneration Committee and the Board have again considered whether any element of the Remuneration Policy could conceivably encourage Executive Directors to take inappropriate risks and have concluded that this is not the case, given the following:

- there is an appropriate balance between fixed and variable pay, and therefore Executive Directors are not required to earn performance-related pay to meet their day-to-day living expenses;
- there is a blend of short-term and long-term performance metrics with an appropriate mix of performance conditions, meaning that there is no undue focus on any one particular metric;
- there is a high level of share ownership amongst Executive Directors, meaning that there is a strong focus on sustainable long-term shareholder value; and
- the Company has the power to claw back bonuses (including the deferred element of the annual bonus) and long-term incentive payments made to Executive Directors in the event of material misstatements in the Group's consolidated financial statements, errors in the calculation of any performance condition, or the Executive Director ceasing to be a Director and/or employee due to gross misconduct.

### How the views of shareholders are taken into account

The Committee Chairman and, where appropriate, the Company Chairman, consult with major investors and representative bodies on any significant remuneration proposal relating to Executive Directors. Views of shareholders at the AGM, and feedback received at other times, will be considered by the Committee. In January 2019 the Committee Chairman conducted a consultation on behalf of the Committee with various shareholders and proxy advisory agencies to seek feedback on the Committee's plans to implement the Remuneration Policy for the Executive Directors for 2019 without any material changes to the approach adopted in 2018. Feedback received was supportive of that approach.

### How the views of employees are taken into account

The Remuneration Committee takes into account levels of pay elsewhere in the Group when determining the pay levels for Executive Directors. The Remuneration Policy for all staff is, in principle, broadly the same as that for Executive Directors in that any of the Group's employees may be offered similarly structured packages, with participation in annual bonus and long-term incentive plans, although award types (restricted cash, restricted stock or performance shares) and size may vary between different categories of staff. For Executive Directors, with higher remuneration levels, a higher proportion of the compensation package is subject to performance pay, share-based remuneration and deferral. This ensures that there is a strong link between remuneration, Company performance and the interests of shareholders.

Reflecting good practice in this area, Executive Directors' pension provision is no more generous than the pension contributions made to employees in the Group (in percentage of salary terms).

The Company does not consult with employees on Executive Directors' remuneration. However, as noted above, the Committee is made aware of pay structures across the wider Group when setting the Remuneration Policy for Executive Directors. The Committee also reviews and approves the size of any annual bonus pot to be distributed amongst the staff population and the allocation of RSS awards, and its practice in this regard is well aligned with the expectations introduced within the revised Code.

## Remuneration Policy table

| **Base salary** | |
|---|---|
| Purpose and link to strategy | Helps recruit, motivate and retain high-calibre Executive Directors by offering salaries at market competitive levels.<br>Reflects individual experience and role. |
| Operation | Normally reviewed annually and fixed for 12 months, typically effective from 1 January. Positioning and annual increases influenced by:<br>• role, experience and performance;<br>• change in broader workforce salary;<br>• changes to the size and complexity of the business; and<br>• changes in responsibility or position.<br>Salaries are benchmarked periodically against insurance company peers in the UK, U.S. and in Bermuda. |
| Opportunity | No maximum. |

| **Benefits** | |
|---|---|
| Purpose and link to strategy | Market competitive structure to support recruitment and retention.<br>Medical cover aims to ensure minimal business interruption as a result of illness. |
| Operation | Executive Directors' benefits may include healthcare, dental, vision, gym membership and life insurance. Other additional benefits may be offered from time to time that the Committee considers appropriate based on the Executive Director's circumstances.<br>Executive Directors who are expatriates or are required to relocate may be eligible for a housing allowance or other relocation-related expenses.<br>Any reasonable business-related expense can be reimbursed, including any personal tax thereon if such expense is determined to be a taxable benefit. |
| Opportunity | No maximum. |

| **Pension** | |
|---|---|
| Purpose and link to strategy | Contribution towards funding post-retirement lifestyle. |
| Operation | The Company operates a defined contribution pension scheme (via outsourced pension providers) or cash-in-lieu of pension.<br>There is a salary sacrifice structure in the UK.<br>There is the opportunity for additional voluntary contributions to be made by individuals, if elected. |
| Opportunity | Company contribution is currently 10 per cent of base salary. |

| **Annual bonus[1,2]** | |
|---|---|
| Purpose and link to strategy | Rewards the achievement of financial and personal targets. |
| Operation | The annual bonus is based on financial and personal performance.<br>The precise weightings may differ each year, although there will be a greater focus on financial as opposed to personal performance.<br>The Committee will have the ability to override the bonus outcome by either increasing or decreasing the amount payable (subject to the cap) to ensure a robust link between reward and performance.<br>At least 25 per cent of each Executive Director's bonus is automatically deferred into shares as nil-cost options or conditional awards over three years, with one-third vesting each subsequent year.<br>A dividend equivalence provision operates enabling dividends to be accrued (in cash or shares) on unvested deferred bonus shares in the form of nil-cost options up to the point of exercise.<br>The bonus is subject to clawback if the financial statements of the Company were materially misstated or an error occurred in assessing the performance conditions on bonus and/or if the Executive ceased to be a Director or employee due to gross misconduct. |

| | |
|---|---|
| Opportunity | The maximum bonus for Executive Directors for achieving target level of performance as a percentage of salary is 200 per cent of salary. Maximum opportunity is two times target.<br>Note: The Committee may set bonus opportunities less than the amounts set out above – see Implementation of Policy section of the Annual Report on Remuneration. |
| Performance metrics | The weightings that apply to the bonus measures and the degree of stretch in objectives may vary each year depending on the business aims and the broader economic or industry environment at the start of the relevant year. For Executive Directors, the financial component will be at least 75 per cent of the overall opportunity, and no more than 25 per cent will be based on personal or strategic objectives.<br>**Financial performance**<br>The financial component is based on the Company's key financial measures of performance. For any year, these may include RoE, growth in BVS, profit, comprehensive income, combined ratio, investment return or any other financial KPI[3].<br>Typically, a sliding scale of targets applies for financial performance targets. Bonus is earned on an incremental basis once a predetermined threshold level is achieved. Up to 25 per cent of the total bonus opportunity is payable for achieving threshold/median, rising to maximum bonus for stretch/upper quartile performance.<br>The degree of stretch in targets may vary each year depending on the business aims and the broader economic or industry environment at the start of the relevant year.<br>**Personal performance**<br>Personal performance is based upon achievement of clearly articulated objectives. A performance rating is attributed to participating Executive Directors, which determines the payout for this part of the bonus. |
| **Long Term Incentives (LTI)** | |
| Purpose and link to strategy | Rewards Executive Directors for achieving superior returns for shareholders over a longer time frame.<br>Enables Executive Directors to build a meaningful shareholding over time and align goals with shareholders. |
| Operation[2,3] | RSS awards are normally made annually in the form of nil-cost options (or conditional awards) with vesting dependent on the achievement of performance conditions over at least three financial years, commencing with the year of grant. This three-year period is longer than the typical pattern of loss reserve development on the Group's insurance business, which is approximately two years.<br>The number of awards will normally be determined by reference to the share price around the time of grant unless the Committee, at its discretion, determines otherwise.<br>The Committee considers carefully the quantum of awards each year to ensure that they are competitive in light of peer practice and the targets set.<br>Awards are subject to clawback if there is a material misstatement in the Company's financial statements, an error in the calculation of any performance conditions or if the Executive Director ceases to be a Director or employee due to gross misconduct.<br>A dividend equivalence provision operates enabling dividends to be accrued (in cash or shares) on RSS awards up to the point of exercise.<br>The Committee has the discretion, in exceptional circumstances, to settle an award made to Executive Directors in cash.<br>A two-year post-vesting holding period applies to awards made to Executive Directors since 2016. |
| Opportunity | Award levels are determined primarily by seniority. A maximum individual grant limit of 350 per cent of salary applies.<br>Note: The Committee may set the normal level of award at less than the percentage set out above – see Implementation of Remuneration Policy section of the Annual Report on Remuneration. |
| Performance metrics | Awards vest at the end of a three-year performance period based on performance measures reflecting the long-term strategy of the business at the time of grant.<br>These may include measures such as TSR, RoE/BVS, Company profitability, or any other relevant financial measures.<br>If more than one measure is used, the Committee will review the weightings between the measures chosen and the target ranges prior to each LTI grant to ensure that the overall balance and level of stretch remains appropriate.<br>A sliding scale of targets applies for financial metrics with no more than 25 per cent vesting for threshold performance.<br>For TSR, none of this part of the award will vest below median ranking or achievement of an index. No more than 25 per cent of this part of the award will vest for achieving median or index. |

## Remuneration Policy table continued

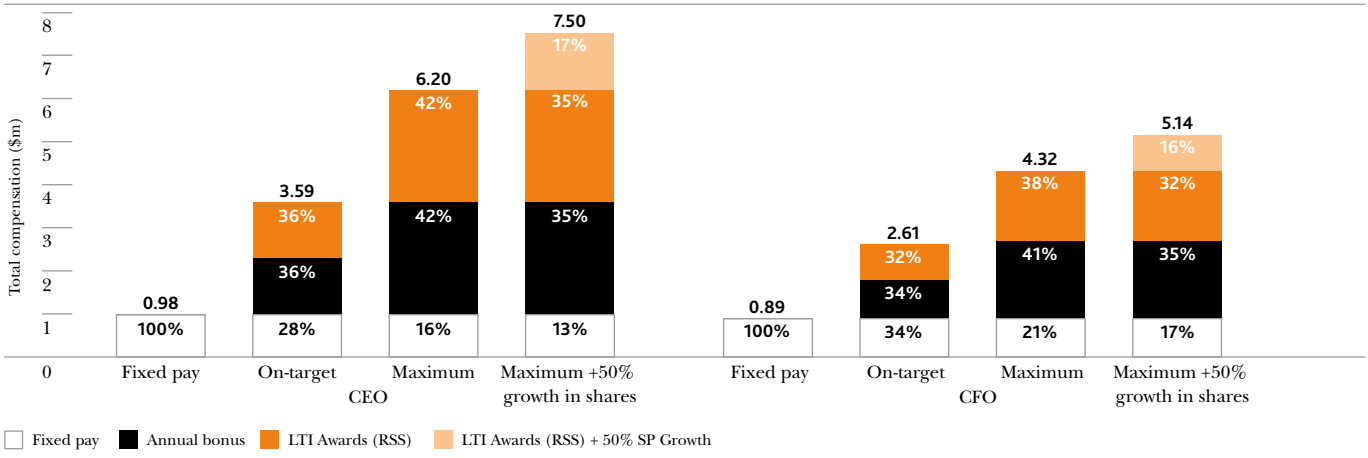
| Share ownership guidelines[4] |
|---|
| Under the guidelines, Executive Directors are expected to maintain an interest equivalent in value to no less than two times salary over time. Until such time as the guideline threshold is achieved Executive Directors are required to retain no less than 50 per cent of the net of tax value of awards that vest under the RSS. |

| Chairman and Non-Executive Directors' fees | |
|---|---|
| Purpose and link to strategy | Helps recruit, motivate and retain a Chairman and Non-Executive Directors of a high calibre by offering a market competitive fee level. |
| Operation | The Chairman is paid a single fee for his responsibilities as Chairman. The level of these fees is reviewed periodically by the Committee and the CEO by reference to broadly comparable businesses in terms of size and operations.<br>In general, the Non-Executive Directors are paid a single fee for all responsibilities, although supplemental fees may be payable where additional responsibilities are undertaken, including a Non-Executive Director role on a subsidiary board.<br>Any reasonable business-related expenses (including any personal tax payable) can be reimbursed. |
| Opportunity | No maximum. |

1. The Committee operates the annual bonus plan and RSS according to their respective rules and in accordance with the Listing Rules. The Committee, consistent with normal market practice, retains discretion over a number of areas relating to the operation and administration of these plans and this discretion forms part of this policy.
2. All historical awards that were granted under any current or previous share scheme operated by the Company that remain outstanding remain eligible to vest based on their original award terms and this provision forms part of the policy.
3. Performance measures: these may include the performance indicators shown on pages 20 to 21 or others described within the Annual Report and Accounts Glossary commencing on page 162 or any other measure that supports the achievement of the Company's short to long-term objectives.
4. Share ownership interest equivalent is defined as wholly owned shares or the net of taxes value of RSS awards which have vested but are unexercised and the net of tax value of deferred bonus RSS awards. Shares include those owned by persons closely associated with the relevant Executive Director.

## Illustrations of annual application of Remuneration Policy

The charts below show the potential total remuneration opportunities for the Executive Directors in 2019 at different levels of performance under the Directors' Remuneration Policy.




Fixed pay = 2019 Salary + Actual Value of 2018 Benefits + 2019 Pension Contribution.

On-target = Fixed Pay + Target Bonus (being half the Maximum Bonus Opportunity) + Target Value of 2019 RSS grant (assuming 50 per cent vesting with face values of grant).

Maximum = Fixed Pay + Maximum Bonus Opportunity + Maximum Value of 2019 RSS grant (assuming 100 per cent vesting with the face values of grant).

Maximum + 50% growth over performance period = Fixed Pay + Maximum Bonus Opportunity + Maximum Value of 2019 RSS grant + 50% share price appreciation (assuming 100 per cent vesting with the face values of grant).

## Approach to recruitment remuneration

The remuneration package for a new Executive Director would be set in accordance with the terms of the Company's prevailing approved Remuneration Policy at the time of appointment and take into account the skills and experience of the individual, the market rate for a candidate of that experience and the importance of securing the relevant individual.

Salary would be provided at such a level as is required to attract the most appropriate candidate. The Committee retains the flexibility to set base salary for a newly appointed Executive Director below the mid-market level and allow them to progress quickly to or around mid-market level once expertise and performance have been proven. This decision would take into account all relevant factors noted above.

The annual bonus and LTI potential would be in line with the Policy. Depending on the timing of the appointment, the Committee may deem it appropriate to set different bonus performance measures for the performance year during which he or she became an Executive Director. The Committee may grant an LTI award to an executive shortly after joining, up to the plan limits set out in the Remuneration Policy table (assuming the Company is not in a closed period).

In addition, the Committee may offer additional cash and/or share-based elements to replace deferred or incentive pay forfeited by an Executive leaving a previous employer. It would seek to ensure, where possible, that these awards would be consistent with awards forfeited in terms of vesting periods (which may be less than three years), expected value and performance conditions.

For an internal Executive Director appointment, any variable pay element awarded in respect of the prior role may be allowed to pay out according to its terms, adjusted as relevant to take into account the appointment. In addition, any other ongoing remuneration obligations existing prior to appointment may continue.

The Committee may agree that the Company will meet certain relocation expenses as appropriate and is able to provide expatriate benefits including housing, a relocation allowance, assignment-related costs or tax equalisation.

## Service contracts and loss of office payment policy for Executive Directors

Executive Directors have service contracts with six-month notice periods. In the event of termination, the Executive Directors' contracts provide for compensation up to a maximum of base salary plus the value of benefits to which the Executive Directors are contractually entitled for the unexpired portion of the notice period. The Company may pay statutory claims. No Executive Director has a contractual right to a bonus for any period of notice not worked.

The service contract for a new appointment will be on similar terms as existing Executive Directors, with the facility to include a notice period of no more than 12 months from either party.

The Company seeks to apply the principle of mitigation in the payment of compensation on the termination of the service contract of any Executive Director. There are no special provisions in the service contracts for payments to Executive Directors on a change of control of the Company.

In the event of an exit of an Executive Director, the overriding principle will be to honour contractual remuneration entitlements and determine, on an equitable basis, the appropriate treatment of deferred and performance-linked elements of the package, taking account of the circumstances. Failure will not be rewarded.

Depending on the leaver classification, an Executive Director may be eligible for certain payments or benefits continuation after cessation of employment.

If an Executive Director resigns or is summarily dismissed, salary, pension and benefits will cease on the last day of employment and there will be no further payments.

## Leaver on arranged terms or good leaver

If an Executive Director leaves on agreed terms, including compassionate circumstances, there may be payments after cessation of employment. Salary, pension and benefits will be paid up to the length of the agreed notice period or agreed period of gardening leave.

Subject to performance, a bonus may be payable at the discretion of the Committee pro-rata for the portion of the financial year worked.

Vested but unexercised deferred bonus RSS awards will remain exercisable. Unvested deferred bonus RSS awards will ordinarily vest in full, relative to the normal vesting period. All such vested awards must be exercised within 12 months of the vesting date.

Vested but unexercised RSS awards may remain exercisable for 12 months. Unvested awards may vest on the normal vesting date unless the Committee determines that such awards shall instead vest at the time of cessation. Unvested awards will only vest to the extent that the performance conditions have been satisfied (over the full or curtailed period as relevant). A pro-rata reduction in the size of awards may apply, based upon the period of time after the grant date and ending on the date of cessation of employment relative to the three-year or other relevant vesting period.

The Committee has discretion to permit unvested RSS awards to vest early rather than continue on the normal vesting timetable and also retains discretion as to whether or not to apply (or to apply to a lesser extent) the pro-rata reduction to the RSS awards where it feels the reduction would be inappropriate.

Depending upon circumstances, the Committee may consider other payments in respect of any claims in connection with a termination of employment where deemed appropriate, including an unfair dismissal award, outplacement support and assistance with legal fees.

## Terms of appointment for Non-Executive Directors

The Non-Executive Directors serve subject to the Company's Bye-laws and under letters of appointment. They are appointed subject to re-election at the AGM and are also terminable by either party on six months' notice except in the event of earlier termination in accordance with the Bye-laws. The Non-Executive Directors are typically expected to serve for up to six years, although the Board may invite a Non-Executive Director to serve for an additional period. Their letters of appointment are available for inspection at the Company's registered office and at each AGM.

In accordance with best practice under the Code, the Board ordinarily submits the Directors individually for re-election by the shareholders at each AGM.

## Legacy arrangements

In approving the Policy, authority is given to the Company for the duration of the Policy to honour commitments paid, promised to be paid or awarded to: (i) current or former Directors prior to the date of this Policy being approved (provided that such payments or promises were consistent with any Remuneration Policy of the Company which was approved by shareholders and was in effect at the time they were made); or (ii) to an individual (who subsequently is appointed as a Director of the Company) at a time when the relevant individual was not a Director of the Company and, in the opinion of the Committee, was not paid, promised to be paid or awarded as financial consideration of that individual becoming a Director of the Company, even where such commitments are inconsistent with the provisions of the revised Policy.

For the avoidance of doubt, this includes all awards granted under the 2008 RSS rules in accordance with the Policy approved at the 2014 AGM and the current Policy which was approved by shareholders at the 2017 AGM, and to employees of the Company who are not Directors at the date of grant. Outstanding RSS awards that remain unvested or unexercised at the date of this report (including for current Executive Directors as detailed on page 84 of the Annual Report on Remuneration) remain eligible for vesting or exercise based on their original award terms.

## Annual Report on Remuneration

This Annual Report on Remuneration together with the Chairman's Statement, as detailed on pages 70 and 71, will be subject to an advisory vote at the 2019 AGM. The following sections in respect of Directors' emoluments have been audited by KPMG:

- Single figure of remuneration.
- Non-Executive Directors' fees.
- 2019 annual bonus payment in respect of 2018 performance.
- Long-term share awards with performance periods ending in the year – 2016 RSS award.
- Scheme interests awarded during the year.
- Loss of office payments.
- Performance and deferred bonus awards under the RSS.
- Directors' shareholdings and share interests.

### Implementation of Remuneration Policy for 2019

In relation to the Policy described in the previous section, the following section sets out additional disclosure on the expected application of the Policy for 2019.

### Base salary and fees

*Executive Directors*

Increases and resulting salaries effective from 1 January 2019 are set out below:

- CEO – salary increased by 3 per cent to $869,460.
- CFO – salary increased by 3 per cent to $597,030.

For 2019, increases of 3 per cent are in line with the standard salary increases for Group employees.

*Non-Executive Directors*

The Chairman's and Non-Executive Directors' fees are as follows for 2019:

- The fee for the Chairman (Peter Clarke) will remain at $350,000 per annum.
- The Non-Executive Director fee will remain at $175,000 per annum.

*Other fees*

- Samantha Hoe-Richardson is a Non-Executive Director of LUK in which capacity she will receive a fee of $67,099 per annum.
- Simon Fraser is a Non-Executive Director of CUL in which capacity he will receive a fee of $80,000 per annum.

### Annual bonus

For 2019, the CEO and CFO will have a target bonus of 150 per cent of salary and, therefore, a maximum opportunity of 300 per cent of salary. This is within the approved policy limit and is in line with last year's opportunity and represents a maximum bonus opportunity which is 100 per cent of salary less than the set policy limit.

The financial and personal portions of the annual bonus will remain unchanged with 75 per cent on financial performance and 25 per cent on personal performance.

*Financial performance (75 per cent)*

The Company's most important financial KPI is RoE, which is the core indicator of the delivery of its strategic priorities of ensuring underwriting comes first, effectively balancing risk and return and managing capital nimbly through the insurance cycle (see the strategic overview on pages 16 and 17 of this Annual Report and Accounts). For 2019, the financial component for annual bonus is to be based on the performance of the Group's RoE, measured as the internal rate of return of the change in FCBVS plus accrued dividends.

A sliding scale range of RoE targets has been set by reference to the Risk Free Rate of Return as follows:

- 25 per cent of target bonus shall be payable at a threshold level of RoE equal to RFRoR + 6 per cent (0 per cent will be payable below this threshold).
- 50 per cent of target bonus shall be payable at a level of RoE equal to RFRoR + 7 per cent.
- 100 per cent of target bonus shall be payable at a level of RoE equal to RFRoR + 8 per cent.
- 200 per cent of target bonus shall be payable at a level of RoE equal to RFRoR + 14 per cent.

There shall be linear interpolation between these points. The Board considers that these target ranges are appropriately challenging, given the current insurance market conditions, and will help to ensure a strong link between remuneration for the Executive Directors and the Company's financial performance, the strategy and risk profile of the business and the investment return environment, without encouraging excessive risk-taking.

*Personal performance (25 per cent)*
This element of the bonus plan is based upon the individual achievement of clearly articulated objectives created at the beginning of each year. The table below sets out a broad summary of the 2019 personal objectives for each Executive Director.

| Executive Director | Personal performance |
|---|---|
| Alex Maloney | Effective leadership and management of the senior executive team and Group.<br>Development of the general business strategy.<br>Contribution aligned to the Lancashire Group Values. |
| Elaine Whelan | Effective leadership and management of the finance function and the Bermuda office.<br>Development of the general business strategy.<br>Contribution aligned to the Lancashire Group Values. |

The personal targets are broadly common among the Executive Directors, with variances being attributable to the specifics of their respective roles. Specific granular areas for personal development within the set broad personal objectives are discussed between the Chairman and the Executive Directors and agreed by the Committee. As part of the 2019 annual performance reviews, each Executive Director will receive a performance rating which will determine the level of personal performance bonus payout for which each Executive Director will be eligible.

## Restricted Share Scheme

### Performance conditions

For Executive Directors, 2019 RSS awards are subject to a range based on (i) annual growth in FCBVS plus accrued dividends and (ii) absolute TSR performance conditions, both measured by reference to a period ending on 31 December 2021. These metrics aim to provide an appropriate focus on the Company's underlying financial performance and cycle management, and in the case of absolute TSR to provide an objective reward for delivering value to shareholders.

*Weighting*
For 2019, the weighting is 85 per cent on annual growth in FCBVS plus accrued dividends and 15 per cent on absolute TSR.

*Target ranges*
The annual growth in FCBVS plus accrued dividends target range for 2019 awards is:

- threshold – 6 per cent; and
- maximum – 13 per cent.

Within the three-year performance period each of the separate financial years will be treated as a separate element, each one contributing one-third to the overall outcome of the vesting of this element of the RSS award. In each year performance will be measured against the target range to determine the ultimate level of vesting in respect of one-third of the RSS award. Vesting will only occur after completion of the full three-year performance period, and continued employment of the Executive Director at the time of vesting.

The relevant element of the RSS award will not vest if annual growth in FCBVS plus accrued dividends is below threshold, 25 per cent of the relevant element of the RSS award will vest at threshold, and 100 per cent of the relevant element of the RSS award will vest at maximum. Performance between threshold and maximum is determined on a straight-line basis.

*Overriding downwards discretion*
If any year produces a return that the Committee believes is significantly worse than competitors and reflects poor management decisions, the Remuneration Committee will use its discretion to determine that no part (or a lesser part) of the RSS award accrued over the full three-year period shall vest.

The TSR target range for 2019 awards is:

- threshold – 8 per cent compound annual growth; and
- maximum – 12 per cent compound annual growth.

Absolute TSR will be measured over the full three-year performance period rather than looking at each year separately.

None of the award will vest if TSR is below threshold, 25 per cent of the award will vest at threshold, and 100 per cent of the award will vest at maximum. Performance between threshold and maximum is determined on a straight-line basis.

### Award levels

2019 RSS award levels are as follows:

- CEO – shares to the value of $2,608,380 (being 300 per cent of salary).
- CFO – shares to the value of $1,641,833 (being 275 per cent of salary).

The number of shares awarded shall be determined based on the closing average share price for a period of five trading days immediately prior to the date of the award.

### Post-vesting holding period

For RSS awards made in 2016 or subsequent years, Executive Directors are expected to hold vested RSS awards (or the resultant net of tax shares) which had a performance period of at least three years, for a further period of not less than two years following vesting.

## Single figure of remuneration

The following table presents the Executive Directors' emoluments in U.S. dollars in respect of the years ended 31 December 2018 and 31 December 2017.

| Executive Directors | | Salary $ | Pension $ | Taxable benefits[1] $ | Annual bonus[5] $ | Long-Term Incentives (RSS)[2,3] $ | Total[4] $ |
|---|---|---|---|---|---|---|---|
| Alex Maloney[4,], CEO | **2018** | 846,910 | 84,691 | 24,879 | 474,826 | 0 | 1,431,306 |
| | 2017 | 811,311 | 81,227 | 21,910 | 420,000 | 608,696 | 1,943,144 |
| Elaine Whelan[4,6], CFO | **2018** | 579,967 | 57,795 | 234,144 | 326,048 | 0 | 1,197,954 |
| | 2017 | 562,268 | 56,275 | 155,960 | 310,000 | 419,120 | 1,503,623 |

1. Benefits comprise Bermudian payroll taxes, social insurance, medical, dental and vision coverage and housing and other allowances paid by the Company for expatriates (as is the case for the CFO), but exclude UK National Insurance contributions.
2. For 2018, the long-term incentive values are based on the 2016 RSS awards which vest at 0 per cent on 14 February 2019 and are based on a three-year performance period that ended on 31 December 2018.
3. For 2017, the long-term incentive values were based on the 2015 RSS awards which vested at 22.5 per cent on 15 February 2018 and were based on a three-year performance period that ended on 31 December 2017. The values are re-presented from the 2017 Annual Report and Accounts based on the share price at the vesting date, 15 February 2018 ($8.397), and include the value of dividends accrued on vested shares.
4. Some amounts were paid in Sterling and converted at the average exchange rate of 1.3420 for the year as they are set in U.S. dollars.
5. Bonus targets were set at the beginning of 2018 and are based on a clear split between Company financial performance and personal performance on a 75:25 basis. Company financial performance is based on absolute financial performance against the RFRoR. The Company financial performance component paid out at 0 per cent of target as the RoE was 2.4 per cent against a target level of RFRoR +8 per cent. The personal element of Executive Directors' bonus opportunity was the only bonus element to pay out. Final bonus payout to Executive Directors will be 19 per cent of the maximum for the CEO and 19 per cent of the maximum for the CFO. For full details of Executive Directors' bonuses and the associated performance delivered see pages 81 and 82. 25 per cent of Executive Directors' annual bonus is deferred into RSS awards without performance conditions, vesting at 33.3 per cent per year over a three-year period.
6. For Elaine Whelan, the increase in taxable benefits from 2017 to 2018 is a result of changes in the Bermuda payroll tax regime.

## Non-Executive Directors' fees

| Current Non-Executive Directors | | Fee $ | Other $ | Total $ |
|---|---|---|---|---|
| Peter Clarke | **2018** | **350,000** | **–** | **350,000** |
| | 2017 | 350,000 | – | 350,000 |
| Michael Dawson | **2018** | **175,000** | **–** | **175,000** |
| | 2017 | 175,000 | – | 175,000 |
| Simon Fraser | **2018** | **175,000** | **80,000** | **255,000** |
| | 2017 | 175,000 | 80,000 | 255,000 |
| Samantha Hoe-Richardson[3] | **2018** | **175,000** | **67,099** | **242,099** |
| | 2017 | 175,000 | 64,500 | 239,500 |
| Robert Lusardi | **2018** | **175,000** | **–** | **175,000** |
| | 2017 | 175,000 | – | 175,000 |
| Sally Williams[2] | **2018** | **–** | **–** | **–** |
| | 2017 | – | – | – |
| **Former Non-Executive Directors** | | | | |
| Tom Milligan[1] | **2018** | **43,750** | **–** | **43,750** |
| | 2017 | 175,000 | – | 175,000 |

1. Tom Milligan was appointed as a Non-Executive Director with effect from 3 February 2015 and retired effective 31 March 2018. His 2018 fees were proportionally pro-rated for the year.
2. Sally Williams was appointed on 10 July 2018 as a Non-Executive Director and her appointment took effect on 14 January 2019.
3. Samantha Hoe-Richardson is remunerated in GBP for her LUK Non-Executive Director fee and this is converted to USD at the average annual FX rate of 1.3420 for 2018 (1.2900 was used for 2017).

## 2019 annual bonus payments in respect of 2018 performance

As detailed in the Policy Report, each Executive Director participates in the annual bonus plan, under which performance is measured over a single financial year.

The target value of bonus was 150 per cent of salary for the CEO and CFO, and the maximum payable was two times the target value. The RoE is 2.4 per cent.

*Financial performance*

75 per cent of the 2018 bonus was based on Company performance conditions and the extent to which these were achieved is as follows:

| Performance Measure | Financial Performance Weighting (of total bonus) % | Threshold % | Target % | Max % | Actual performance % | % payout |
|---|---|---|---|---|---|---|
| Absolute RoE | 75 | RFRoR +6% | RFRoR +8% | RFRoR +14% | 2.4 | 0% of target payable in respect of Company performance |

In 2018 natural catastrophe losses occurred at above average frequency and financial returns were below the lower threshold targets. Bonus targets were set at the beginning of 2018 and based on a clear split between Company financial performance and personal performance on a 75:25 basis. The Company financial performance component paid out at 0 per cent of target as RoE was 2.4 per cent against a target level of RFRoR +8 per cent and a threshold of RFRoR +6 per cent.

*Personal performance*

25 per cent of the 2018 bonus was based on performance against clearly defined personal objectives set at the start of the year.

The table below sets out a summary of the 2018 personal objectives for each Executive Director.

| Executive Director | Personal performance |
|---|---|
| Alex Maloney | Effective leadership and management of the senior executive team and Group.<br>Development of the general business strategy.<br>Contribution aligned to the Lancashire Group Values. |
| Elaine Whelan | Effective leadership and management of the finance function and the Bermuda office.<br>Development of the general business strategy.<br>Contribution aligned to the Lancashire Group Values. |

The personal targets were broadly common among the Executive Directors, with variances being attributable to the specifics of their respective roles and performance targets relating to areas of personal development.

During the 2018 annual performance reviews of each Executive Director, a performance rating was assigned to determine the level of bonus payout for which each Executive Director was eligible.

Notwithstanding the financial performance of the Group in what was a higher than average year for catastrophe loss activity (in this regard please see the strategy and performance sections on pages 16 to 21 of this Annual Report and Accounts), the Executive Directors each achieved a strong performance rating against their objectives, in particular in delivering an underwriting portfolio which operated in such a way as to moderate loss exposures through a combination of underwriting discipline and a carefully structured reinsurance programme. The leadership of the Executive Directors in delivering a team of employees with strong professional skills at all levels throughout the Group and in particular the recruitment of new underwriting teams during the year (see pages 22 to 25 for further details) is considered by the Board to position the business well for the challenges and opportunities which lie ahead. For the 2018 performance against personal objectives, the ratings were determined following a process for the evaluation of performance of the Executive Directors against the agreed personal targets and discussion and agreement of the outcomes with the Chairman and members of the Board. The outcomes are expressed as a percentage of the maximum award as illustrated in the table below.

A table of performance measures and total 2018 bonus achievement is set out below:

| Executive Director | Financial performance (max % of total bonus) % | Personal performance (max % of total bonus) % | Bonus % of maximum awarded % | Total bonus value[1] $ | Value of bonus paid in cash (75 per cent of total bonus) $ | Value of bonus deferred into RSS awards (25 per cent of total bonus)[1] $ |
|---|---|---|---|---|---|---|
| Alex Maloney | 75 | 25 | 19 | 474,826 | 356,119 | 118,707 |
| Elaine Whelan | 75 | 25 | 19 | 326,048 | 244,536 | 81,512 |

1. 25 per cent of total bonus award will be deferred into RSS awards with one third vesting annually, each year, over a three-year period with the first third becoming exercisable in February 2020, subject to the Company not being in a closed period. These awards vest on the relevant dates subject to continued employment only.

## Long-term share awards with performance periods ending in the year – 2016 RSS award

The 2016 RSS awards were based on a three-year performance period ending on 31 December 2018 and vest following the determination of financial results by the Board. The tables below set out the achievement against the performance conditions attached to the award, resulting in aggregate vesting of 0 per cent, and the actual number of awards vesting.

| | TSR (relative to a comparator group of 11 companies) (relevant to 25% of the 2016 RSS awards) | | Average annual RoE (over three years in excess of 13-week Treasury bill rate) (relevant to 75% of the 2016 RSS awards) | |
|---|---|---|---|---|
| Performance level | Performance required | % vesting | Performance required (%) | % vesting |
| Below threshold | Below median | 0 | Below 6 | 0 |
| Threshold | Median | 25 | 6 | 25 |
| Stretch or above | Upper quartile or above | 100 | 15 or above | 100 |
| Actual achieved | Below median | 0 | 2.4 | 0 |

Details of the vesting for each Executive Director, based on the above, are shown in the table below:

| Executive Director | Number of shares at grant | Number of shares to lapse | Number of shares to vest | Dividend accrual on vested shares value[2] $ | Value of shares including dividend accrual[1] $ |
|---|---|---|---|---|---|
| Alex Maloney | 219,254 | 219,254 | 0 | 0 | 0 |
| Elaine Whelan | 157,104 | 157,104 | 0 | 0 | 0 |

1. The value of the vested shares is based on the 2016 RSS awards which vest at 0 per cent on 14 February 2019 and are based on a three-year performance period that ended on 31 December 2018.
2. Dividends accrue on awards at the record date of a dividend payment and upon exercise the cash value of the accrued dividends is paid to the employee on the number of vested awards net of tax required.

## Scheme interests awarded during the year

The table below sets out the performance RSS awards that were granted as nil-cost options on 23 February 2018.

| Executive Director | Grant date[2] | Number of awards granted during the year | Face value of awards granted during the year[1,3] $ | % vesting at threshold performance |
|---|---|---|---|---|
| Alex Maloney | 23-Feb-2018 | 315,762 | 2,532,876 | 25 |
| Elaine Whelan | 23-Feb-2018 | 198,755 | 1,594,308 | 25 |

1. The awards were based on the five-day average closing share price prior to the award date, being £5.74 (a share price of $8.02 based on the exchange rate of 1.3982) and the awards were granted as nil-cost options.
2. These awards are due to vest subject to performance conditions being met at the end of the performance period ending 31 December 2020 and becoming exercisable in the first open period following the release of the Company's 2020 year-end results after the meeting of the Board in February 2021.
3. The exercise share price is determined once an award has vested on the basis of the share price on the date an award is exercised.

## Loss of office payments

There were no loss of office payments during the 2018 year.

## Details of all outstanding share awards

In addition to awards made during the 2018 financial year, the table below sets out details of all outstanding RSS awards held by Executive Directors.

## Performance and deferred bonus awards under the RSS

| | | Grant date[1] | Exercise price | Awards held at 1-Jan-18 | Awards granted during the year | Awards vested during the year | Awards lapsed during the year | Awards exercised during the year | Awards held at 31-Dec-18 | End of performance period |
|---|---|---|---|---|---|---|---|---|---|---|
| Alex Maloney, Group CEO | Performance RSS[2,3] | 12-Feb-15 | – | 244,208 | – | **54,947** | **189,261** | **54,947** | – | 31-Dec-17 |
| | Deferred Bonus RSS[4] | 20-Mar-15 | – | 13,976 | – | **13,976** | – | **13,976** | – | |
| | Performance RSS[2,3] | 18-Feb-16 | – | 219,254 | – | – | – | – | **219,254** | 31-Dec-18 |
| | Deferred Bonus RSS[4] | 11-Mar-16 | – | 37,483 | – | **18,742** | – | **18,742** | **18,741** | |
| | Performance RSS[2,3] | 14-Mar-17 | – | 286,666 | – | – | – | – | **286,666** | 31-Dec-19 |
| | Deferred Bonus RSS[4] | 14-Mar-17 | – | 53,215 | – | **17,738** | – | **17,738** | **35,477** | |
| | Performance RSS[3,5] | 23-Feb-18 | – | – | **315,762** | – | – | – | **315,762** | 31-Dec-20 |
| | Deferred Bonus RSS[4] | 23-Feb-18 | – | – | **13,090** | – | – | – | **13,090** | |
| **Total** | | | | **854,802** | **328,852** | **105,403** | **189,261** | **105,403** | **888,990** | |
| Elaine Whelan, Group CFO & LICL CEO | Performance RSS[2,3] | 12-Feb-15 | – | 168,149 | – | **37,834** | **130,315** | **37,834** | – | 31-Dec-17 |
| | Deferred Bonus RSS[4] | 20-Mar-15 | – | 9,847 | – | **9,847** | – | **9,847** | – | |
| | Performance RSS[2,3] | 18-Feb-16 | – | 157,104 | – | – | – | – | **157,104** | 31-Dec-18 |
| | Deferred Bonus RSS[4] | 11-Mar-16 | – | 25,738 | – | **12,869** | – | **12,869** | **12,869** | |
| | Performance RSS[2,3] | 14-Mar-17 | – | 180,441 | – | – | – | – | **180,441** | 31-Dec-19 |
| | Deferred Bonus RSS[4] | 14-Mar-17 | – | 36,541 | – | **12,180** | – | **12,180** | **24,361** | |
| | Performance RSS[3,5] | 23-Feb-18 | – | – | **198,755** | – | – | – | **198,755** | 31-Dec-20 |
| | Deferred Bonus RSS[4] | 23-Feb-18 | – | – | **9,663** | – | – | – | **9,663** | |
| **Total** | | | | **577,820** | **208,418** | **72,730** | **130,315** | **72,730** | **583,193** | |

1. The market values of the common shares on the dates of grant were:
   - 12 February 2015 £6.36
   - 20 March 2015 £6.30
   - 18 February 2016 £6.17
   - 11 March 2016 £5.37
   - 14 March 2017 £7.02
   - 23 February 2018 £5.69
2. The vesting of the RSS performance awards above is subject to two performance conditions as follows:
   - 25 per cent of each award is subject to a performance condition measuring the TSR performance of the Company against the TSR performance of a select group of comparator companies (see page 86 for a list of comparator companies for each grant year), over a three-year performance period. 25 per cent of this part of the award vests for median performance by the Company, rising to 100 per cent vesting of this part of the award for upper quartile performance by the Company or better (with proportionate vesting between these two points).
   - The other 75 per cent of each award is subject to a performance condition based on average annual RoE over a three-year performance period. 25 per cent of this part of the award will vest if average annual RoE over the performance period exceeds the criteria set out in the table on page 85, whilst all of this part of the award will vest if the Company's average RoE is equal to the more stringent criteria set out in the table on page 85. Between these two points vesting will take place on a straight-line basis from 25 per cent to 100 per cent for RoE performance.
3. The vesting dates of the RSS performance awards are subject to being out of a closed period and are as follows:
   - 2015 – 15 February 2018;
   - 2016 – 14 February 2019;
   - 2017 – first open period following the release of the Company's 2019 year-end results; and
   - 2018 – first open period following the release of the Company's 2020 year-end results.
4. The vesting dates of the RSS Deferred Bonus awards are subject to being out of a closed period and, for the 2015 to 2018 Deferred Bonus awards, are as follows:
   - 2015 – vest 33.33 per cent per year over a three-year period at the first open period following the release of the Company's year-end results for 2015, 2016 and 2017;
   - 2016 – vest 33.33 per cent per year over a three-year period at the first open period following the release of the Company's year-end results for 2016, 2017 and 2018;
   - 2017 – vest 33.33 per cent per year over a three-year period at the first open period following the release of the Company's year-end results for 2017, 2018 and 2019; and
   - 2018 – vest 33.33 per cent per year over a three-year period at the first open period following the release of the Company's year-end results for 2018, 2019 and 2020.
5. The vesting of the RSS performance awards above is subject to two performance conditions as follows:
   - 15 per cent of each award is subject to a performance condition measuring the absolute TSR performance of the Company over a three-year performance period. 25 per cent of this part of the award vests for threshold (8 per cent compound annual growth) performance by the Company, rising to 100 per cent vesting of this part of the award for maximum performance (12 per cent compound annual growth) by the Company or better. Performance between threshold and maximum is determined on a straight-line basis.
   - The other 85 per cent of each award is subject to a performance condition based on the annual growth in FCBVS plus accrued dividends over a three-year performance period. 25 per cent of this part of the award will vest if annual growth in FCBVS plus accrued dividends over the performance period exceeds the criteria set out in the table on page 85, whilst all of this part of the award will vest if the Company's annual growth in FCBVS plus accrued dividends is equal to the more stringent criteria set out in the table on page 85. Between these two points vesting will take place on a straight-line basis. Within the three-year performance period each of the separate financial years will be treated as a separate element, each one contributing one-third to the overall outcome of the vesting of this element of the RSS award. Details of this calculation method were disclosed on page 69 of the 2017 Annual Report and Accounts.

## Relative TSR targets for RSS (25 per cent weighting)

| | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|
| 100% | 75th percentile | 75th percentile | 75th percentile | 75th percentile |
| 25% | = median | = median | = median | = median |
| Nil | < median | < median | < median | < median |

## RoE targets for RSS (75 per cent weighting)

| | 2014 | 2015 | 2016 | 2017* |
|---|---|---|---|---|
| 100% | RFRoR +15% | RFRoR +15% | RFRoR +15% | 13% |
| 25% | RFRoR + 6% | RFRoR + 6% | RFRoR + 6% | 6% |
| Nil | < RFRoR + 6% | < RFRoR + 6% | < RFRoR + 6% | < 6% |

* Average annual growth in FCBVS plus accrued dividends.

## Absolute TSR targets for RSS (15 per cent weighting)

| | 2018* | 2019* |
|---|---|---|
| 100% | 12% | 12% |
| 25% | 8% | 8% |
| Nil | < 8% | < 8% |

## Annual growth in FCBVS plus accrued dividends targets for RSS (85 per cent weighting)

| | 2018* | 2019* |
|---|---|---|
| 100% | 13% | 13% |
| 25% | 6% | 6% |
| Nil | < 6% | < 6% |

* See pages 79 and 80 for the vesting methodology to be applied for the 2018 and onwards RSS awards.

## Historical Peer Group Data for 2017 and prior RSS awards (relative TSR element)

| Peer Companies [13] | 2014 awards | 2015 awards | 2016 awards | 2017 awards |
|---|---|---|---|---|
| Amlin plc[1,6] | X | X | – | – |
| Arch Capital Group Limited[2, 5] | – | – | X | X |
| Argo Group International Holdings, Ltd. | X | X | X | X |
| Aspen Insurance Holdings Limited[3] | X | X | X | X |
| Axis Capital Holdings Limited | X | X | X | X |
| Beazley plc | X | X | X | X |
| Catlin Group Ltd.[4] | X | – | – | – |
| Endurance Specialty Holdings Ltd.[5,8] | X | X | X | – |
| Everest Re Group, Ltd.[6] | – | X | X | X |
| Greenlight Capital Re, Ltd.[11] | – | – | X | X |
| The Hanover Insurance Group[7] | – | X | X | X |
| Hiscox Ltd. | X | X | X | X |
| Montpelier Re Holdings Ltd.[7,8] | X | – | – | – |
| Novae Group plc[9,10] | – | X | X | X |
| Renaissance Re Holdings Ltd. | X | X | X | X |
| Third Point Reinsurance Ltd. [12] | – | – | X | X |
| Validus Holdings Ltd. [11] | X | X | X | X |
| XL Group Ltd[10,12] | – | X | X | X |

1. Mitsui Sumitomo Insurance Company acquired Amlin plc on 1 February 2016. Accordingly, the Committee decided to use Amlin plc as a comparator company up to 30 June 2015 and it was replaced with Everest Re Group, Ltd with effect from 1 July 2015.
2. Arch Capital Group Limited was added to the peer group of companies with effect from 1 October 2016 as a replacement for Endurance Specialty Holdings Ltd.
3. Apollo Funds announced on 28 August 2018 that it intended to acquire all outstanding common shares of Aspen Insurance Holdings Limited ('Aspen'). The transaction is due to close in the first half of 2019, subject to approval by regulators, Aspen shareholders and the satisfaction of other customary closing conditions. As a result of this announcement, Aspen ceased to be in the comparator peer group from 30 June 2018.
4. Catlin Group Ltd. was acquired by the XL Group Ltd. with effect from 1 May 2015 and so was used as a comparator company up to 31 December 2014 and was replaced by Novae Group plc.
5. Sompo Holdings Inc. announced on 5 October 2016 that it intended to acquire Endurance Specialty Holdings Ltd. ('Endurance'). The transaction subsequently achieved shareholder approval. Accordingly, the Committee decided to use Arch Capital Group Limited as a comparator company with effect from 1 October 2016 as a replacement for Endurance.
6. Everest Re Group, Ltd. was added to the peer group of companies with effect from 1 July 2015 as a replacement for Amlin plc.
7. The Hanover Insurance Group was added to the peer group of companies with effect from 1 January 2015 as a replacement for Montpelier Re Holdings Ltd.
8. Montpelier Re Holdings Ltd. was acquired by Endurance with effect from 31 July 2015 and so was used as a comparator company up to 31 December 2014 and was replaced by The Hanover Insurance Group.
9. Novae Group plc was added to the peer group of companies with effect from 1 January 2015 as a replacement for Catlin Group Ltd.
10. Novae Group plc was acquired by Axis Capital Holdings Limited with effect from 2 October 2017 and so was used as a comparator company up to 30 June 2017 and was replaced by XL Group Ltd as of 1 July 2017.
11. American International Group, Inc. announced on 22 January 2018 that it intended to acquire Validus Holdings Ltd ('Validus'). Accordingly, the Committee decided to use Greenlight Capital Re, Ltd as a comparator company with effect from 1 January 2018 as a replacement for Validus.
12. AXA announced on 5 March 2018 that it had entered into an agreement to acquire 100% of XL Group Ltd, which was approved by XL Group Ltd's common shareholders on 6 June 2018. Accordingly, the Committee decided to use Third Point Reinsurance Ltd as a comparator company with effect from 1 January 2018 as a replacement for XL Group Ltd.
13. For 2018 and onwards RSS awards the Board adopted a range of absolute TSR targets. See page 85 for further details.

## Directors' shareholdings and share interests

Formal shareholding guidelines were first introduced in 2012 and have subsequently been modified. The guidelines require the CEO and CFO to build and maintain a shareholding in the Company worth two times annual salary as set out in the Policy Report.

Details of the Directors' interests in shares are shown in the table below.

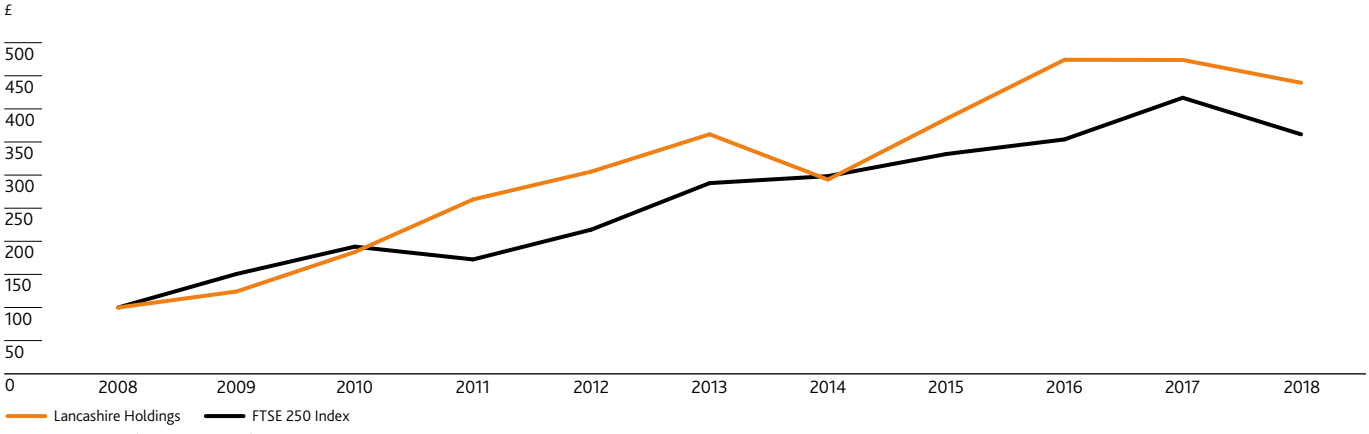
| | Number of Common Shares | | | | | | |
|---|---|---|---|---|---|---|---|
| | Total as at 1 January 2018 | As at 31 December 2018 | | | | | |
| Directors | | Legally owned | Subject to deferral under the RSS | Subject to performance conditions under the RSS | Vested but unexercised awards under other share-based plans | Total | Shareholding guideline achieved? |
| Alex Maloney | 1,435,104 | **657,724** | **67,308** | **821,682** | **N/A** | **1,546,714** | **Yes** |
| Elaine Whelan | 1,102,190 | **627,169** | **46,893** | **536,300** | **N/A** | **1,210,362** | **Yes** |
| Peter Clarke | 44,000 | **60,000** | **N/A** | **N/A** | **N/A** | **N/A** | **N/A** |
| Michael Dawson | 7,200 | **11,000** | **N/A** | **N/A** | **N/A** | **N/A** | **N/A** |
| Simon Fraser | 1,000 | **1,000** | **N/A** | **N/A** | **N/A** | **N/A** | **N/A** |
| Samantha Hoe-Richardson | 3,947 | **5,356** | **N/A** | **N/A** | **N/A** | **N/A** | **N/A** |
| Robert Lusardi | 3,000 | **8,000** | **N/A** | **N/A** | **N/A** | **N/A** | **N/A** |
| Sally Williams | – | **–** | **N/A** | **N/A** | **N/A** | **N/A** | **N/A** |

Note: Share ownership interest equivalent is defined as wholly owned shares or the net of taxes value of RSS awards which have vested but are unexercised and the net of tax value of deferred bonus RSS awards. Shares include those owned by persons closely associated with the relevant Executive Director.

## Performance graph

The following graph shows the Company's performance, measured by TSR, compared with the performance of the FTSE 250 Index. The Company's common shares commenced trading on the main market of the LSE on 16 March 2009 and the Company joined the FTSE 250 Index on 22 June 2009 and is currently a constituent of this.

TOTAL SHAREHOLDER RETURN




Source: Datastream (Thomson Reuters)

This graph shows the value, by 31 December 2018, of £100 invested in LHL on 31 December 2008 compared with the value of £100 invested in the FTSE 250 Index. The other points plotted are the values at intervening financial year ends.

## Total remuneration history for CEO

The table below sets out the total single figure of remuneration for the CEOs over the last ten years with the annual bonus paid as a percentage of the maximum and the percentage of long-term share awards vesting in each year.

| | 2009 | 2010 | 2011 | 2012 | 2013 | 2014[1] | 2014[2] | 2015 | 2016 | 2017 | **2018** |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Total remuneration ($000s) | 7,244 | 9,945 | 9,623 | 10,460 | 10,175 | 10,072 | 2,405 | 3,853 | 3,800 | 1,943 | **1,431** |
| Annual bonus (%) | 68 | 94 | 73 | 73 | 80 | 80 | 73 | 72 | 76 | 17 | **19** |
| LTI vesting (%) | N/A | 99.6 | 100 | 99 | 100 | 61[1] | 50 | 75 | 67 | 22.5[3] | **0** |

1. Richard Brindle was the CEO from 2005 until he retired from the Group and as a Director on 30 April 2014. Mr Brindle was afforded good leaver status and all RSS award interests were vested upon his departure, using estimated TSR and RoE values at the time of his retirement. The amounts in the table above reflect all awards which vested in 2014. Further particulars of the vesting were reported in the Group's 2014 Annual Report and Accounts.
2. Alex Maloney was appointed CEO effective 1 May 2014, after the retirement of Mr Brindle. For the purposes of this table his numbers have been pro-rated to account for only his time in office as CEO for 2014.
3. For 2017, the long-term incentive values were based on the 2015 RSS awards which vested at 22.5 per cent on 15 February 2018 and were based on a three-year performance period that ended on 31 December 2017. The values are re-presented from the 2017 Annual Report and Accounts based on the share price at the vesting date, 15 February 2018 ($8.397), and include the value of dividends accrued on vested shares.

The table above shows the total remuneration figure for the former CEO during each of the relevant financial years; figures for the current CEO are shown since his appointment to the position on 1 May 2014. The total remuneration figure includes the annual bonus and LTI awards which vested based on performance in those years. The annual bonus and LTI percentages show the payout for each year as a percentage of the maximum.

## Percentage change in CEO remuneration

The following table sets out the percentage change in the aggregate value of salary, benefits and bonus for the CEO from the preceding year and the average percentage change in respect of the employees of the Group taken as a whole.

| | Year-on-year change CEO[2] % | Average year-on-year change employees[1,3] % |
|---|---|---|
| Base salary | 4 | 5 |
| Benefits | 6 | 5 |
| Bonus | 13 | 33 |

1. Employee numbers were calculated on a per permanent employee headcount basis for the years ending 31 December 2018 and 31 December 2017, adjusted for any joiners and leavers during this period.
2. The underlying salary increase from 2017 to 2018 for the CEO was 3 per cent. However some amounts were paid in Sterling and converted at the average exchange rate of 1.3420 for the year, which has resulted in the overall 4 per cent base salary year-on-year change above.
3. The underlying salary increase from 2017 to 2018 for Group employees was a standard 3 per cent. The 5 per cent increase reflects staff promotions and other adjustments made during the year.

## Relative importance of the spend on pay

The following table sets out the percentage change in dividends and overall spend on pay in the year ended 31 December 2018 compared with the year ended 31 December 2017.

| | **2018 $m** | 2017 $m | Percentage change % |
|---|---|---|---|
| Employee remuneration costs | **56.9** | 39.8 | 43 |
| Dividends | **70.2** | 29.9 | 135 |

## Committee members, attendees and advice

For Remuneration Committee membership and attendance at meetings through 2018, please refer to page 68 of this Annual Report and Accounts. The Remuneration Committee's responsibilities are contained in its Terms of Reference, a copy of which is available on the Company's website. These responsibilities include determining the framework for the remuneration, including pension arrangements, for all Executive Directors, the Chairman and senior executives. The Committee is also responsible for approving employment contracts for senior executives.

## Remuneration Committee adviser

The Remuneration Committee is advised by the Executive Compensation practice at Aon plc. Aon was appointed by the Remuneration Committee in 2007. Aon has discussions with the Remuneration Committee Chairman regularly on Committee process and topics which are of particular relevance to the Company.

Aon ReInsurance Solutions (which is part of Aon but is a separate business division) provides reinsurance broking services to the Group.

The primary role of Aon is to provide independent and objective advice and support to the Committee's Chairman and members. In order to manage any possible conflict of interest, Aon operates as a distinct business within the Aon Group and there is a robust separation between the business activities and management of Aon and all other parts of the wider Aon Group. The Committee is satisfied that the advice that it receives is objective and independent. Aon is also a signatory to the Remuneration Consultants Group ('RCG') Code of Conduct which sets out guidelines for managing conflicts of interest, and has confirmed to the Committee its compliance with the RCG Code.

The total fees paid to Aon in respect of its services to the Committee for the year ended 31 December 2018 were $71,334 (2017 – $68,072). Fees are predominantly charged on a 'time spent' basis.

## Engagement with shareholders

Details of votes cast for and against the resolution to approve last year's Remuneration Report are shown below along with the votes to approve the 2017 Remuneration Policy which have been stated below; any matters discussed with shareholders during the year are provided in the Implementation of Remuneration Policy for 2019 section of the report starting on page 78.

| | Vote to approve 2017 Annual Report on Remuneration (at the 2018 AGM) | | Vote to approve 2017-2019 Remuneration Policy (at the 2017 AGM) | |
|---|---|---|---|---|
| | **Total number of votes** | **% of votes cast** | Total number of votes | % of votes cast |
| For | **135,967,463** | **80.6** | 144,229,951 | 94.8 |
| Against | **32,740,906** | **19.4** | 7,870,777 | 5.2 |
| Total | **168,708,369** | **100.0** | 152,100,728 | 100.0 |
| Abstentions | **205,726** | | 9,125,993 | |

Approved by the Board of Directors and signed on behalf of the Board.

**Simon Fraser**
Chairman of the Remuneration Committee

13 February 2019

## Overview of the Group

Lancashire Holdings Limited is a Bermuda incorporated company (Registered Company No. 37415) with operating subsidiaries in Bermuda and London, and two syndicates at Lloyd's.

The Company's common shares were admitted to trading on AIM in December 2005 and were subsequently moved up to the Official List and to trading on the main market of the LSE on 16 March 2009. The shares have been included in the FTSE 250 Index since 22 June 2009 and have a premium listing on the LSE.

## Principal activities

The Company's principal activity, through its wholly owned subsidiaries, is the provision of global specialty insurance and reinsurance products. On 7 November 2013, the Company completed the acquisition of CCL, an established Lloyd's insurance group, and in June 2013 established Kinesis, a third-party capital and underwriting management facility, to complement the Group's longstanding specialty insurance activities. An analysis of the Group's business performance can be found in the business review on pages 26 to 32.

## Dividends

For the year ended 31 December 2018, the following dividends were declared:

- a final dividend of $0.10 per common share was declared on 14 February 2018 and paid on 21 March 2018 in pounds sterling at the pound/U.S. dollar exchange rate of 1.3985 or £0.0715 per common share;
- an interim dividend of $0.05 per common share was declared on 25 July 2018 and paid on 12 September 2018 in pounds sterling at the pound/U.S. dollar exchange rate of 1.2715 or £0.0393 per common share; and
- a special dividend of $0.20 per common share was declared on 31 October 2018 and paid on 12 December 2018 in pounds sterling at the pound/U.S. dollar exchange rate of 1.3030 or £0.1535 per common share.

## Dividend policy

The Group intends to maintain a strong balance sheet at all times, while generating an attractive risk-adjusted total return for shareholders. We actively manage capital to achieve those aims. Capital management is expected to include the payment of a sustainable annual (interim and final) dividend, supplemented by special dividends from time to time. Dividends will be linked to past performance and future prospects.

Under most scenarios, the annual dividend is not expected to reduce from one year to the next. Special dividends are expected to vary substantially in size and in timing. The Board may cancel the payment of any dividend between declaration and payment for purposes of compliance with regulatory requirements or for exceptional business reasons.

## Current Directors

- Peter Clarke (Non-Executive Chairman)
- Michael Dawson (Non-Executive Director)
- Simon Fraser (Senior Independent Non-Executive Director)
- Samantha Hoe-Richardson (Non-Executive Director)
- Robert Lusardi (Non-Executive Director)
- Alex Maloney (Chief Executive Officer)
- Elaine Whelan (Chief Financial Officer)
- Sally Williams (Non-Executive Director)

## Directors' interests

The Directors' beneficial interests in the Company's common shares as at 31 December 2018 and 2017 including interests held by family members were as follows:

| Directors | Common shares held as at 31 December 2018 | Common shares held as at 31 December 2017 |
|---|---|---|
| Peter Clarke[1] | **60,000** | 44,000 |
| Michael Dawson[2] | **11,000** | 7,200 |
| Simon Fraser | **1,000** | 1,000 |
| Samantha Hoe-Richardson[3] | **5,356** | 3,947 |
| Robert Lusardi[4] | **8,000** | 3,000 |
| Alex Maloney[5] | **657,724** | 580,302 |
| Elaine Whelan[6] | **627,169** | 524,370 |
| Sally Williams[7] | **–** | – |

There have been no changes in Directors' shareholdings between the end of the financial year and the date of this Report.

1. Peter Clarke conducted the following transactions in the Company's shares during 2018:
   - 16 February – purchase of 16,000 shares at a price of £5.67 costing £90,705.56.
2. Michael Dawson conducted the following transactions in the Company's shares during 2018:
   - 16 February – purchase of 3,800 shares at a price of £5.89 costing £22,363.
3. Samantha Hoe-Richardson conducted the following transactions in the Company's shares during 2018:
   - 19 February – purchase of 1,409 shares at a price of £5.68 costing £7,999.60.
4. Robert Lusardi conducted the following transactions in the Company's shares during 2018:
   - 20 February – purchase of 5,000 shares at a price of $7.89 costing $39,450.
5. Includes 155,722 shares owned by his spouse, Amanda Maloney. Alex Maloney conducted the following transactions in the Company's shares during 2018:
   - 15 February – exercise of 54,947 RSS awards and 50,456 deferred bonus RSS awards and related sale of 49,681 shares to cover tax liabilities, at a price of £6.08 realising £302,042.59. The balance of 55,722 shares was transferred to his spouse, Amanda Maloney.
   - 16 February – purchase of 21,700 shares at a price of £5.73 costing £124,341.
6. Includes 11,590 shares owned by her spouse, Kilian Whelan. Elaine Whelan conducted the following transactions in the Company's shares during 2018:
   - 15 February – exercise of 37,834 RSS awards and 34,896 deferred bonus RSS awards and related sale of 3,431 shares to cover tax liabilities, at a price of £6.08 realising £20,859.24.
   - 16 February – purchase of 20,000 shares at a price of £5.90 costing £117,900.
   - 20 February – purchase of 13,500 shares at a price of £5.58 costing £75,262.50.
7. Sally Williams was appointed to the Board with effect from 14 January 2019.

## Transactions in own shares

The Company did not repurchase any of its own common shares during 2018 or 2017.

The Group's current repurchase programme has 20,134,192 common shares remaining to be purchased as at 31 December 2018 (approximately $172.7 million at the 31 December 2018 share price). Further details of the share repurchase authority and programme are set out in note 19 to the consolidated financial statements on page 156. The repurchase programme is subject to renewal at the 2019 AGM in an amount of up to 10 per cent of the then issued common share capital.

## Directors' remuneration

Details of the Directors' remuneration are set out in the Directors' Remuneration Report on pages 70 to 89.

## Substantial shareholders

As at 13 February 2019, the Company was aware of the following interests of 3 per cent or more in the Company's issued share capital:

| Name | Number of shares as at 13 February 2019 | % of shares in issue |
|---|---|---|
| Invesco Limited | 32,247,491 | 15.97 |
| Setanta Asset Management Limited | 26,367,532 | 13.06 |
| Franklin Mutual Advisers, LLC | 12,222,897 | 6.05 |
| Oppenheimer Funds | 10,000,000 | 4.95 |
| Frank W Cawood & Associates | 9,302,300 | 4.61 |
| Wellington Management | 9,047,266 | 4.48 |
| Dimensional Fund Advisors LP | 8,414,981 | 4.17 |
| BlackRock, Inc. | 7,823,145 | 3.87 |
| Vanguard Group | 7,546,539 | 3.74 |
| Troy Asset Management Limited | 7,444,804 | 3.69 |

## Corporate governance – compliance statement

The Company's compliance with the Code is summarised in the Corporate Governance section of this Report on pages 55 to 57.

The Board considers and the Company confirms, in accordance with the principle of 'comply or explain' that the Company has complied with the principles and provisions set out in the UK Corporate Governance Code throughout the year ended 31 December 2018.

## Health and safety

The Group considers the health and safety of its employees to be a management responsibility equal to that of any other function.

The Group operates in compliance with health and safety legislative requirements in Bermuda and the UK.

## Greenhouse gas emissions

The Group's greenhouse gas emissions are detailed in the engagement and sustainability section on page 43.

## Employees

The Group is an equal opportunity employer, and does not tolerate unfair discrimination of any kind in any area of employment or corporate life. The Group believes that education and training for employees is a continuous process and employees are encouraged to discuss training needs with their managers. The Group's health and safety, equal opportunities, training and other policies are available to all employees in the staff handbook which is available on the Group's intranet.

## Creditor payment policy

The Group aims to pay all creditors promptly and in accordance with contractual and legal obligations.

## Financial instruments and risk exposures

Information regarding the Group's risk exposures is included in the ERM report on pages 33 to 39 and in the risk disclosures section on pages 111 to 133 of the consolidated financial statements. The Group's use of derivative financial instruments can be found on pages 124 to 125.

## Accounting standards

The Group's consolidated financial statements are prepared on a going concern basis in accordance with accounting principles generally accepted under IFRS as adopted by the EU. Where IFRS is silent, as it is in respect of certain aspects relating to the measurement of insurance products, the IFRS framework allows reference to another comprehensive body of accounting principles. In such instances, the Group's management determines appropriate measurement bases, to provide the most useful information to users of the consolidated financial statements, using their judgement and considering U.S. GAAP.

## Annual general meeting

The notice of the 2019 AGM, to be held on 1 May 2019 at the Company's head office, Power House, 7 Par-la-Ville Road, Hamilton HM 11, Bermuda, is contained in a separate circular to shareholders which is made available to shareholders at the same time as this Annual Report and Accounts. The notice of the AGM is also available on the Company's website.

## Electronic and web communications

Provisions of the Bermuda Companies Act 1981 enable companies to communicate with shareholders by electronic and/or website communications. The Company will notify shareholders (either in writing or by other permitted means) when a relevant document or other information is placed on the website and a shareholder may request a hard copy version of the document or information.

## Going concern and viability statement

The business review section on pages 26 to 32 sets out details of the Group's financial performance, capital management, business environment and outlook. In addition, further discussion of the principal risks and material uncertainties affecting the Group can be found on pages 36 to 39. Starting on page 111, the risk disclosures section of the consolidated financial statements sets out the principal risks to which the Group is exposed, including insurance, market, liquidity, credit, operational and strategic, together with the Group's policies for monitoring, managing and mitigating its exposures to these risks. The Board considers annually and on a rolling basis a three-year strategic plan for the business which the Company progressively implements. A three-year plan period aligns to the short-tail nature of the Group's liabilities and the agility in the business model, allowing the Group to adapt capital and solvency quickly in response to market cycles, events and opportunities. This is consistent with the outlook period in the Group's ORSA report. The three-year strategic plan was last approved by the Board on 25 July 2018. The Board receives quarterly reports from the Group CRO and sets, approves and monitors risk tolerances for the business.

During 2018, the Board carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity. As part of this assessment the business plan was stressed for a number of severe but plausible scenarios and the impact on capital (on both an IFRS and Solvency II basis) evaluated. The Directors believe that the Group is well placed to manage its business risks successfully, having taken into account the current economic outlook. Accordingly, the Board believes that, taking into account the Group's current position, and subject to the principal risks faced by the business, the Group will be able to continue in operation and to meet its liabilities as they fall due for the period up to 31 December 2021, being the period considered under the Group's current three-year strategic plan.

The Directors have a reasonable expectation that the Company will be able to continue in operation and meet its liabilities as they fall due over the period to 31 December 2021. Accordingly, the Board has adopted and continues to consider appropriate the going concern basis in preparing the Annual Report and Accounts.

## Auditors

Resolutions will be proposed at the Company's 2019 AGM to re-appoint KPMG as the Company's auditors and to authorise the Directors to set the auditor's remuneration.

## Disclosure of information to the auditors

Each of the persons who is a Director at the date of approval of this Annual Report and Accounts confirms that:

- so far as the Director is aware, there is no relevant audit information of which the Company's auditors are unaware; and
- the Director has taken all the steps that he or she ought to have taken as a Director in order to make himself or herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Approved by the Board of Directors and signed on behalf of the Board.

**Christopher Head**
Company Secretary

13 February 2019

# Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and Accounts and the Group's consolidated financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Group and of the profit or loss of the Group for that year. The consolidated financial statements have been prepared in accordance with IFRS as adopted by the EU. Where IFRS, as adopted by the EU, is silent, as it is in respect of certain aspects relating to the measurement of insurance products, the IFRS framework allows reference to another comprehensive body of accounting principles. In such instances, the Group's management determines appropriate measurement bases to provide the most useful information to users of the consolidated financial statements, using their judgement and considering U.S. GAAP. Further detail on the basis of preparation is described in the consolidated financial statements. In preparing the consolidated financial statements, the Directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRS as adopted by the EU;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the Group's consolidated financial statements;
- provide additional disclosures where compliance with the specific requirements of IFRS as adopted by the EU are considered to be insufficient to enable users to understand the impact of particular transactions, events and conditions on the financial position and performance;
- assess the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Group or to cease operations or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the financial position of the Group, and enable them to ensure that the consolidated financial statements comply with applicable laws and regulations. They are also responsible for such internal control as they determine is necessary to enable the preparation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error, and also have general responsibility for safeguarding the assets of the Group and hence for taking reasonable steps for prevention and detection of fraud and other irregularities.

## Directors' responsibility statement

The Directors confirm that to the best of their knowledge:

- the consolidated financial statements, prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group;
- the Board considers the Annual Report and Accounts, taken as a whole, are fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy; and
- the strategy and the business review sections of this Annual Report and Accounts include a fair review of the development and performance of the business and the position of the Group, together with a description of the principal risks and uncertainties that the Group faces.

Legislation in Bermuda governing the preparation and dissemination of the consolidated financial statements may differ from legislation in other jurisdictions. In addition, the rights of shareholders under Bermuda law may differ from those for shareholders of companies incorporated in other jurisdictions.

By order of the Board

13 February 2019