PARTNERRE LTD
Form 10-Q
August 09, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2006

OR

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

For the transition period from ______ to ______.

Commission file number 1-14536

PartnerRe Ltd.

(Exact name of Registrant as specified in its charter)

Bermuda	**Not Applicable**
(State of incorporation)	**(I.R.S. Employer Identification No.)**

90 Pitts Bay Road, Pembroke, HM08, Bermuda

(Address of principal executive offices) (Zip Code)

(441) 292-0888

(Registrant s telephone number, including area code)

96 Pitts Bay Road, Pembroke, HM08, Bermuda

(Former name, former address and former fiscal year, if changed since last report)

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

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

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

The number of the Registrant s common shares (par value $1.00 per share) outstanding as of August 1, 2006 was 56,802,478.

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PartnerRe Ltd.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of PartnerRe Ltd.

We have reviewed the accompanying condensed consolidated balance sheet of PartnerRe Ltd. and subsidiaries as of June 30, 2006, and the related condensed consolidated statements of operations and comprehensive income for the three-month and six-month periods ended June 30, 2006 and 2005 and of shareholders equity and of cash flows for the six-month periods ended June 30, 2006 and 2005. These interim condensed consolidated financial statements are the responsibility of the Company s management.

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

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

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of PartnerRe Ltd. and subsidiaries as of December 31, 2005 and the related consolidated statements of operations and comprehensive income, shareholders equity and cash flows for the year then ended (not presented herein); and in our report dated March 1, 2006 (June 30, 2006 as to Note 20), we expressed an unqualified opinion on those consolidated financial statements, which included an explanatory paragraph relating to the restatement described in Note 20. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2005 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Deloitte & Touche
Deloitte & Touche

Hamilton, Bermuda
August 8, 2006

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PartnerRe Ltd.

Unaudited Condensed Consolidated Balance Sheets

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

	June 30, 2006	December 31, 2005
Assets		
Investments:		
Fixed maturities, available for sale, at fair value (amortized cost: 2006, $6,901,912; 2005, $6,682,243)	**$ 6,758,874**	$ 6,686,822
Short-term investments, available for sale, at fair value (amortized cost: 2006, $271,027; 2005, $231,442)	**270,485**	230,933
Equities, available for sale, at fair value (cost: 2006, $995,508; 2005, $1,246,192)	**1,059,029**	1,334,374
Trading securities, at fair value (cost: 2006, $295,505; 2005, $210,432)	**297,619**	220,311
Other invested assets	**98,321**	104,920
Total investments	**8,484,328**	8,577,360
Cash and cash equivalents, at fair value, which approximates amortized cost	**1,407,979**	1,001,378
Accrued investment income	**139,607**	143,548
Reinsurance balances receivable	**1,873,063**	1,493,507
Reinsurance recoverable on paid and unpaid losses	**196,539**	217,948
Funds held by reinsured companies	**988,127**	970,614
Deferred acquisition costs	**551,229**	437,741
Deposit assets	**302,598**	289,459
Net tax assets	**91,120**	87,667
Goodwill	**429,519**	429,519
Other	**87,291**	95,389
Total assets	**$ 14,551,400**	$ 13,744,130
Liabilities		
Unpaid losses and loss expenses	**$ 6,802,291**	$ 6,737,661
Policy benefits for life and annuity contracts	**1,279,769**	1,223,871
Unearned premiums	**1,650,518**	1,136,233
Reinsurance balances payable	**135,621**	127,607
Ceded premiums payable	**21,417**	25,110
Funds held under reinsurance treaties	**20,395**	18,910
Deposit liabilities	**348,951**	333,820
Net payable for securities purchased	**123,962**	93,318
Accounts payable, accrued expenses and other	**132,518**	128,627
Long-term debt	**620,000**	620,000
Debt related to trust preferred securities	**206,186**	206,186
Total liabilities	**11,341,628**	10,651,343
Shareholders Equity		
Common shares (par value $1.00, issued and outstanding: 2006, 56,799,778; 2005, 56,730,195)	**56,800**	56,730
Series C cumulative preferred shares (par value $1.00, issued and outstanding: 2006 and 2005, 11,600,000; aggregate liquidation preference: 2006 and 2005, $290,000,000)	**11,600**	11,600
Series D cumulative preferred shares (par value $1.00, issued and outstanding: 2006 and 2005, 9,200,000; aggregate liquidation preference: 2006 and 2005, $230,000,000)	**9,200**	9,200
Additional paid-in capital	**1,391,816**	1,373,992
Deferred compensation		(107)
Accumulated other comprehensive (loss) income:		

Net unrealized (losses) gains on investments (net of tax benefit (expense) amounting to: 2006, $11,439; 2005, ($13,639))	**(71,711)**		77,049
Currency translation adjustment	**52,209**		12,614
Retained earnings	**1,759,858**		1,551,709
Total shareholders equity	**3,209,772**		3,092,787
Total liabilities and shareholders equity	**$ 14,551,400**	$	13,744,130

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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PartnerRe Ltd.

Unaudited Condensed Consolidated Statements of Operations and Comprehensive Income

(Expressed in thousands of U.S. dollars, except share and per share data)

	For the three months ended June 30, 2006	For the three months ended June 30, 2005	For the six months ended June 30, 2006	For the six months ended June 30, 2005
Revenues				
Gross premiums written	**$ 817,610**	$ 767,457	**$ 2,190,456**	$ 2,213,393
Net premiums written	**$ 815,893**	$ 763,855	**$ 2,160,497**	$ 2,178,724
Decrease (increase) in unearned premiums	**43,070**	116,404	**(468,713)**	(402,053)
Net premiums earned	**858,963**	880,259	**1,691,784**	1,776,671
Net investment income	**108,320**	90,224	**208,272**	177,077
Net realized investment (losses) gains	**(58,928)**	55,588	**(3,830)**	92,970
Other income (loss)	**12,704**	(1,143)	**20,460**	11,659
Total revenues	**921,059**	1,024,928	**1,916,686**	2,058,377
Expenses				
Losses and loss expenses and life policy benefits	**541,377**	546,171	**1,040,195**	1,160,036
Acquisition costs	**199,425**	203,426	**398,682**	413,351
Other operating expenses	**76,482**	74,500	**150,912**	147,190
Interest expense	**13,200**	7,363	**25,921**	14,691
Net foreign exchange losses	**4,116**	2,456	**7,462**	2,442
Total expenses	**834,600**	833,916	**1,623,172**	1,737,710
Income before taxes and interest in earnings of equity investments	**86,459**	191,012	**293,514**	320,667
Income tax expense	**11,845**	33,497	**27,976**	54,289
Interest in earnings of equity investments	**2,917**	2,394	**5,236**	4,946
Net income	**$ 77,531**	$ 159,909	**$ 270,774**	$ 271,324
Preferred dividends	**8,631**	8,631	**17,263**	17,263
Net income available to common shareholders	**$ 68,900**	$ 151,278	**$ 253,511**	$ 254,061
Comprehensive income, net of tax				
Net income	**$ 77,531**	$ 159,909	**$ 270,774**	$ 271,324
Change in net unrealized gains or losses on investments	**(56,710)**	82,481	**(148,760)**	(8,317)
Change in currency translation adjustment	**29,870**	(35,308)	**39,595**	(60,742)
Comprehensive income	**$ 50,691**	$ 207,082	**$ 161,609**	$ 202,265
Per share data				
Net income per common share:				
Basic net income	**$ 1.21**	$ 2.76	**$ 4.47**	$ 4.63
Diluted net income	**$ 1.20**	$ 2.72	**$ 4.40**	$ 4.56
Weighted average number of common shares outstanding	**56,763.5**	54,791.5	**56,748.6**	54,873.6

Weighted average number of common and common share equivalents outstanding		**57,656.0**		55,698.7		**57,628.6**		55,764.5
Dividends declared per common share	**$**	**0.40**	$	0.38	**$**	**0.80**	$	0.76

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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PartnerRe Ltd.

Unaudited Condensed Consolidated Statements of Shareholders Equity

(Expressed in thousands of U.S. dollars)

	Common shares	Preferred shares	Additional paid-in capital	Deferred compensation	Net unrealized (losses) gains on investments, net of tax	Currency translation adjustment	Retained earnings	Total shareholders equity
Balance at December 31, 2005	**$ 56,730**	**$ 20,800**	**$ 1,373,992**	**$ (107)**	**$ 77,049**	**$ 12,614**	**$ 1,551,709**	**$ 3,092,787**
Issue of common shares	**70**		**17,824**					**17,894**
Amortization of deferred compensation				**107**				**107**
Net unrealized losses on investments					**(148,760)**			**(148,760)**
Currency translation adjustment						**39,595**		**39,595**
Net income							**270,774**	**270,774**
Dividends on common shares							**(45,362)**	**(45,362)**
Dividends on preferred shares							**(17,263)**	**(17,263)**
Balance at June 30, 2006	**$ 56,800**	**$ 20,800**	**$ 1,391,816**	**$**	**$ (71,711)**	**$ 52,209**	**$ 1,759,858**	**$ 3,209,772**

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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PartnerRe Ltd.

Unaudited Condensed Consolidated Statements of Shareholders Equity

(Expressed in thousands of U.S. dollars)

	Common shares	Preferred shares	Additional paid-in capital	Deferred compensation	Net unrealized gains (losses) on investments, net of tax	Currency translation adjustment	Retained earnings	Total shareholders equity
Balance at December 31, 2004	$ 54,854	$ 20,800	$ 1,288,292	$ (199)	$ 194,575	$ 72,510	$ 1,721,032	$ 3,351,864
Issue of common shares	426		24,420					24,846
Repurchase of common shares	(637)		(37,803)					(38,440)
Amortization of deferred compensation				46				46
Net unrealized losses on investments					(8,317)			(8,317)
Currency translation adjustment						(60,742)		(60,742)
Net income							271,324	271,324
Dividends on common shares							(41,629)	(41,629)
Dividends on preferred shares							(17,263)	(17,263)
Balance at June 30, 2005	$ 54,643	$ 20,800	$ 1,274,909	$ (153)	$ 186,258	$ 11,768	$ 1,933,464	$ 3,481,689

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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PartnerRe Ltd.

Unaudited Condensed Consolidated Statements of Cash Flows

(Expressed in thousands of U.S. dollars)

	For the six months ended June 30, 2006	For the six months ended June 30, 2005
Cash Flows from Operating Activities		
Net income	**$ 270,774**	$ 271,324
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of net premium on investments	**15,941**	23,264
Net realized investment losses (gains)	**3,830**	(92,970)
Changes in:		
Unearned premiums	**468,713**	402,053
Net reinsurance balances	**(327,949)**	(315,460)
Unpaid losses and loss expenses including life policy benefits	**(88,598)**	331,061
Net tax assets	**21,752**	45,322
Other changes in operating assets and liabilities	**9,021**	(74,795)
Net (purchases) sales of trading securities	**(69,281)**	10,055
Other, net	**7,600**	2,324
Net cash provided by operating activities	**311,803**	602,178
Cash Flows from Investing Activities		
Sales of fixed maturities	**1,418,577**	2,519,685
Redemptions of fixed maturities	**339,677**	402,303
Purchases of fixed maturities	**(1,897,256)**	(2,672,218)
Sales of short-term investments	**20,007**	101,748
Redemptions of short-term investments	**79,491**	9,827
Purchases of short-term investments	**(128,523)**	(254,650)
Sales of equities	**8,385,666**	1,800,634
Purchases of equities	**(8,073,219)**	(1,815,235)
Other, net	**9,812**	(7,169)
Net cash provided by investing activities	**154,232**	84,925
Cash Flows from Financing Activities		
Cash dividends paid to shareholders	**(62,625)**	(59,556)
Net issue (repurchase) of common shares	**3,361**	(20,458)
Contract fees on forward sale agreement	**(4,756)**	
Net cash used in financing activities	**(64,020)**	(80,014)
Effect of foreign exchange rate changes on cash	**4,586**	(7,236)
Increase in cash and cash equivalents	**406,601**	599,853
Cash and cash equivalents beginning of period	**1,001,378**	436,003
Cash and cash equivalents end of period	**$ 1,407,979**	$ 1,035,856
Supplemental cash flow information:		

Net taxes paid	**$**	**(6,445)**	$	(9,030)
Interest paid	**$**	**(25,263)**	$	(14,606)

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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PartnerRe Ltd.

Notes to Unaudited Condensed Consolidated Financial Statements

1. Organization

PartnerRe Ltd. (the Company) provides reinsurance on a worldwide basis through its principal, wholly owned subsidiaries, Partner Reinsurance Company Ltd. (Partner Reinsurance), PartnerRe SA and Partner Reinsurance Company of the U.S. (PartnerRe U.S.). Risks reinsured include, but are not limited to property, casualty, motor, agriculture, aviation/space, catastrophe, credit/surety, engineering, energy, marine, specialty property, specialty casualty, other lines and life/annuity and health. The Company also offers alternative risk products that include weather and credit protection to financial, industrial and service companies on a worldwide basis.

2. Significant Accounting Policies

The Company s Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) for interim financial information and with the instructions on Form 10-Q and Article 10 of Regulation S-X. The Condensed Consolidated Financial Statements include the accounts of the Company and its subsidiaries, including those that meet the consolidation requirements of variable interest entities (VIEs). The Company assesses the consolidation of VIEs based on whether the Company is the primary beneficiary of the entity in accordance with FASB Interpretation No. 46 (revised December 2003) Consolidation of Variable Interest Entities (FIN 46R). The Company consolidates the VIE if the Company is subject to a majority of the risk of loss from the entity s activities or is entitled to receive a majority of the entity s residual returns. Entities in which the Company has an ownership of more than 20% or less than 50% of the voting shares are accounted for using the equity method. Intercompany accounts and transactions have been eliminated. To facilitate comparison of information across periods, certain reclassifications have been made to prior year amounts to conform to the current year s presentation.

The preparation of financial statements in conformity with U.S. GAAP requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. While Management believes that the amounts included in the Condensed Consolidated Financial Statements reflect its best estimates and assumptions, actual results could differ from those estimates. The Company s principal estimates include:

- Unpaid losses and loss expenses, including policy benefits for life and annuity contracts;
- Gross and net premiums written and net premiums earned;
- Recoverability of deferred acquisition costs;
- Determination of other-than-temporary impairments of investments;
- Recoverability of tax loss carry-forwards;
- Valuation of goodwill; and
- Valuation of certain derivative financial instruments.

In the opinion of Management, all adjustments (which include normal recurring adjustments) necessary for a fair presentation of results for the interim periods have been made. The results for the three-month and six-month periods ended June 30, 2006 are not necessarily indicative of results to be expected for the full fiscal year. These Condensed Consolidated Financial Statements should be read in conjunction with the

Consolidated Financial Statements and notes thereto included in the Company s Annual Report on Form 10-K/A for the year ended December 31, 2005.

3. Share-Based Compensation

The Company adopted the fair value provisions of Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation (SFAS 123), as amended by SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure (SFAS 148), in 2003 and elected to use the prospective transition method as described in SFAS 123, which resulted in the expensing of options granted subsequent to January 1, 2003. Effective January 1, 2006, the Company adopted the provisions of SFAS No. 123 (revised 2004), Share-Based Payment (SFAS 123R) using the modified prospective method. Under both SFAS 123 and SFAS 123R, the fair value of the compensation cost is measured at grant date and is expensed over the period for which the employee is required to provide services in exchange for the award. SFAS 123R, however, requires that forfeiture benefits be estimated at the time of grant and incorporated in the determination of share-based compensation costs. For awards issued prior to the adoption of SFAS 123R, forfeiture benefits are recognized when employees leave the Company. SFAS 123R also differs from SFAS 123 in that it requires that awards granted to employees who are eligible for retirement and do not have to provide additional services be expensed at the date of grant. Awards granted to employees prior to the adoption of SFAS 123R continue to be amortized over the stated service period of the award and accelerated if the employee retires prior to the end of the service period.

During the first six months of 2006 and 2005, the Company s stock compensation expense was $12.0 million with a related tax benefit of $0.7 million and $7.6 million with no related tax benefit, respectively. The adoption of SFAS 123R resulted in additional compensation expense for the Company for the first six months of 2006 of $1.2 million, or approximately $0.02 per basic and diluted share.

Employee Equity Plan

The PartnerRe Ltd. 2005 Employee Equity Plan (the EEP), which is shareholder-approved, permits the grant of stock options, restricted shares (RS), restricted share units (RSU), stock appreciation rights (SAR) or other share-based awards to employees of the Company. Currently, the plan permits the grant of up to 2.2 million shares, of which a total of 750,000 shares can be issued as either RS or RSU. If an award under the EEP is cancelled or forfeited without the delivery of the full number of shares underlying such award, only the net number of shares actually delivered to the Participant will be counted against the EEP s authorized shares. If an outstanding award under the Company s predecessor equity plans is cancelled or forfeited without the delivery of the number of shares underlying such award, such undelivered shares will also be available for issuance under the EEP in addition to all other shares authorized for issuance. The number of shares that may be added back to the plan from net share settlement of share appreciation rights and options is capped at 400,000 shares over the life of the plan. Under the EEP, the exercise price of the award will not be less than the market value of the award at the time of grant. Awards issued under the EEP generally vest over 3 years of continuous service, either ratably or with a cliff-vest provision, are expensed ratably over the vesting period and have a ten-year contractual term.

Certain awards to certain senior executives will, if the Compensation Committee intends any such award to qualify as qualified performance based compensation under Section 162(m) of the Internal Revenue Code (IRC), become earned and payable only if pre-established targets relating to one or more of the following performance measures are achieved: (i) earnings per share, (ii) financial year return on common equity, (iii) underwriting year return on equity, (iv) return on net assets, (v) organizational objectives and (vi) premium growth. The individual maximum number of shares underlying any such share-denominated award granted in any year will be 800,000 shares, and the individual maximum amount earned with respect to any such non-share denominated award granted in any year will be $5,000,000.

Non-Employee Directors Stock Plan

The Non-Employee Directors Stock Plan (Directors Stock Plan), which is shareholder-approved, permits the grant of up to 0.5 million stock options, RS, RSU, alternative awards and other share-based awards. Under the Directors Stock Plan, the exercise price of the stock options will be equivalent to the market value of the stock options at the time of grant. Awards issued under the Directors Stock Plan generally vest at the time of grant, are expensed immediately and have a ten year contractual term.

Employee Share Purchase Plan

The Employee Share Purchase Plan (the ESPP), which is shareholder-approved, has one offering period per year with two purchase periods of six months. All employees are eligible to participate in the ESPP and can contribute between 1% and 10% of their base salary toward the purchase of the Company s shares up to the limit set by the IRC. Employees who enroll in the ESPP may purchase the Company s shares at a 15% discount of the fair market value. Participants in the ESPP are eligible to receive dividends on their shares as of the purchase date. A total of 300,000 common shares may be issued under the ESPP.

Swiss Share Purchase Plan

The Swiss Share Purchase Plan (the SSPP) has two offering periods per year with two purchase periods of six months. All full-time Swiss employees are eligible to participate in the SSPP and can contribute between 1% and 8% of their base salary toward the purchase of PartnerRe Ltd. shares up to a maximum of 5,000 Swiss francs per annum. Employees who enroll in the SSPP may purchase PartnerRe Ltd. shares at a 40% discount of the fair market value. Once purchased, there is a restriction on transfer or sale of these shares for a period of two years following purchase. Participants in the SSPP are eligible to receive dividends on their PartnerRe Ltd. shares as of the purchase date. A total of 200,000 common shares may be issued under the SSPP.

Under each of the Company s equity plans, the Company issues new shares upon the exercise of stock options or the conversion of RSU and SAR into shares.

Stock Options

In the first six months of 2006 the Company issued 71,870 stock options with a weighted average grant-date fair value of $14.86. In the first six months of 2005 the Company issued 460,019 stock options with a weighted average grant-date fair value of $17.14. In the first six months of 2006 and 2005, 36,133 stock options with a total grant-date value of $0.5 million, and 389,469 stock options with a total grant-date value of $5.0 million were exercised, respectively. The Company received $1.8 million and $16.4 million, respectively, from stock option exercises in the first six-months of 2006 and 2005. The activity related to the Company s stock options issued under all plans for the three-month and six-month periods ended June 30, 2006 was as follows:

	For the three months ended June 30, 2006		For the six months ended June 30, 2006	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding at beginning of period	3,321,714	$ 52.81	3,323,006	$ 52.79
Granted	71,870	63.21	71,870	63.21
Exercised	(34,841)	48.09	(36,133)	48.87
Forfeited	(6,141)	58.43	(6,141)	58.43
Expired	(2,880)	53.73	(2,880)	53.73
Outstanding at end of period	3,349,722	$ 53.05	3,349,722	$ 53.05
Ending vested options and options expected to vest			3,348,652	$ 53.05
Options exercisable at end of period			2,662,646	$ 51.73

The aggregate intrinsic value and weighted average remaining contractual term of stock options vested and expected to vest were $36.8 million and 6.4 years, respectively, at June 30, 2006. The aggregate intrinsic value and weighted average remaining contractual term of stock options exercisable at June 30, 2006 were $32.8 million and 6.1 years, respectively.

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The Company valued stock-options issued under all plans with a Black-Scholes valuation model and used the following assumptions:

	For the three months ended June 30, 2006	For the three months ended June 30, 2005	For the six months ended June 30, 2006	For the six months ended June 30, 2005
Weighted average assumptions used:				
Expected life	**6 years**	7 years	**6 years**	7 years
Risk-free interest rate	**5.0%**	4.2%	**5.0%**	4.1%
Expected volatility	**22.5%**	25.0%	**22.5%**	25.0%
Dividend yield	**2.6%**	2%	**2.6%**	2%

Prior to the adoption of SFAS 123R on January 1, 2006, the Company used historical experience to determine the expected life of stock options; an expected volatility equivalent to the historical volatility of the Company s common shares since inception of the Company; a risk-free interest rate based on the market yield of U.S securities with maturities equivalent to the expected life of the Company s stock options; and a dividend yield reflecting the inception-to-date average dividend yield of the Company. Since January 1, 2006, the Company has used the simplified method for vanilla options under Staff Accounting Bulletin No. 107 (SAB 107) to determine the expected life of options. Expected volatility is based on the historical volatility of the Company s common shares over a period equivalent to the expected life of the Company s options. The risk-free interest rate is based on the market yield of U.S securities with maturities equivalent to the expected life of the Company s options. The dividend yield is based on the average dividend yield of the Company s shares over the expected life of the Company s options.

Restricted Share Units (RSU)

The Company values RSU issued under all plans at the fair market value of its common shares at the time of grant. In the first six months of 2006, the Company issued 104,112 RSU with a weighted average grant date fair value of $61.12 per RSU and in the same period of 2005, the Company issued 213,993 RSU with a weighted average grant date fair value of $62.82.

The activity related to the Company s RSU for the three-month and six-month periods ended June 30, 2006 was as follows:

	For the three months ended June 30, 2006	For the six months ended June 30, 2006
RSU unvested and unreleased at beginning of period	392,021	294,174
Granted	5,530	104,112
Vested		(495)
Forfeited	(2,030)	(2,270)
RSU unvested and unreleased at end of period [(1)]	395,521	395,521

(1) Of the 395,521 RSU outstanding at June 30, 2006, 75,362 RSU were vested but were not released to the employees for conversion into share, as these RSU are subject to a 5 year block from the grant date.

Stock Appreciation Rights (SAR)

The Company issued SAR for the first time in the first quarter of 2006 and issued no SAR in the second quarter. The Company issued 155,270 SAR with a weighted average grant-date fair value of $14.31. No SAR were exercised, vested or forfeited during the first six-months of 2006.

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The Company valued SAR issued under all plans with a Black-Scholes valuation model and used the following assumptions:

	For the six months ended June 30, 2006
Weighted average assumptions used:	
Expected life	6 years
Risk-free interest rate	4.6%
Expected volatility	23.4%
Dividend yield	2.6%

The Company used the simplified method for vanilla options under SAB 107 to determine the expected life of SAR. Expected volatility is based on the historical volatility of the Company s common shares over a period equivalent to the expected life of the Company s SAR. The risk-free interest rate is based on the market yield of U.S securities with maturities equivalent to the expected life of the Company s SAR. The dividend yield is based on the average dividend yield of the Company s shares over the expected life of the Company s SAR.

Pro Forma Information

The following table illustrates the net effect on net income available to common shareholders and net income per share as if the fair value provisions of SFAS 123 had been applied retroactively to all outstanding share-based compensation issued (in thousands of U.S. dollars, except per share data):

	For the three months ended June 30, 2005	For the six months ended June 30, 2005
Net income available to common shareholders:		
As reported	$ 151,278	$ 254,061
Add: Stock-related compensation expense included in net income as reported	2,337	4,491
Less: Total stock-related compensation expense determined under fair value method for all grants	3,070	6,517
Pro forma	$ 150,545	$ 252,035
Net income per common share:		
Basic		
As reported	$ 2.76	$ 4.63
Pro forma	$ 2.75	$ 4.59
Diluted		
As reported	$ 2.72	$ 4.56
Pro forma	$ 2.70	$ 4.52

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4. Computation of Net Income per Common and Common Share Equivalents

	For the three months ended June 30, 2006	For the three months ended June 30, 2005	For the six months ended June 30, 2006	For the six months ended June 30, 2005
Basic net income per ordinary share:				
Net income	**$ 77,531**	$ 159,909	**$ 270,774**	$ 271,324
Less: preferred dividends	**8,631**	8,631	**17,263**	17,263
Net income available to common shareholders	**$ 68,900**	$ 151,278	**$ 253,511**	$ 254,061
Weighted average number of common shares outstanding	**56,763.5**	54,791.5	**56,748.6**	54,873.6
Basic net income per share	**$ 1.21**	$ 2.76	**$ 4.47**	$ 4.63
Diluted net income per ordinary share:				
Net income	**$ 77,531**	$ 159,909	**$ 270,774**	$ 271,324
Less: preferred dividends	**8,631**	8,631	**17,263**	17,263
Net income available to common shareholders	**$ 68,900**	$ 151,278	**$ 253,511**	$ 254,061
Weighted average number of common shares outstanding - basic	**56,763.5**	54,791.5	**56,748.6**	54,873.6
Stock options and other	**892.5**	907.2	**880.0**	890.9
Weighted average number of common and common share equivalents outstanding - diluted	**57,656.0**	55,698.7	**57,628.6**	55,764.5
Diluted net income per share	**$ 1.20**	$ 2.72	**$ 4.40**	$ 4.56

5. Legal Proceedings

Litigation

The Company s reinsurance subsidiaries, and the insurance and reinsurance industry in general, are subject to litigation and arbitration in the normal course of their business operations. In addition to claims litigation, the Company and its subsidiaries are subject to lawsuits and regulatory actions in the normal course of business that do not arise from or directly relate to claims on reinsurance treaties. This category of business litigation typically involves, inter alia, allegations of underwriting errors or misconduct, employment claims or regulatory activity. While the outcome of the business litigation cannot be predicted with certainty, the Company is disputing and will continue to dispute all allegations against the Company and/or its subsidiaries that Management believes are without merit.

As of June 30, 2006, the Company was not a party to any material litigation or arbitration other than as part of the ordinary course of business. While Management does not expect any of this will have a significant adverse effect on the Company s results of operations, financial condition and cash flows for a year, it does have the potential to adversely impact the results of a quarter.

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Subpoenas

The Company has received subpoenas from the office of the New York Attorney General (NYAG) and the SEC that seek information relating to the Company s investment in Channel Re and from the United States Attorney for the Southern District of New York requesting information relating to the Company s finite reinsurance products. In addition, the Company s wholly owned subsidiary, PartnerRe U.S., has received a subpoena from the Florida Office of Insurance Regulation requesting information in connection with its investigation of insurance industry practices related to finite reinsurance activities. The Company is cooperating with these requests for information.

6. New Accounting Pronouncements

FSP FAS 115-1 and FAS 124-1

In November 2005, the Financial Accounting Standards Board (FASB) issued FSP Nos. FAS 115-1 and FAS 124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments (FSP). The FSP addresses the determination as to when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss by reference to various existing accounting literature. The FSP replaces the guidance set forth in paragraphs 10 18 of EITF 03-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments, with references to existing other-than-temporary impairment guidance. The FSP supersedes EITF D-44, Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value and clarifies that an investor should recognize an impairment loss no later than when the impairment is deemed other-than-temporary, even if a decision to sell has not been made.

The Company adopted these new pronouncements on January 1 for its other-than-temporary impairment analysis conducted in the period beginning January 1, 2006. The adoption of these new pronouncements did not have a significant impact on the consolidated equity or net income of the Company.

SFAS 155

In February 2006, the FASB issued Statement No. 155 Accounting for Certain Hybrid Financial Instruments an amendment of FASB Statements No. 133 and 140 (SFAS 155). This Statement amends SFAS No. 133 Accounting for Derivative Instruments and Hedging Activities (SFAS 133) and SFAS No. 140 Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities (SFAS 140). This Statement resolves issues addressed in Statement 133 Implementation Issue No. D1 Application of Statement 133 to Beneficial Interests in Securitized Financial Assets . It permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation; clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS 133; establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation; clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and amends SFAS 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS 155 will be effective in periods that begin after September 15, 2006. The Company is currently evaluating the impact of the adoption of SFAS 155, if any, on its consolidated equity or net income.

FIN 48

In June 2006, the FASB issued Interpretation No. 48 Accounting for Uncertainty in Income Taxes (FIN 48). This Interpretation clarifies the accounting for uncertainty in income taxes recognized in financial statements in accordance with FASB Statement No. 109 Accounting for Income Taxes . FIN 48 prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. This Interpretation will be effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact of the adoption of FIN 48 and the impact on its consolidated equity or net income.

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7. Segment Information

The Company monitors the performance of its underwriting operations in three segments, Non-life, ART and Life. The Non-life segment is further divided into three sub-segments, U.S. Property and Casualty (U.S. P&C), Global (Non-U.S.) Property and Casualty (Global (Non-U.S.) P&C) and Worldwide Specialty. Segments and sub-segments represent markets that are reasonably homogeneous in terms of geography, client types, buying patterns, underlying risk patterns and approach to risk management.

The U.S. P&C sub-segment includes property, casualty and motor risks generally originating in the United States and written by PartnerRe U.S. The Global (Non-U.S.) P&C sub-segment includes property, casualty and motor risks generally originating outside of the United States, written by Partner Reinsurance and PartnerRe SA. The Worldwide Specialty sub-segment is comprised of business that is generally considered to be specialized due to the sophisticated technical underwriting required to analyze risks, and is global in nature, inasmuch as appropriate risk management for these lines requires a globally diversified portfolio of risks. This sub-segment consists of several lines of business for which the Company believes it has developed specialized knowledge and underwriting capabilities. These lines of business include agriculture, aviation/space, catastrophe, credit/surety, engineering, energy, marine, specialty property, specialty casualty and other lines. The ART segment includes structured risk transfer, principal finance, weather-related products and strategic investments, which includes the Company s share of Channel Re s net income. The Life segment includes life, health and annuity lines of business.

Because the Company does not manage its assets by segment, investment income is not allocated to the Non-life segment of the reinsurance operations. However, because of the interest-sensitive nature of some of the Company s Life and ART products, investment income is considered in Management s assessment of the profitability of the Life and ART segments. The following items are not considered in evaluating the results of each segment: net realized investment gains or losses, interest expense, net foreign exchange gains or losses, income tax expense or benefit and preferred share dividends. Segment results are shown net of intercompany transactions.

Management measures results for the Non-life segment on the basis of the loss ratio, acquisition ratio, technical ratio, other operating expense ratio and combined ratio. Management measures results for the Non-life sub-segments on the basis of the loss ratio, acquisition ratio and technical ratio. Management measures results for the ART segment on the basis of the underwriting result, which includes revenues from net premiums earned, other income and net investment income for ART, and expenses from losses and loss expenses, acquisition costs and other operating expenses. The Company s share of Channel Re s net income is part of the ART segment and is presented on the interest in earnings of equity investments line. Management measures results for the Life segment on the basis of the allocated underwriting result, which includes revenues from net premiums earned and allocated net investment income, and expenses from losses and loss expenses and life policy benefits, acquisition costs and other operating expenses.

The following tables provide a summary of the segment revenues and results for the three-month and six-month periods ended June 30, 2006 and 2005 (in millions of U.S. dollars, except ratios):

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Segment Information

For the three months ended June 30, 2006

	Global							
	U.S. P&C	**(Non-U.S.) P&C**	**Worldwide Specialty**	**Total Non-Life Segment**	**ART Segment[A]**	**Life Segment**	**Corporate**	**Total**
Gross premiums written	$ 170	$ 128	$ 408	$ 706	$ 7	$ 105	$	$ 818
Net premiums written	$ 170	$ 127	$ 409	$ 706	$ 7	$ 103	$	$ 816
Decrease (increase) in unearned premiums	35	54	(51)	38	1	4		43
Net premiums earned	$ 205	$ 181	$ 358	$ 744	$ 8	$ 107	$	$ 859
Losses and loss expenses and life policy benefits	(170)	(95)	(192)	(457)	(3)	(82)		(542)
Acquisition costs	(48)	(48)	(70)	(166)	(1)	(32)		(199)
Technical result	**$ (13)**	**$ 38**	**$ 96**	**$ 121**	**$ 4**	**$ (7)**	**$**	**$ 118**
Other income	n/a	n/a	n/a		13			13
Other operating expenses	n/a	n/a	n/a	(48)	(5)	(7)	(16)	(76)
Underwriting result	**n/a**	**n/a**	**n/a**	**$ 73**	**$ 12**	**$ (14)**	**n/a**	**$ 55**
Net investment income	n/a	n/a	n/a	n/a		13	95	108
Allocated underwriting result[1]	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**$ (1)**	**n/a**	**n/a**
Net realized investment losses	n/a	n/a	n/a	n/a	n/a	n/a	(59)	(59)
Interest expense	n/a	n/a	n/a	n/a	n/a	n/a	(13)	(13)
Net foreign exchange losses	n/a	n/a	n/a	n/a	n/a	n/a	(4)	(4)
Income tax expense	n/a	n/a	n/a	n/a	n/a	n/a	(12)	(12)
Interest in earnings of equity investments	n/a	n/a	n/a	n/a	3	n/a	n/a	3
Net income	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**$ 78**
Loss ratio[2]	83.0%	52.3%	53.7%	61.4%				
Acquisition ratio[3]	23.3	26.9	19.5	22.4				
Technical ratio[4]	106.3%	79.2%	73.2%	83.8%				
Other operating expense ratio[5]				6.5				
Combined ratio[6]				90.3%				

(A) The Company reports the results of Channel Re on a one-quarter lag. The 2006 and 2005 periods include the Company s share of Channel Re s net income in the amount of $2.8 million and $2.3 million, respectively.

(1) *Allocated underwriting result is defined as net premiums earned and allocated net investment income less life policy benefits, acquisition costs and other operating expenses.*

(2) *Loss ratio is obtained by dividing losses and loss expenses by net premiums earned.*

(3) *Acquisition ratio is obtained by dividing acquisition costs by net premiums earned.*

(4) *Technical ratio is defined as the sum of the loss ratio and the acquisition ratio.*

(5) *Other operating expense ratio is obtained by dividing other operating expenses by net premiums earned.*

(6) *Combined ratio is the sum of the technical ratio and the other operating expense ratio.*

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Segment Information

For the three months ended June 30, 2005

	U.S. P&C	Global (Non-U.S.) P&C	Worldwide Specialty	Total Non-Life Segment	ART Segment(A)	Life Segment	Corporate	Total
Gross premiums written	$ 150	$ 156	$ 345	$ 651	$ 7	$ 109	$	$ 767
Net premiums written	$ 150	$ 157	$ 344	$ 651	$ 7	$ 106	$	$ 764
Decrease (increase) in unearned premiums	51	58	6	115	(4)	5		116
Net premiums earned	$ 201	$ 215	$ 350	$ 766	$ 3	$ 111	$	$ 880
Losses and loss expenses and life policy benefits	(142)	(157)	(166)	(465)		(81)		(546)
Acquisition costs	(48)	(51)	(71)	(170)		(33)		(203)
Technical result	**$ 11**	**$ 7**	**$ 113**	**$ 131**	**$ 3**	**$ (3)**	**$**	**$ 131**
Other loss	n/a	n/a	n/a		(1)			(1)
Other operating expenses	n/a	n/a	n/a	(49)	(4)	(6)	(16)	(75)
Underwriting result	**n/a**	**n/a**	**n/a**	**$ 82**	**$ (2)**	**$ (9)**	**n/a**	**$ 55**
Net investment income	n/a	n/a	n/a	n/a		13	77	90
Allocated underwriting result[1]	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**$ 4**	**n/a**	**n/a**
Net realized investment gains	n/a	n/a	n/a	n/a	n/a	n/a	56	56
Interest expense	n/a	n/a	n/a	n/a	n/a	n/a	(7)	(7)
Net foreign exchange losses	n/a	n/a	n/a	n/a	n/a	n/a	(3)	(3)
Income tax expense	n/a	n/a	n/a	n/a	n/a	n/a	(33)	(33)
Interest in earnings of equity investments	n/a	n/a	n/a	n/a	2	n/a	n/a	2
Net income	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**$ 160**
Loss ratio[2]	70.7%	73.0%	47.5%	60.7%				
Acquisition ratio[3]	23.7	23.9	20.4	22.3				
Technical ratio[4]	94.4%	96.9%	67.9%	83.0%				
Other operating expense ratio[5]				6.4				
Combined ratio[6]				89.4%				

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Segment Information

For the six months ended June 30, 2006

	U.S. P&C	Global (Non-U.S.) P&C	Worldwide Specialty	Total Non-Life Segment	ART Segment(A)	Life Segment	Corporate	Total
Gross premiums written	$ 466	$ 493	$ 956	$ 1,915	$ 26	$ 249	$	$ 2,190
Net premiums written	$ 466	$ 491	$ 936	$ 1,893	$ 25	$ 242	$	$ 2,160
Increase in unearned premiums	(62)	(126)	(255)	(443)	(10)	(15)		(468)
Net premiums earned	$ 404	$ 365	$ 681	$ 1,450	$ 15	$ 227	$	$ 1,692
Losses and loss expenses and life policy benefits	(313)	(232)	(319)	(864)	(7)	(169)		(1,040)
Acquisition costs	(99)	(99)	(133)	(331)	(2)	(66)		(399)
Technical result	**$ (8)**	**$ 34**	**$ 229**	**$ 255**	**$ 6**	**$ (8)**	**$**	**$ 253**
Other income	n/a	n/a	n/a		20			20
Other operating expenses	n/a	n/a	n/a	(96)	(9)	(14)	(32)	(151)
Underwriting result	**n/a**	**n/a**	**n/a**	**$ 159**	**$ 17**	**$ (22)**	**n/a**	**$ 122**
Net investment income	n/a	n/a	n/a	n/a		24	184	208
Allocated underwriting result[1]	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**$ 2**	**n/a**	**n/a**
Net realized investment losses	n/a	n/a	n/a	n/a	n/a	n/a	(3)	(3)
Interest expense	n/a	n/a	n/a	n/a	n/a	n/a	(26)	(26)
Net foreign exchange losses	n/a	n/a	n/a	n/a	n/a	n/a	(7)	(7)
Income tax expense	n/a	n/a	n/a	n/a	n/a	n/a	(28)	(28)
Interest in earnings of equity investments	n/a	n/a	n/a	n/a	5	n/a	n/a	5
Net income	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**$ 271**
Loss ratio[2]	77.5%	63.7%	46.8%	59.6%				
Acquisition ratio[3]	24.5	27.0	19.6	22.9				
Technical ratio[4]	102.0%	90.7%	66.4%	82.5%				
Other operating expense ratio[5]				6.6				
Combined ratio[6]				89.1%				

(A) The Company reports the results of Channel Re on a one-quarter lag. The 2006 and 2005 periods include the Company s share of Channel Re s net income in the amount of $5.1 million and $4.8 million, respectively.

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Segment Information

For the six months ended June 30, 2005

	U.S. P&C	Global (Non-U.S.) P&C	Worldwide Specialty	Total Non-Life Segment	ART Segment(A)	Life Segment	Corporate	Total
Gross premiums written	$ 461	$ 589	$ 920	$ 1,970	$ 13	$ 230	$	$ 2,213
Net premiums written	$ 462	$ 587	$ 895	$ 1,944	$ 13	$ 222	$	$ 2,179
Increase in unearned premiums	(39)	(130)	(215)	(384)	(8)	(11)		(403)
Net premiums earned	$ 423	$ 457	$ 680	$ 1,560	$ 5	$ 211	$	$ 1,776
Losses and loss expenses and life policy benefits	(304)	(308)	(386)	(998)		(162)		(1,160)
Acquisition costs	(102)	(113)	(141)	(356)	(1)	(56)		(413)
Technical result	**$ 17**	**$ 36**	**$ 153**	**$ 206**	**$ 4**	**$ (7)**	**$**	**$ 203**
Other income	n/a	n/a	n/a		12			12
Other operating expenses	n/a	n/a	n/a	(102)	(6)	(11)	(28)	(147)
Underwriting result	**n/a**	**n/a**	**n/a**	**$ 104**	**$ 10**	**$ (18)**	**n/a**	**$ 68**
Net investment income	n/a	n/a	n/a	n/a		25	152	177
Allocated underwriting result[1]	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**$ 7**	**n/a**	**n/a**
Net realized investment gains	n/a	n/a	n/a	n/a	n/a	n/a	93	93
Interest expense	n/a	n/a	n/a	n/a	n/a	n/a	(15)	(15)
Net foreign exchange losses	n/a	n/a	n/a	n/a	n/a	n/a	(3)	(3)
Income tax expense	n/a	n/a	n/a	n/a	n/a	n/a	(54)	(54)
Interest in earnings of equity investments	n/a	n/a	n/a	n/a	5	n/a	n/a	5
Net income	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**$ 271**
Loss ratio[2]	71.9%	67.4%	56.7%	63.9%				
Acquisition ratio[3]	24.0	24.8	20.8	22.9				
Technical ratio[4]	95.9%	92.2%	77.5%	86.8%				
Other operating expense ratio[5]				6.5				
Combined ratio[6]				93.3%				

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8. Summarized Financial Information of ChannelRe Holdings Ltd.

The following tables provide summarized financial information for ChannelRe Holdings for 2006 and 2005. As the Company reports its share of ChannelRe Holdings on a one-quarter lag, the results presented below included summarized financial information as follow:

The three-month periods include results from January 1 to March 31.

The six-months periods include results from October 1 to March 31.

As ChannelRe Holdings has a financial year-end of December 31, the results presented below, which combined quarterly information from two financial years, are not presented in the annual financial statements of ChannelRe Holdings.

Balance Sheet Data (in millions of U.S. dollars):

	March 31, 2006	September 30, 2005
Total investments available for sale	**$ 593**	$ 579
Cash and cash equivalents	**6**	5
Deferred acquisition costs	**46**	48
Other assets	**10**	9
Total assets	**$ 655**	$ 641
Deferred premium revenue	**$ 180**	$ 187
Loss and loss adjustment expense reserves	**17**	14
Other liabilities	**6**	5
Total liabilities	**203**	206
Minority interest	**128**	121
Shareholders equity	**324**	314
Total liabilities, minority interest and shareholders equity	**$ 655**	$ 641

Income Statement Data (in millions of U.S. dollars):

	For the three months ended March 31, 2006	For the three months ended March 31, 2005	For the six months from October 1, 2005 to March 31, 2006	For the six months from October 1, 2004 to March 31, 2005
Premiums earned	**$ 16**	$ 16	**$ 32**	$ 32
Net investment income	**6**	4	**11**	8
Total revenues	**22**	20	**43**	40
Losses incurred	**2**	2	**4**	3
Amortization of deferred acquisition costs	**4**	4	**8**	8
Other expenses	**2**	3	**6**	5
Total expenses	**8**	9	**18**	16

Minority interest		**(4)**		(3)		**(7)**		(7)
Net income	**$**	**10**	$	8	**$**	**18**	$	17

There is diversity in practice among financial guarantee insurers and reinsurers with respect to their accounting policies for loss reserves. Current accounting literature does not specifically address the unique characteristics of financial guarantee insurance contracts. The Securities and Exchange Commission has held preliminary discussions with the financial guarantee industry and the Financial Accounting Standards Board (FASB) in 2005, and the industry is expecting final guidance by the end of 2006. Such final guidance may require ChannelRe and its financial guarantee peers to change some aspects of their respective loss reserving policies and the potential change could extend to premium and expense recognition. The Company cannot currently assess how the FASB and SEC Staff s ultimate resolution of the issue will impact ChannelRe.

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

Executive Overview

The Company operates on a global basis providing multi-line reinsurance to insurance companies. The Company also offers alternative risk products that include weather and credit protection to financial, industrial and service companies. The Company writes all lines of business in virtually all markets worldwide, and differentiates itself through its approach to risk, its strategy to manage risk, and its financial strength.

Reinsurance is by its nature a risk assumption business. The Company s philosophy is to assume its clients risks, thereby removing their volatility associated with these risks, and then to manage those risks and risk-related volatility. The Company s ability to succeed in the risk assumption business is dependent on its ability to accurately analyze and quantify risk, to understand volatility and how risks aggregate or correlate, and to establish the appropriate capital requirements and absolute limits for the risks assumed. The reinsurance markets have historically been highly cyclical in nature. The cycle is driven by competition, the amount of capital and capacity in the industry, loss events, and investment returns. The Company s long-term strategy to generate shareholder value focuses on broad product and geographic diversification of risks, assuming a moderately greater degree of risk than the market average, actively managing its capital across its risk portfolio and over the duration of the cycle, transactional excellence, and achieving superior returns on invested assets in the context of a disciplined risk framework.

For an expanded discussion, see the Executive Overview in the Company s 2005 Annual Report on Form 10-K/A.

Key Financial Measures

In addition to the Consolidated Balance Sheets and Consolidated Statement of Operations and Comprehensive Income, Management uses four key financial measures to evaluate its financial performance as well as the overall growth in value generated for the Company s common shareholders.

See the Key Financial Measures in the Company s 2005 Annual Report on Form 10-K/A for a discussion of book value per share, the dividend policy, ROE and the combined ratio.

Other Key Issues of Management

The Company s 2005 Annual Report on Form 10-K/A includes a discussion of Other Key Issues of Management. The following discussion updates and expands the Risk Management section included in that report.

Risk Management

Management believes that every organization faces numerous risks that could threaten the successful execution of the Company s goals and objectives. These include choice of strategy and markets, economic and business cycles, competition, changes in regulation, data quality and security, fraud, business interruption and management continuity, all factors which can be viewed as either strategic or operational risks that are common to any industry. In addition to these risks, the Company operates as an assumer of risk and its results are primarily determined by how well the Company understands, prices and manages risk. While many industries and companies start with a return goal and then attempt to shed risks that may derail that goal, the Company starts with a capital-based risk appetite and then looks for risks that meet its return targets within that framework. Management believes that this construct allows the Company to balance the cedants need for absolute certainty of claims payment with shareholders need for an adequate return on their capital.

The Company s risk management framework encompasses all the risks faced by the Company: the strategic risks that it shares with the rest of the reinsurance industry, assumed risks (the reinsurance and capital market risks that it is paid to assume) and the operational risks that are a part of running any business. Management identifies and categorizes risks in terms of their source, their impact on the Company and the preferred strategies for dealing with them. It takes an integrated approach, because it is impossible to manage any of these risks in isolation. There are interrelationships and dependencies between the various categories of risk. Each must be viewed in the context of the whole if their potential impact on the organization is to be fully understood and effectively managed.

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The Executive Management and the Board are responsible for managing strategic risks and setting key risk policies and limits. These risks include the direction and governance of the Company, as well as its response to key external factors faced by the reinsurance industry. Operational risks are managed by designated functions within the organization. They include failures or weaknesses in financial reporting and controls, non-compliance, poor cash management, fraud, breach of information technology security and reliance on third party vendors. The Company seeks to minimize these risks through robust processes and controls. Controls and monitoring processes throughout the organization ensure that Management and the Board have a comprehensive view of the Company s risks and related mitigation strategies at all times. Individual business units manage assumed risks, subject to the limits and policies established by the Executive Management and the Board. These are the reinsurance risks that the Company s clients want to transfer and are the core of the Company s business. They also include the capital market risks that the Company assumes in the investment of its assets.

At a strategic level, the Company manages these risks through diversification and absolute limits. At an operational level, risk mitigation strategies for assumed risks include strong processes, technical risk assessment and collaboration among different groups of professionals who each contribute a particular area of expertise.

The Company maintains a risk appetite moderately above the average of the reinsurance market because Management believes that this position offers the best potential for creating shareholder value at an acceptable risk level. Therefore, the most profitable products generally present the most volatility and potential downside risk. The Company manages that risk through diversification, and absolute limits on any one risk. The Company accepts that results on a quarterly basis may be volatile, however it seeks to protect itself from downside risk that can materially impair its balance sheet. The limits imposed represent the boundaries of risk tolerance and are based on the amount of capital that may be lost.

The major risks to the Company s balance sheet are typically due to events that Management refers to as shock losses. The Company defines a shock loss as an event that has the potential to materially damage economic value. The Company calculates its economic value as the difference between the net present value of tangible assets and the net present value of liabilities, using appropriate risk discount rates. For traded assets, the calculated net present values are equivalent to market values.

There are three areas of risk that the Company has currently identified as having the greatest potential for shock losses. These are catastrophe, reserving for casualty and other long-tail lines, and equity investment risk. The Company manages the risk of shock losses by setting limits on its tolerance for specific risks and on the amount of capital that it is willing to expose to such risks. The Company establishes limits to manage the absolute maximum foreseeable loss from any one event and considers the possibility that several shock losses could occur at one time, for example a major catastrophe event accompanied by a collapse in the equity markets. Management believes that the limits that it has placed on shock losses will allow the Company to continue writing business in such an event.

Other risks such as interest rate risk and credit risk have the ability to impact results substantially and may result in volatility in results from quarter to quarter, but Management believes that by themselves they are unlikely to represent a material downside threat to the Company s long-term economic value. See Quantitative and Qualitative Disclosures about Market Risk in Item 3 of this report for additional disclosure on interest rate risk, foreign currency risk, credit risk and equity price risk.

Catastrophe Risk

The Company defines this risk as the risk that the aggregate losses from natural perils materially exceed the net premiums that are received to cover such risks. The Company considers both the loss of capital due to a single large event and the loss of capital that would occur from multiple (but potentially smaller) events in any year.

The Company imposes an absolute limit to catastrophe risk from any single loss through exposure limit caps in each zone and to each peril, with the largest zonal limit currently set at no more than $1.25 billion. This risk is managed through the real time allocation of catastrophe exposure capacity on each exposure zone to different business units, regular modeling of aggregate loss scenarios through proprietary models, and a combination of quantitative and qualitative analysis. A zone is a geographic area in which the insurance risks are considered to be correlated to a single catastrophic event. Not all zones have the same limit and zones are broadly defined so that it would be highly unlikely for any single event to substantially erode the aggregate exposure limits from more than one zone. Even extremely high severity/low likelihood events will only partially exhaust the limits in any zone, as they are likely to only affect a part of the area covered by a wide zone.

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The Company also manages its exposures so that the chance that an economic loss to the Company from all catastrophe losses in any one year exceeds $750 million has a modeled probability of occurring less than once in 75 years. To measure this probability, the Company uses proprietary models that take into account not only the exposures in any zone, but also the likely frequency and severity of catastrophic events. This quantitative analysis is supplemented with the professional judgment of experienced underwriters.

Casualty Reserving Risk

The Company defines this risk as the risk that the estimates of ultimate losses for casualty and other long-tail lines that underlie its booked reserves will prove to be too low, leading to substantial reserve strengthening. The tolerance set by the Company for this risk is measured using total earned premium for casualty and other long-tail lines. Total earned premiums for casualty and other long-tail lines for the four most recent underwriting periods is currently limited to $3 billion.

One of the greatest risks in long-tail lines of business, and particularly in U.S. casualty, is that the loss trends are higher than the assumptions underlying the Company s ultimate loss estimates, resulting in ultimate losses that exceed recorded loss reserves. When loss trends prove to be higher than those underlying the reserving assumptions, the risk is great because of a stacking up effect: for long-tail lines, the Company carries reserves to cover claims arising from several years of underwriting activity and these reserves are likely to be adversely affected by unfavorable loss trends. The effect is likely to be more pronounced for recent underwriting years because, with the passage of time, actual loss emergence and data provide greater confidence around the adequacy of ultimate liability estimates for older underwriting years. Management believes that the volume of long-tail business most exposed to these reserving uncertainties should be limited to a predetermined amount.

The Company manages and mitigates the reserve risk for long-tail lines in a variety of ways. Underwriters and pricing actuaries follow a disciplined underwriting process that utilizes all available data and information, including industry trends. The Company establishes prudent reserving policies for determining carried reserves. These policies are systematic and Management endeavors to apply them consistently over time. See Critical Accounting Policies and Estimates - Losses and Loss Expenses and Life Policy Benefits below.

Equity Investment Risk

The Company defines this risk as the risk of a substantial decline in the value of its equity securities during the year. The tolerance set by the Company for this risk is measured using the value of equity securities as a percentage of available economic capital and is currently set at $2 billion. Assuming equity risk (and equity-like risks such as high yield bonds and convertible securities) within that part of the investment portfolio that is not required to support liability funds provides valuable diversification from other risk classes, along with the potential for higher returns. However, an overweight position could lead to a large loss of capital and impair the balance sheet in the case of a market crash.

The Company manages its equity exposure within strict guidelines, with a cap on assets other than investment-grade bonds set at no more than $2 billion. The Company sets strict limits on investments in any one name and any one industry, which creates a diversified portfolio and allows Management to focus on the systemic effects of equity risks. Systemic risk is managed by asset allocation, subject to strict caps on other than investment-grade bonds as a percentage of capital. A fully integrated information system provides real-time data on the investment portfolios, allowing for continuous monitoring and decision-support. Each portfolio is managed against a pre-determined benchmark to enable alignment with appropriate risk parameters and achievement of desired returns.

Critical Accounting Policies and Estimates

See the discussion of the Company s Critical Accounting Policies and Estimates in Management s Discussion and Analysis of Financial Condition and Results of Operations included in the Company s 2005 Annual Report on Form 10-K/A. The following discussion updates specific information related to the Company s estimates for unpaid loss and loss expense reserves and life policy benefits since December 31, 2005.

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Losses and Loss Expenses and Life Policy Benefits

Because a significant amount of time can lapse between the assumption of risk, occurrence of a loss event, the reporting of the event to an insurance company (the primary company or the cedant), the subsequent reporting to the reinsurance company (the reinsurer) and the ultimate payment of the claim on the loss event by the reinsurer, the Company s liability for unpaid losses and loss expenses (loss reserves) is based largely upon estimates. The Company categorizes loss reserves into three types of reserves: reported outstanding loss reserves (case reserves), additional case reserves (ACRs) and incurred but not reported (IBNR) reserves. Case reserves represent unpaid losses reported by the Company s cedants and recorded by the Company. ACRs are established for particular circumstances where, on the basis of individual loss reports, the Company estimates that the particular loss or collection of losses covered by a treaty may be greater than those advised by the cedant. IBNR reserves represent a provision for claims that have been incurred but not yet reported to the Company, as well as future loss development on losses already reported, in excess of the case reserves and ACRs. Unlike case reserves and ACRs, IBNR reserves are generally calculated in the aggregate for each line of business and they cannot usually be identified as reserves for a particular loss or treaty. The Company updates its estimates for each of the aforementioned categories on a quarterly basis using information received from its cedants. The Company also estimates the future unallocated loss adjustment expenses associated with the loss reserves (ULAE) and these form part of the Company s loss adjustment expense reserves. The Company s Non-life loss reserves for each category and sub-segment are reported in the table included later in this section.

The amount of time that elapses before a claim is reported to the cedant and then subsequently reported to the reinsurer is commonly referred to in the industry as the reporting tail. Lines of business for which claims are reported quickly are commonly referred to as short-tail lines; and lines of business for which a longer period of time elapses before claims are reported to the reinsurer are commonly referred to as long-tail lines. In general, for reinsurance, the time lags are longer than for primary business due to the delay that occurs between the cedant becoming aware of a loss and reporting the information to its reinsurer(s). The delay varies by reinsurance market (country of cedant), type of treaty, whether losses are paid by the cedant and the size of the loss. The delay could vary from a few weeks to a year or sometimes longer. For both short and long-tail lines, the Company s objective is to estimate ultimate losses and loss expenses. Total loss reserves are then calculated by subtracting losses paid. Similarly, IBNR reserves are calculated by subtraction of case reserves and ACRs from total loss reserves.

The Company analyzes its ultimate losses and loss expenses after consideration of the loss experience of various reserving cells. The losses on each treaty for every underwriting year are assigned to a reserving cell. An underwriting year is the year during which the reinsurance treaty was entered into as opposed to the year in which the loss occurred (accident year), or the calendar year for which financial results are reported. The reserving cells are selected in order to ensure that the underlying treaties have homogeneous loss development characteristics (e.g., reporting tail) but are large enough to make estimation of trends credible. The selection of reserving cells is reviewed annually and changes over time as the business of the Company evolves. For each reserving cell, the Company s estimates of loss reserves are reached after a review of the results of several commonly accepted actuarial projection methodologies. In selecting its best estimate, the Company considers the appropriateness of each methodology to the individual circumstances of the cell and underwriting year for which the projection is made. The methodologies that the Company employs include, but may not be limited to, paid loss development methods, incurred loss development methods, paid Borhuetter Ferguson (B-F) methods, incurred B-F methods, loss ratio methods and Bektander methods. In addition, the Company uses other methodologies to estimate liabilities for specific types of claims. For example, internal and vendor catastrophe models are typically used in the estimation of loss and loss expenses at the early stages of catastrophe losses before loss information is reported to the reinsurer. In the case of asbestos and environmental claims, the Company has established reserves for future loss and allocated loss expenses based on the results of periodic actuarial studies, which consider the underlying exposures of the Company s cedants.

Often the selected best estimate is a blend of the results from two or more methods (e.g., weighted averages). Furthermore, the judgment as to which method(s) is most appropriate for a particular underwriting year and reserving cell could change over time as new information emerges regarding underlying loss activity and other data issues. See the Company s 2005 Annual Report on Form 10K/A for a brief discussion of the strengths and weaknesses of the various standard actuarial techniques we use.

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The reserve methodologies employed by the Company are dependent on data that the Company collects. This data consists primarily of loss amounts reported by the Company s cedants, loss payments made by the Company s cedants, and premiums written and earned reported by the cedants or estimated by the Company. The actuarial methods used by the Company to project its liabilities recorded today but that will be paid in the future (future liabilities) do not generally include methodologies that are dependent on claim counts reported, claim counts settled or claim counts open because, due to the nature of the Company s business, this information is not routinely provided by the cedants for every treaty. Consequently, actuarial methods relying on this information cannot be used by the Company to estimate loss reserves.

The Company examines loss development trends by underwriting year to determine various assumptions that are required as inputs in the actuarial methodologies it employs. This typically involves the analysis of historical loss development trends by reserving cell and by underwriting year, and the calculation of long-term averages. In addition, the Company utilizes external or internal benchmark sources of information for the reserving cells for which the Company does not have sufficient loss development data to calculate credible trends.

Several underlying assumptions are used in the construction of average trends and their subsequent use in the actuarial methodologies we employ. The validity of these underlying assumptions is reviewed periodically and if appropriate, modifications are made in the selection of average trends or other reserving inputs to reflect deviations from the underlying assumptions.

The validity of all assumptions used in the reserving process is reaffirmed on a quarterly basis. Reaffirmation of the assumptions means that the actuaries determine that the assumptions continue to form a sound basis for projection of future liabilities. Assumptions used in projecting future liabilities are themselves estimates based on historical information. As new information becomes available (e.g., additional losses reported), our actuaries determine whether a revised estimate of the reserving assumptions that reflects all available information is consistent with the previous reserving assumptions employed. In general, to the extent that the revised estimate of assumptions are within a close range of our original assumptions, we determine that the assumptions employed continue to form an appropriate basis for projections and continue to use the original assumptions in our models. In this case, any differences could be attributed to the imprecise nature of the assumption estimation process. However, to the extent that the deviations between the two sets of estimates are not within a close range of our original assumptions, we react by adopting the revised assumptions as a basis for our reserve models. Notwithstanding the above, even where we have experienced no material deviations from our original assumptions during any quarter, we will generally revise our reserving assumptions at least once a year to reflect all accumulated available information. Critical underlying assumptions are:

(i) the cedant s business practices will proceed as in the past with no material changes either in submission of accounts or cash flows;

(ii) any internal delays in processing accounts received by the cedant are not materially different from that experienced historically, and hence the implicit reserving allowance made in loss reserves through our methods continues to be appropriate;

(iii) case reserve reporting practices, particularly the methodologies used to establish and report case reserves, are unchanged from historical practices;

(iv) the Company s internal claim practices, particularly the level and extent of use of ACRs are unchanged;

(v) historical levels of claim inflation can be projected into the future and will have no material effect on either the acceleration or deceleration of claim reporting and payment patterns;

(vi) the selection of reserving cells results in homogeneous and credible future expectations for all business in the cell and any changes in underlying treaty terms are either reflected in cell selection or explicitly allowed in the selection of trends;

(vii) in cases where benchmarks are used, they are derived from the experience of similar business; and

(viii) the Company can form a credible initial expectation of the ultimate loss ratio of recent underwriting years through a review of pricing information supplemented by qualitative information on market events.

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All of our critical assumptions can be thought of as key assumptions in the sense that they can have a material impact on the adequacy of our reserves. In general, the various actuarial techniques we use assume that loss reporting and payment patterns in the future can be estimated from past experience. To the extent that any of the above assumptions are not valid, future payment and reporting patterns could differ from historical experience. In practice, it is difficult to be precise on the effect of each assumption. However, due to a greater potential for estimation error, and thus greater volatility, our reserves may be more sensitive to the effects of deviations from assumptions (v), (vii) and (viii) than the other assumptions.

The Company s best estimate of total loss reserves is typically in excess of the midpoint of the actuarial reserve estimates. The Company believes that there is potentially significant risk in estimating loss reserves for long-tail lines of business and for immature underwriting years that may not be adequately captured through traditional actuarial projection methodologies. These methodologies usually rely heavily on projections of prior year trends into the future. In selecting its best estimate of future liabilities, the Company considers both the results of actuarial point estimates of loss reserves as well as the potential variability of these estimates as captured by a reasonable range of actuarial reserve estimates. Selected reserves are always within the indicated reasonable range of estimates indicated by the Company s actuaries. However, primarily for long-tail lines and immature underwriting years, the Company s best estimate of reserves reflects the effect of inherent risks that the Company believes are not adequately reflected in actuarial point estimates. In determining the appropriate best estimate, the Company reviews (i) the position of overall reserves within the actuarial reserve range, (ii) the result of bottom up analysis by underwriting year reflecting the impact of parameter uncertainty in actuarial calculations, and (iii) specific qualitative information on events that may have an effect on future claims but which may not have been adequately reflected in actuarial mid-estimates, such as potential for outstanding litigation, claims practices of cedants, etc.

In general, the estimates of loss reserves recorded for short-tail business are subject to less volatility than those for long-tail lines. Carried loss reserves for the U.S. P&C sub-segment are considered to be predominantly long-tail due to the significant volume of U.S. casualty business written in this sub-segment. The casualty line comprised 70% of the net premiums written for this sub-segment, or 15% of the Company s total net premiums written in the first six months of 2006. The remaining business within this sub-segment, property and motor, is considered to be short-tail. Within the Global (Non-U.S.) P&C sub-segment, the Company considers both its casualty business as well as its non-proportional motor business to be long-tail. These two lines represented 27% of the net premiums written in the Global (Non-U.S.) P&C sub-segment, or 6% of the Company s total net premiums written in the first six months of 2006. Management considers the short-tail lines within the Global (Non-U.S.) P&C sub-segment to be property and proportional motor. The Worldwide Specialty sub-segment is primarily comprised of lines of business that are thought to be either short or medium-tail. The short-tail lines consist of agriculture, catastrophe, energy, credit/surety and specialty property and account for 67% of the net premiums written in this sub-segment, or 29% of the Company s total net premiums written in the first six months of 2006. Aviation/space, engineering and marine are considered by the Company to have a medium-tail and represent 25% of this sub-segment s net premiums written, or 11% of the Company s total net premiums written in the first six months of 2006. Specialty casualty business is considered to be long-tail and represents 8% of net premiums written in this sub-segment, or 3% of the Company s total net premiums written in the first six months of 2006.

In the second quarter of 2006 and 2005, the Company reviewed its estimate for prior year losses for each sub-segment of the Non-life segment and, in light of developing data, determined to adjust its ultimate loss ratios for prior accident years. The components of the net favorable (adverse) loss development for the three months and six months ended June 30, 2006 and 2005 are described in more detail in the discussion of the sub-segments that make up the Non-life segment.

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The following table summarizes the net favorable (adverse) development of loss reserves in the Non-life segment (in millions of U.S. dollars):

	For the three months ended June 30, 2006	For the three months ended June 30, 2005	For the six months ended June 30, 2006	For the six months ended June 30, 2005
Prior year favorable (adverse) loss development:				
Non-life segment				
U.S. P&C	**$ (18)**	$ 1	**$ (19)**	$ (4)
Global (Non-U.S) P&C	**47**	19	**47**	47
Worldwide Specialty	**33**	46	**102**	88
Total prior year loss development	**$ 62**	$ 66	**$ 130**	$ 131

Case reserves are reported to the Company by its cedants, while ACRs and IBNR are estimated by the Company. The following table shows the gross reserves reported by cedants (case reserves), those estimated by the Company (ACRs and IBNR) and the total net loss reserves recorded at June 30, 2006 for each Non-life sub-segment (in millions of U.S. dollars):

	Case reserves	ACRs	IBNR reserves	Total gross loss reserves recorded	Retroceded loss reserves	Total net loss reserves recorded
U.S. P&C	$ 623	$ 100	$ 1,409	$ 2,132	$ (14)	$ 2,118
Global (Non-U.S.) P&C	1,125	20	1,039	2,184	(45)	2,139
Worldwide Specialty	1,269	252	952	2,473	(100)	2,373
Total Non-life	$ 3,017	$ 372	$ 3,400	$ 6,789	$ (159)	$ 6,630

The Company estimates its net loss reserves using single point estimates for each sub-segment. These loss reserves represent the Company s best estimate of future losses and loss expense amounts. Ranges around these point estimates are developed using stochastic simulations and techniques and provide an indication as to the degree of variability of the loss reserves. The Company interprets the ranges produced by these techniques as confidence intervals around the best estimates for each sub-segment. However, due to the inherent volatility in the business written by the Company, there can be no guarantee that the final settlement of the loss reserves will fall within these ranges. The point estimates recorded by the Company and the range of estimates around these point estimates at June 30, 2006, were as follows for each Non-life sub-segment (in millions of U.S. dollars):

	Recorded Point Estimate	High	Low
Net Non-life loss reserves:			
U.S. P&C	$ 2,118	$ 2,408	$ 1,712
Global (Non-U.S.) P&C	2,139	2,261	1,854
Worldwide Specialty	2,373	2,429	2,143

It is not appropriate to add together the ranges of each sub-segment in an effort to determine a high and low range around the Company s total Non-life carried loss reserves.

Estimates of ultimate liabilities are contingent on many future events. The eventual outcome of these events may be different from the assumptions underlying the reserve estimates. Loss reserves are established to cover the Company s estimated liability for the payment of all losses and loss expenses incurred with respect to premiums earned on the contracts that it writes. Loss reserves do not represent an exact calculation of liability. Loss reserves are estimates involving actuarial and statistical projections at a given time to reflect the Company s expectations of the costs of the ultimate settlement and administration of claims. In the event that the business environment and social trends diverge from historical trends, the Company may have to adjust its loss reserves to amounts falling significantly outside its current estimate range. Management believes that the recorded loss reserves represent its best estimate of future liabilities based on information available as of June 30, 2006. The estimates are continually reviewed and the ultimate liability may be in excess of, or less than, the amounts provided, for which any adjustments will be reflected in the period in which the need for an adjustment is determined.

Included in the business that is considered to have a long reporting tail is the Company s exposure to asbestos and environmental claims. The Company s net reserve for unpaid losses and loss expenses for asbestos and environmental exposures has not changed significantly since December 31, 2005. (See Note 4 to Consolidated Financial Statements in the Company s 2005 Annual Report on Form 10-K/A.)

Liabilities for policy benefits for ordinary life and accident and health policies have been established based upon information reported by cedants supplemented by the Company s actuarial estimates of mortality, critical illness, persistency and future investment income, with appropriate provision to reflect uncertainty. Future policy benefit reserves for annuity and universal life products are carried at their accumulated values. Reserves for policy claims and benefits include both mortality and critical illness claims in the process of settlement and claims that are assumed to have been incurred but not yet reported. Interest rate assumptions used to estimate liabilities for policy benefits for life and annuity contracts ranged from 1.5% to 5.5%. Actual experience in a particular period may vary from expected experience and, consequently, may affect the Company s results in future periods.

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Results of Operations for the Three Months and Six Months Ended June 30, 2006 and 2005

The following discussion of Results of Operations contains forward-looking statements made based upon assumptions and expectations concerning the potential effect of future events that are subject to uncertainties. See Item 1A of Part I of the Company s 2005 Annual Report on Form 10-K/A for a complete list of the Company s risk factors. Any of these risk factors could cause actual results to differ materially from those reflected in such forward-looking statements.

The Company s reporting currency is the U.S dollar. The Company s subsidiaries and branches have one of the following functional currencies: U.S. dollar, euro or Canadian dollar. In recording foreign currency transactions, revenue and expense items are converted into the functional currency at the average exchange rates for each quarter. Assets and liabilities are converted to the functional currency at the exchange rates in effect at the balance sheet date. Financial statements expressed in functional currencies other than the U.S. dollar are translated to U.S. dollars using each quarter s average exchange rate for the Statements of Operations and Cash Flows and the exchange rate in effect at the balance sheet date for the Balance Sheets. As a significant portion of the Company s operations is performed in foreign currencies, fluctuations in foreign exchange rates may affect period-to-period comparisons. To the extent that fluctuations in foreign exchange rates affect comparisons, their impact has been quantified, when possible, and discussed in each of the relevant sections.

The following tables, which provide foreign exchange rates for the principal currencies in which the Company transacts business, highlight that while the U.S. dollar strengthened, on average, against the euro and other currencies, except for the Canadian dollar, in the second quarter and first six months of 2006 compared to the same periods of 2005 (see first table), the U.S. dollar weakened against these currencies when we compare the balance sheet rates at June 30, 2006 with those at December 31, 2005 (see second table).

	Statements of operations and cash flows (average rates)					
	Three months ended			Six months ended		
Exchange rate against U.S. dollar	June 30, 2006 (A)	Three months ended June 30, 2005 (A)	% Change	June 30, 2006 (B)	Six months ended June 30, 2005 (B)	% Change
Euro	**1.2243**	1.2968	**(5.59)%**	**1.2084**	1.3092	**(7.70)%**
British pound	**1.7780**	1.8920	**(6.02)**	**1.7621**	1.8955	**(7.04)**
Swiss franc	**0.7814**	0.8389	**(6.85)**	**0.7752**	0.8484	**(8.63)**
Japanese yen.	**0.0086**	0.0094	**(8.16)**	**0.0086**	0.0095	**(10.09)**
Canadian dollar	**0.8756**	0.8081	**8.36**	**0.8695**	0.8143	**6.78**

(A) Obtained by arithmetic average of mid-month and month-end rates.
(B) Obtained by arithmetic average of first and second quarter average rates.

	Balance sheets (end of period rates)		
Exchange rate against U.S. dollar	At June 30, 2006	At December 31, 2005	% Change
Euro	**1.2549**	1.1843	**5.96%**
British pound	**1.8161**	1.7209	**5.53**
Swiss franc	**0.8023**	0.7600	**5.55**
Japanese yen.	**0.0086**	0.0085	**1.33**
Canadian dollar	**0.8931**	0.8580	**4.09**

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Overview

The Company measures its performance in several ways. Among the performance measures accepted under U.S. GAAP is diluted net income per share, a measure that focuses on the return provided to the Company s common shareholders. Diluted net income per share is obtained by dividing net income available to common shareholders by the weighted average number of common and common share equivalents outstanding. Net income available to common shareholders is defined as net income less preferred share dividends.

Net income, preferred dividends, net income available to common shareholders and diluted net income per share for the three months and six months ended June 30, 2006 and 2005 were as follows (in millions of U.S. dollars, except per share data):

	For the three months ended June 30, 2006	% Change 2006 over 2005	For the three months ended June 30, 2005	For the six months ended June 30, 2006	% Change 2006 over 2005	For the six months ended June 30, 2005
Net income	**$ 78**	**(52)%**	$ 160	**$ 271**		$ 271
Less: preferred dividends	**9**		9	**17**		17
Net income available to common shareholders	**$ 69**	**(54)%**	$ 151	**$ 254**		$ 254
Diluted net income per share	**$ 1.20**	**(56)%**	$ 2.72	**$ 4.40**	**(4)%**	$ 4.56

Three-month result

Net income, net income available to common shareholders and diluted net income per share for the second quarter have decreased compared to the same period of 2005, as a result of net realized investment losses incurred in the 2006 period. While the Company recorded pre-tax net realized investment gains of $56 million in the second quarter of 2005, pre-tax net realized investment losses amounted to $59 million in the second quarter of 2006, following a steady rise in interest rates during the 2006 period.

Six-month result

Net income and net income available to common shareholders for the first six months of 2006 are essentially flat compared to the same period of 2005. Diluted net income per share for the first six months of 2006 is lower than 2005 as a result of the Company s issuance of common shares in the fourth quarter of 2005, which resulted in a higher number of common and common share equivalents outstanding at June 30, 2006.

Review of Net Income

Management analyzes the Company s net income in three parts: underwriting result, net investment income and other components of net income. Underwriting result consists of net premiums earned and other income less losses and loss expenses and life policy benefits, acquisition costs and other operating expenses. Investment income includes interest and dividends, net of investment expenses, generated by the Company s investment portfolio, as well as interest income generated on funds held and certain ART transactions. Other components of net income include net realized investment gains and losses, interest expense, net foreign exchange gains and losses, income tax expense or benefit and interest in earnings of equity investments.

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The components of net income for the three months and six months ended June 30, 2006 and 2005 were as follows (in millions of U.S. dollars):

	For the three months ended June 30, 2006	% Change 2006 over 2005	For the three months ended June 30, 2005	For the six months ended June 30, 2006	% Change 2006 over 2005	For the six months ended June 30, 2005
Underwriting result:						
Non-life	**$ 73**	**(11)%**	$ 82	**$ 159**	**51%**	$ 104
ART	**12**	**NM**	(2)	**17**	**83**	10
Life	**(14)**	**63**	(9)	**(22)**	**14**	(18)
Corporate expenses	**(16)**	**2**	(16)	**(32)**	**14**	(28)
Net investment income	**108**	**20**	90	**208**	**18**	177
Net realized investment (losses) gains	**(59)**	**NM**	56	**(3)**	**NM**	93
Interest expense	**(13)**	**79**	(7)	**(26)**	**76**	(15)
Net foreign exchange losses	**(4)**	**68**	(3)	**(7)**	**206**	(3)
Income tax expense	**(12)**	**(65)**	(33)	**(28)**	**(48)**	(54)
Interest in earnings of equity investments	**3**	**22**	2	**5**	**6**	5
Net income	**$ 78**	**(52)**	$ 160	**$ 271**		$ 271

NM: not meaningful

Underwriting result is a measurement that the Company uses to manage and evaluate its segments and sub-segments, as it is a primary measure of underlying profitability for the Company s core reinsurance operations, separate from the investment results. The Company believes that in order to enhance the understanding of its profitability, it is useful for investors to evaluate the components of net income separately and in the aggregate. Underwriting result should not be considered a substitute for net income and does not reflect the overall profitability of the business, which is also impacted by investment results and other items.

Three-month result

The underwriting result for the Non-life segment decreased by $9 million, from $82 million in 2005 to $73 million in 2006. The decrease was principally attributable to:

- a decrease in the volume of business earned and normal fluctuations in profitability on the premiums earned in 2006 totaling approximately $6 million; and
- a decrease in net favorable development on prior accident years of $4 million, from $66 million in 2005 to $62 million in 2006. The components of the net favorable loss development on prior accident year losses are described in more detail in the discussion of individual sub-segments in the next section; offset by
- reductions in other operating expenses of $1 million.

Underwriting result for the ART segment increased by $14 million, from a loss of $2 million in the second quarter of 2005 to a gain of $12 million in 2006. While all lines had positive results in the second quarter of 2006, the second quarter of 2005 included negative results for the weather business. The weather business, which incurred an other loss (composed of realized and unrealized gains or losses on derivative contracts) in the second quarter of 2005, had a strong result in the second quarter of 2006.

Underwriting result for the Life segment decreased from a loss of $9 million in the second quarter of 2005 to a loss of $14 million in 2006, due to net adverse reserve development in the longevity line in the second quarter of 2006.

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Corporate expenses were flat in the second quarter of 2006 compared to 2005. Increases in operating expenses of approximately $1.2 million, resulting primarily from the adoption on January 1, 2006, of Statement of Financial Accounting Standards (SFAS) No. 123 (Revised 2004), Share-Based Payment (SFAS 123R), and annual increases in payroll costs were offset by lower accruals for consulting and compliance fees in the second quarter of 2006.

The Company reported net investment income of $108 million in the second quarter of 2006 compared to $90 million for the same period in 2005. The 20% increase in net investment income was primarily attributable to the increase in the asset base resulting from the investment of the Company s significant cash flows from operations, which totaled $742 million since June 30, 2005, and cash proceeds of $549 million from the Company s capital raises in October 2005. The higher interest rates prevailing during the second quarter of 2006 for the U.S. dollar, euro and other currencies also contributed to the improvement in net investment income. This increase was partially offset by changes in average foreign exchange rates, which resulted in a decrease of net investment income of approximately 1%, as a result of the strengthening of the U.S. dollar against the euro and other currencies.

Realized investment gains and losses are generally a function of multiple factors, with the most significant being the prevailing interest rates and equity market conditions, the timing of disposition of fixed maturities and equity securities, and charges for the recognition of other-than-temporary impairments in the Company s investment portfolio. Net realized investment gains and losses decreased by $115 million, from a net gain of $56 million in the second quarter of 2005 to a net loss of $59 million for the same period in 2006, primarily as a result of losses in the Company s fixed income and equity portfolios, including other-than-temporary impairments. Following a steady rise in interest rates during the second quarter of 2006, the majority of the Company s fixed income investments decreased in value. The Company s equity portfolio also experienced a decrease in value in the difficult capital market environment prevailing during the second quarter of 2006. As the Company repositioned its investment portfolio to take advantage of market conditions, it generated sales of securities that resulted in the realization of the unrealized market value depreciation on the securities. Although the depreciation in value of fixed income and equity securities during the second quarter of 2006 reduced the Company s shareholder s equity, the realization of the unrealized market value depreciation did not change the Company s shareholders equity, as it merely transferred the loss from the accumulated other comprehensive income section of the balance sheet to net income on the statement of operations and retained earnings on the balance sheet.

Interest expense increased by $6 million in the second quarter of 2006 compared to the same period in 2005 due to the $400 million bank loan received by the Company in October 2005.

The income tax expense decreased by $21 million from $33 million in the second quarter of 2005 to $12 million for the same period in 2006. The decrease is primarily due to a) the decrease in net realized investment gains and losses discussed above; and b) the normal shifts in geography (or tax jurisdictions) of pre-tax income.

Six-month result

The underwriting result for the Non-life segment increased by $55 million, from $104 million in 2005 to $159 million in 2006. The increase was principally attributable to:

- a decrease in the level of large catastrophic losses of $81 million (net of reinstatement premiums) in the first six months of 2006 for the Global (Non-U.S.) P&C sub-segment ($2 million) and the Worldwide Specialty sub-segment ($79 million);

- reductions in other operating expenses of $6 million; partially offset by

- a decrease of approximately $31 million resulting from the combination of the decrease in the volume of business earned, normal fluctuations in profitability and a modest decline in profitability on the premiums earned in 2006; and

- a decrease of $1 million in net favorable development on prior accident years, from $131 million in 2005 to $130 million in 2006. The components of the net favorable loss development on prior accident year losses are described in more detail in the discussion of individual sub-segments in the next section.

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Underwriting result for the ART segment increased by $7 million, from $10 million in the first six months of 2005 to $17 million in 2006. While all lines had positive results in the first six months of 2006 and 2005, the weather, structured risk transfer and principal finance businesses were more profitable in the 2006 period. The weather business experienced higher other income while the structured risk and principal finance businesses had a higher volume of business in the first six months of 2006.

Underwriting result for the Life segment decreased from a loss of $18 million in the first six months of 2005 to a loss of $22 million in 2006, due to net adverse reserve development in the longevity line in the first six months of 2006.

Corporate expenses increased by $4 million, from $28 million in the first six months of 2005 to $32 million in 2006. Increases in operating expenses of approximately $1.2 million, resulting primarily from the adoption on January 1, 2006, of SFAS 123R, the addition of staff in corporate departments and annual increases in payroll, were partially offset by lower accruals for consulting and compliance fees during the first six months of 2006.

The Company reported net investment income of $208 million in the first six months of 2006 compare