VALIDUS HOLDINGS LTD
Form 10-K
February 15, 2013
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2012
Commission file number 001-33606
VALIDUS HOLDINGS, LTD.
(Exact name of registrant as specified in its charter)

BERMUDA	98-0501001
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

29 Richmond Road, Pembroke, Bermuda HM 08
(Address of principal executive offices and zip code)
(441) 278-9000
(Registrant's telephone number, including area code)
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class:	Name of Each Exchange on Which Registered:
Common Shares, $0.175 par value per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ý No o
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No ý
Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ý	Accelerated filer o	Non-accelerated filer o (Do not check if a	Smaller reporting company o

smaller reporting company)

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of June 30, 2012 was $2,077.0 million computed upon the basis of the closing sales price of the Common Shares on June 30, 2012. For the purposes of this computation, shares held by directors and officers of the registrant have been excluded. Such exclusion is not intended, nor shall it be deemed, to be an admission that such persons are affiliates of the registrant.

As of February 13, 2013, there were 107,468,544 outstanding Common Shares, $0.175 par value per share, of the registrant.

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates information from certain portions of the registrant’s definitive proxy statement to be filed with the Securities and Exchange Commission within 120 days after the fiscal year ended December 31, 2012.

Table of Contents

Table of Contents

This Annual Report on Form 10-K contains “Forward-Looking Statements” as defined in the Private Securities Litigation Reform Act of 1995. A non-exclusive list of the important factors that could cause actual results to differ materially from those in such Forward-Looking Statements is set forth herein under the caption “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Cautionary Note Regarding Forward-Looking Statements.”

PART I

All amounts presented in this part are in U.S. dollars except as otherwise noted.

Item 1. Business

Overview

Validus Holdings, Ltd. (the “Company”) was incorporated under the laws of Bermuda on October 19, 2005. Our initial investor, which we refer to as our founding investor, is Aquiline Capital Partners LLC, a private equity firm dedicated to investing in financial services companies. Other sponsoring investors included private equity funds managed by Goldman Sachs Capital Partners, Vestar Capital Partners, New Mountain Capital and Merrill Lynch Global Private Equity. The Company conducts its operations worldwide through three operating segments which have been determined under U.S. GAAP segment reporting, Validus Reinsurance, Ltd. (“Validus Re”), Talbot Holdings Ltd. (“Talbot”) and AlphaCat Managers, Ltd. ("AlphaCat"). The Company provides reinsurance, insurance and insurance linked securities management. Validus Re is a Bermuda based reinsurer focused on short tail lines of reinsurance. Talbot is the Bermuda parent of the specialty insurance group primarily operating within the Lloyd's insurance market through Syndicate 1183. AlphaCat is a Bermuda based investment adviser, managing third-party capital in insurance linked securities and other investments in the property catastrophe reinsurance space.

We seek to establish ourselves as a leader in the global insurance and reinsurance markets. Our principal operating objective is to use our capital efficiently by underwriting primarily short-tail insurance and reinsurance contracts with superior risk and return characteristics. Our primary underwriting objective is to construct a portfolio of short-tail insurance and reinsurance contracts which maximizes our return on equity subject to prudent risk constraints on the amount of capital we expose to any single event. We manage our risks through a variety of means, including contract terms, portfolio selection, diversification criteria, including geographic diversification criteria, and proprietary and commercially available third-party vendor catastrophe models.

Since our formation in 2005, we have been able to achieve substantial success in the development of our business. Selected examples of our accomplishments are as follows:

- Raising approximately $1.0 billion of initial equity capital in December 2005 and underwriting $217.4 million in gross premiums written for the January 2006 renewal season;
- At the time of the Company’s formation an executive management team was assembled with an average of 20 years of industry experience and senior expertise spanning multiple aspects of the global insurance and reinsurance business;
- Building a risk analytics staff comprised of over 40 experts, many of whom have PhDs and Masters degrees in related fields;
- Developing Validus Capital Allocation and Pricing System (“VCAPS”), a proprietary computer-based system for modeling, pricing, allocating capital and analyzing catastrophe-exposed risks;
- Acquiring all of the outstanding shares of Talbot Holdings Ltd. on July 2, 2007;
- Completing an initial public offering (“IPO”) on July 30, 2007;
- Acquiring all of the outstanding shares of IPC Holdings Ltd. (“IPC”) on September 4, 2009;
- Raising $185.0 million of initial capital for AlphaCat Re 2011, Ltd. (“AlphaCat Re 2011”) on May 25, 2011 and a further $71.0 million of additional capital on December 23, 2011;
- Raising $500.0 million of capital for PaCRe, Ltd. ("PaCRe") a new Class 4 Bermuda reinsurer formed for the purpose of writing high excess property catastrophe reinsurance, on April 2, 2012;
- Raising $70.0 million of capital for AlphaCat Re 2012, Ltd. (“AlphaCat Re 2012”) on May 29, 2012;
- Acquiring all of the outstanding shares of Flagstone Reinsurance Holdings, S.A. ("Flagstone") on November 30, 2012;

1

- Raising $230.0 million of capital for Alpha Cat 2013, Ltd. ("AlphaCat 2013") on December 17, 2012 and receiving $219.4 million of third party subscriptions for AlphaCat Insurance Linked Securities ("ILS") Funds;
- Increasing the annual dividend by 20% from $1.00 to $1.20 per common share and per common share equivalent and announcing a $2.00 special dividend per common share and per common share equivalent on February 6, 2013; and
- Repurchasing approximately 43.7 million common shares for an aggregate purchase price of $1,227.1 million and paying and aggregate amount of $467.6 million in dividends from inception of the Company to February 13, 2013.

Our Operating Subsidiaries

The following chart shows how our Company and its principal operating subsidiaries are organized.

For a complete list of the Company's subsidiaries, see Exhibit 21.

(a) AlphaCat Re 2012 and AlphaCat 2013 are non-consolidated operating affiliates.

Operating Segments

Validus Re: Validus Re, the Company's principal reinsurance operating subsidiary, operates as a Bermuda-based provider of short-tail reinsurance products on a global basis. Validus Re concentrates on first-party risks, which are property risks and other reinsurance lines commonly referred to as short-tail in nature due to the relatively brief period between the occurrence and payment of a claim.

Validus Re was registered as a Class 4 insurer under The Insurance Act 1978 of Bermuda, amendments thereto and related regulations (the "Insurance Act") in November 2005. It commenced operations with approximately $1.0 billion of equity capital and a balance sheet unencumbered by any historical losses relating to the 2005 hurricane season, the events of September 11, 2001, asbestos or other legacy exposures affecting our industry.

Validus Re entered the global reinsurance market in 2006 during a period of imbalance between the supply of underwriting capacity available for reinsurance on catastrophe-exposed property, marine and energy risks and demand for such reinsurance coverage.

On September 4, 2009, the Company acquired all of the outstanding shares of IPC. The primary lines in which IPC conducted business were property catastrophe reinsurance and, to a limited extent, property-per-risk excess, aviation (including satellite) and

Table of Contents

other short-tail reinsurance on a worldwide basis. For segmental reporting purposes, the results of IPC's operations since the acquisition date have been included within the Validus Re segment in the consolidated financial statements.
On November 30, 2012, the Company acquired all of the outstanding shares of Flagstone, strengthening the Company's leading property catastrophe reinsurance and short-tail specialty insurance platform. The primary lines in which Flagstone conducted business were property catastrophe reinsurance, property pro rata and per-risk excess and short tail specialty and casualty reinsurance such as aviation, energy, personal accident and health, satellite, marine and workers' compensation catastrophe. For segmental reporting purposes, the results of Flagstone's operations since the acquisition date have been included within the Validus Re segment in the consolidated financial statements.
The following are the primary lines in which Validus Re conducts its business. Details of gross premiums written by line of business are provided below:

(Dollars in thousands)	Year Ended December 31, 2012 Gross Premiums Written	Year Ended December 31, 2012 Gross Premiums Written (%)	Year Ended December 31, 2011 Gross Premiums Written	Year Ended December 31, 2011 Gross Premiums Written (%)	Year Ended December 31, 2010 Gross Premiums Written	Year Ended December 31, 2010 Gross Premiums Written (%)
Property	$771,617	68.2 %	$786,937	70.6 %	$778,794	71.5 %
Marine	257,469	22.7 %	232,401	20.9 %	227,135	20.8 %
Specialty	102,873	9.1 %	95,155	8.5 %	83,514	7.7 %
Total	$1,131,959	100.0 %	$1,114,493	100.0 %	$1,089,443	100.0 %

Property: Validus Re underwrites property catastrophe reinsurance, property per risk reinsurance and property pro rata reinsurance.
Property catastrophe: Property catastrophe reinsurance provides reinsurance for insurance companies' exposures to an accumulation of property and related losses from separate policies, typically relating to natural disasters or other catastrophic events. Property catastrophe reinsurance is generally written on an excess of loss basis, which provides coverage to primary insurance companies when aggregate claims and claim expenses from a single occurrence from a covered peril exceed a certain amount specified in a particular contract. Under these contracts, the Company provides protection to an insurer for a portion of the total losses in excess of a specified loss amount, up to a maximum amount per loss specified in the contract. In the event of a loss, most contracts provide for coverage of a second occurrence following the payment of a premium to reinstate the coverage under the contract, which is referred to as a reinstatement premium. The coverage provided under excess of loss reinsurance contracts may be on a worldwide basis or limited in scope to specific regions or geographical areas. Coverage can also vary from "all property" perils, which is the most expansive form of coverage, to more limited coverage of specified perils such as windstorm-only coverage. Property catastrophe reinsurance contracts are typically "all risk" in nature, providing protection against losses from earthquakes and hurricanes, as well as other natural and man-made catastrophes such as floods, tornadoes, fires and storms. The predominant exposures covered are losses stemming from property damage and business interruption coverage resulting from a covered peril. Certain risks, such as war or nuclear contamination may be excluded, partially or wholly, from certain contracts. Gross premiums written on property catastrophe business during the year ended December 31, 2012 were $598.0 million.
Property per risk: Property per risk reinsurance provides reinsurance for insurance companies' excess retention on individual property and related risks, such as highly-valued buildings. Per risk excess of loss reinsurance protects insurance companies on their primary insurance risks on a "single risk" basis. A "risk" in this context might mean the insurance coverage on one building or a group of buildings or the insurance coverage under a single policy which the reinsured treats as a single risk. Coverage is usually triggered by a large loss sustained by an individual risk rather than by smaller losses which fall below the specified retention of the reinsurance contract. Such property per risk coverages are generally written on an excess of loss basis, which provides the reinsured protection beyond a specified amount up to the limit set within the reinsurance contract. Gross premiums written on property per risk business during the year ended December 31, 2012 were $59.3 million.
Property pro rata: Property pro rata contracts require that the reinsurer share the premiums as well as the losses and loss expenses in an agreed proportion with the cedant. Gross premiums written on property pro rata business during

the year ended December 31, 2012 were $114.2 million.

Marine: Validus Re underwrites reinsurance on marine risks covering damage to or losses of marine vessels and cargo, third-party liability for marine accidents and physical loss and liability from principally offshore energy properties. Validus Re underwrites marine on an excess of loss basis and on a pro rata basis. Gross premiums written on marine business during the year ended December 31, 2012 were $257.5 million.

Specialty: Validus Re underwrites other lines of business depending on an evaluation of pricing and market conditions, which include aerospace and aviation, agriculture, financial lines of business, terrorism, life, accident & health, nuclear, workers'

Table of Contents

compensation, crisis management, contingency, motor and technical lines. The Company seeks to underwrite other specialty lines with very limited exposure correlation with its property, marine and energy portfolios. With the exception of the aerospace line of business, which has a meaningful portion of its gross premiums written volume on a proportional basis, the Company's other specialty lines are written on an excess of loss basis. Gross premiums written on specialty business during the year ended December 31, 2012 were $102.9 million.

AlphaCat: The AlphaCat segment manages strategic relationships that leverage the Company's underwriting and investment expertise and earns management, performance and underwriting fees. AlphaCat Managers, Ltd. ("AlphaCat Managers"), formed in 2008, is a core element within the Validus Group strategic initiative to expand into capital market activities by participating in the market for Insurance Linked Securities ("ILS"). ILS are financial instruments whose fundamental value is determined by insurance losses caused by natural catastrophes such as major earthquakes and hurricanes. As the returns of ILS are primarily driven by natural catastrophes, when carefully structured, they are generally uncorrelated with the overall financial market, making ILS an attractive asset class for capital market investors.

AlphaCat helps investors take full advantage of this uncorrelated asset class through various funds and sidecars, accessing the market via AlphaCat Reinsurance Ltd., a Bermuda provider of fully collateralized property catastrophe reinsurance and retrocession capacity. AlphaCat invests in private reinsurance transactions, as well as catastrophe bonds, a common type of ILS issued by insurance and reinsurance companies. AlphaCat leverages the Validus Group's extensive business sourcing, underwriting, research and analytic capabilities to construct ILS portfolios subject to prudent risk constraints.

During the first quarter of 2012, to better align the Company's operating and reporting structure with its current strategy, there was a change in the Company's segment structure. This change included the AlphaCat group of companies as a separate operating segment. The AlphaCat segment was included as an additional segment and includes AlphaCat Re 2011, AlphaCat Re 2012, AlphaCat 2013, PaCRe and other affiliated investment funds. Prior period comparatives have been restated to reflect the change in segmentation.

Talbot: On July 2, 2007, the Company acquired all of the outstanding shares of Talbot. Talbot is the Bermuda parent of a specialty insurance group primarily operating within the Lloyd's insurance market through Syndicate 1183. The acquisition of Talbot provided the Company with significant benefits in terms of product line and geographic diversification as well as offering the Company broader access to underwriting expertise. Similar to Validus Re, Talbot writes primarily short-tail lines of business but, as a complement to Validus Re, focuses mostly on insurance, as opposed to reinsurance risks, and on specialty lines where Validus Re currently has limited or no presence (e.g., war, financial institutions, contingency, accident and health). In addition, Talbot provides the Company with access to the Lloyd's marketplace where Validus Re does not operate. As a London-based insurer, Talbot also writes the majority of its premiums on risks outside the United States. Talbot's team of underwriters have, in many cases, spent most of their careers writing niche, short-tail business and bring their expertise to bear on expanding the Company's short-tail insurance franchise.

The Company has expanded and diversified its business through Syndicate 1183's access to Lloyd's license agreements with regulators around the world. Talbot Underwriting Risk Services Ltd., Talbot Underwriting Services, (U.S.) Ltd., Talbot Underwriting (MENA) Ltd., Validus Reaseguros, Inc., Validus Re Chile S.A. and Talbot Risk Services Pte, Ltd., act as approved Lloyd's coverholders for Syndicate 1183.

The following are the primary lines in which Talbot conducts its business. Details of gross premiums written by line of business are provided below:

	Year Ended December 31, 2012		Year Ended December 31, 2011		Year Ended December 31, 2010	
(Dollars in thousands)	Gross Premiums Written	Gross Premiums Written (%)	Gross Premiums Written	Gross Premiums Written (%)	Gross Premiums Written	Gross Premiums Written (%)
Property	$324,910	30.2 %	$306,317	30.2 %	$314,769	32.1 %
Marine	396,207	36.7 %	341,821	33.7 %	315,102	32.1 %
Specialty	357,519	33.1 %	365,984	36.1 %	351,202	35.8 %

Total	$1,078,636	100.0	%	$1,014,122	100.0	%	$981,073	100.0	%

Property: The main sub-classes within property are international and North American direct and facultative contracts, onshore energy, lineslips and binding authorities together with a book of business written on a treaty reinsurance basis. The business written is mostly commercial and industrial insurance though there is a modest personal lines component. The business is short-tail with premiums for reinsurance and, direct and facultative business, substantially earned within 12 months and premiums for lineslips and binding authorities substantially earned within 12 months of the expiry of the contract. Gross premiums written on property business during the year ended December 31, 2012 were $324.9 million, including $86.3 million of treaty reinsurance.

Table of Contents

Marine: The main types of business within marine are hull, cargo, energy, marine and energy liabilities, yachts and marinas and other treaty. Hull consists primarily of ocean going vessels and cargo and covers worldwide risks. Energy covers a variety of oil and gas industry risks. The marine and energy liability account provides cover for protection and indemnity clubs and a wide range of companies operating in the marine and energy sector. Each of the sub-classes within marine has a different profile of contracts written—some, such as energy, derive up to 36.1% of their business through writing facultative contracts while others, such as cargo, only derive 21.9% through this method. Each of the sub-classes also has a different geographical risk allocation. Most business written is short-tail enabling a quicker and more accurate picture of expected profitability than is the case for long-tail business. The marine and energy liability account, which makes up $60.3 million of the $396.2 million of gross premiums written during the year ended December 31, 2012, is the primary long-tail class in this line. The business written is mainly on a direct and facultative basis with a small element written on a reinsurance basis either as excess of loss reinsurance or proportional reinsurance.

Specialty: This class consists of war (comprising marine & aviation war, political risks and political violence, including war on land), financial institutions, contingency, bloodstock, accident and health, airlines and aviation treaty. With the exception of aviation treaty, most of the business written under the specialty accounts is written on a direct or facultative basis or under a binding authority through a coverholder. Gross premiums written on specialty business during the year ended December 31, 2012 were $357.5 million.

War: The marine & aviation war account covers physical damage to aircraft and marine vessels caused by acts of war and terrorism. The political risk account deals primarily with expropriation, contract frustration/trade credit, kidnap and ransom, and malicious and accidental product tamper. The political violence account mainly insures physical loss to property or goods anywhere in the world, caused by war, terrorism or civil unrest. This class is often written in conjunction with cargo, specie, property, energy, contingency and political risk. The period of the risks can extend up to 36 months and beyond. The attritional losses on the account are traditionally low but the account can be affected by large individual losses. Talbot is a market leader in the war and political violence classes. Gross premiums written on war business during the year ended December 31, 2012 were $184.7 million.

Financial Institutions: Talbot's financial institutions team predominantly underwrites bankers blanket bond, professional indemnity and directors' and officers' coverage for various types of financial institutions and similar companies. Bankers blanket bond insurance products are specifically designed to protect against direct financial loss caused by fraud/criminal actions and mitigate the damage such activities may have on the asset base of the insured. Professional indemnity insurance protects businesses in the event that legal action is taken against them by third parties claiming professional negligence. Directors' and officers' insurance protects directors and officers against personal liability for losses incurred by a third party due to negligent performance by the director or officer. Gross premiums written on financial institutions business for the year ended December 31, 2012 were $35.8 million, comprising:

	Year Ended December 31, 2012		
(Dollars in thousands)	Gross Premiums Written	Gross Premiums Written (%)	
Bankers blanket bond	$20,933	58.5	%
Professional indemnity	12,887	36.0	%
Directors' and Officers'	1,986	5.5	%
Total	$35,806	100.0	%

The risks covered in financial institutions are primarily fraud related and are principally written on an excess of loss basis. Talbot's financial institutions account is concentrated on non-U.S. based clients, with 37.2% of gross premiums written in 2012 generated in Europe, 7.9% from the U.S. and 54.9% from other geographical regions. In addition, Talbot seeks to write regional accounts rather than global financial institutions with exposure in multiple jurisdictions and has only limited participation in exposures to publicly listed U.S. companies. As of December 31, 2012, the Company had gross reserves related to the financial institutions business of $157.9 million, comprised of $71.3 million, or 45.1% of incurred but not reported ("IBNR") and $86.6 million, or 54.9% of case reserves. For comparison,

as at December 31, 2011 the Company had gross reserves related to the financial institutions business of $176.7 million, comprising $69.5 million, or 39.4% of IBNR and $107.2 million, or 60.6% of case reserves. As of December 31, 2012, Talbot had minimal exposure to U.S. directors’ and officers’ risks.
Contingency: The main types of covers written under the contingency account are event cancellation and non-appearance business. Gross premiums written on contingency business during the year ended December 31, 2012 were $20.7 million.
Accident and Health: The accident and health account provides insurance in respect of individuals in both their personal and business activity together with corporations where they have an insurable interest relating to death or disability of employees

---

Table of Contents

or those under contract. Gross premiums written on accident and health business during the year ended December 31, 2012 were $19.4 million.

Aviation: The aviation account insures major airlines, general aviation, aviation hull war and satellites. The coverage includes excess of loss treaties with medium to high attachment points. Gross premiums written on aviation business during the year ended December 31, 2012 were $95.7 million.

Enterprise Risk Management

The Company has implemented an Enterprise Risk Management ("ERM") framework (the "Framework") to identify, assess, quantify and manage risks and opportunities in order to protect our capital and maximize shareholder returns. This Framework is incorporated into the business activities of the Company and its strategic planning processes.

The Company's Board of Directors has established a separate Risk Committee that is responsible for, among other things, approving the Company's ERM Framework, working with management to ensure ongoing, effective implementation of the Framework and reviewing the Company's specific risk limits as defined in the Framework, including limits for underwriting, investment, operational, business and other risks. The Company's Chief Risk Officer prepares a quarterly presentation for the Risk Committee and communicates with the chairman of the Risk Committee on an informal basis periodically throughout the year.

The management committee of the Company that oversees risk management is the Group Risk Management Committee ("GRMC"). The GRMC is comprised of senior executives including among others; the Chief Executive Officer, Chief Financial Officer, Chief Risk Officer, Chief Actuary, Chief Operating Officer, Chief Executive Officer and Chief Risk Officer of Validus Re, Chief Executive Officer and Chief Risk Officer of Talbot and the Chief Executive Officer of Validus Research and AlphaCat.

To efficiently assess risks to the Company the GRMC has identified six key risk categories. Potential risks may span several or all of these key risk areas and as such risks are considered both within the context of these areas and the Company as a whole. The key risk areas are: Credit Risk, Market Risk, Liquidity Risk, Insurance Risk, Operational Risk and Group Risk.

Risk Appetite

The Group's risk appetite sets a context within which all risks and opportunities are viewed. The risk appetite is proposed by management and approved by the Board of Directors, it represents the amount of risk the Company wants to take, within the constraints of capital resources, strategy, regulation and the rating agency environment.

Economic Capital Model

The Group uses economic capital modeling for capital adequacy assessment, risk-adjusted performance measurement and group-level and operating entity-level risk analysis.

Modeling

A pivotal factor in determining whether to found and fund the Company was the opportunity for differentiation based upon superior risk management expertise; specifically, managing catastrophe risk and optimizing our portfolio to generate attractive returns on capital while controlling our exposure to risk, and assembling a management team with the experience and expertise to do so. The Company's proprietary models are current with emerging scientific trends. This has enabled the Company to gain a competitive advantage over those reinsurers who rely exclusively on commercial models for pricing and portfolio management. The Company has made a significant investment in expertise in the risk modeling area to capitalize on this opportunity. The Company has assembled an experienced group of professional experts who operate in an environment designed to allow them to use their expertise as a competitive advantage. While the Company uses both proprietary and commercial probabilistic models, catastrophe risk is ultimately subject to absolute aggregate limitations based on risk levels determined by the Risk Committee of the Board of Directors.

Vendor Models: The Company has global licenses for all three major commercial vendor models (RMS, AIR and EQECAT), to assess the adequacy of risk pricing and to monitor its overall exposure to risk in correlated geographic zones. Commencing in January 2012, the Company incorporated RMS version 11 into its vendor models. The Company models property exposures that could potentially lead to an over-aggregation of property risks (i.e., catastrophe-exposed business) using the vendor models. The vendor models enable the Company to aggregate exposures by correlated event loss scenarios, which are probability-weighted. This enables the generation of exceedance probability curves for the portfolio and major geographic areas. Once exposures are modeled using one of the vendor models, the other two models are used as a reasonability check and validation of the loss scenarios developed and reported by the first. The three commercial models each have unique strengths and weaknesses. For example, it is sometimes necessary to impose changes to frequency and severity ahead of changes made by the model vendors.

The Company's review of market practice revealed a number of areas where quantitative expertise can be used to improve the reliability of the vendor model outputs:

- Ceding companies may often report insufficient data and many reinsurers may not be sufficiently critical in their analysis of this data. The Company generally scrutinizes data for anomalies that may indicate insufficient data quality. These circumstances are addressed by either declining the program or, if the variances are manageable, by modifying the model output and pricing to reflect insufficient data quality;
- Prior to making overall adjustments for changes in climate variables, other variables are carefully examined (for example, demand surge, storm surge, and secondary uncertainty); and
- Pricing individual contracts frequently requires further adjustments to the three vendor models. Examples include bias in damage curves for commercial structures and occupancies and frequency of specific perils.

In addition, many risks, such as second-event covers, aggregate excess of loss, or attritional loss components cannot be fully evaluated using the vendor models. In order to better evaluate and price these risks, the Company has developed proprietary analytical tools, such as VCAPS and other models and data sets.

Proprietary Models: In addition to making frequency and severity adjustments to the vendor model outputs, the Company has implemented a proprietary pricing and risk management tool, VCAPS, to assist in pricing submissions and monitoring risk aggregation.

To supplement the analysis performed using vendor models, VCAPS uses the gross loss output of catastrophe models to generate a 100,000-year simulation set, which is used for both pricing and risk management. This approach allows more precise measurement and pricing of exposures. The two primary benefits of this approach are:

- VCAPS takes into account annual limits, event/franchise/annual aggregate deductibles, and reinstatement premiums. This allows for more accurate evaluation of treaties with a broad range of features, including both common (reinstatement premium and annual limits) and complex features (second or third event coverage, aggregate excess of loss, attritional loss components, covers with varying attachment across different geographical zones or lines of businesses and covers with complicated structures); and
- VCAPS use of 100,000-year simulations enables robust pricing of catastrophe-exposed business. This is possible in real-time operation because the Company has designed a computing hardware platform and software environment to accommodate the significant computing needs.

In addition to VCAPS, the Company uses other proprietary models and other data in evaluating exposures. The Company cannot assure that the models and assumptions used by the software will accurately predict losses. Further, the Company cannot assure that the software is free of defects in the modeling logic or in the software code. In addition, the Company has not sought copyright or other legal protection for VCAPS.

Underwriting Risk Management

We underwrite and manage risk by paying close attention to risk selection and analysis. Through a detailed examination of contract terms, diversification criteria, contract experience and exposure, we aim to outperform our peers. We strive to provide our experienced underwriters with technically sound and objective information. We believe a strong working relationship between the underwriting, catastrophe modeling and actuarial disciplines is critical to long-term success and solid decision-making.

All of the Company's underwriters are subject to a set of underwriting guidelines. At Validus Re, these guidelines are established by the Chief Executive Officer and approved by the Validus Re's Board of Directors. At Talbot, the guidelines are established by executive management at Talbot and approved by their Board of Directors. These guidelines are then subject to review and approval by the Risk Committee of our Board of Directors. Underwriters are also issued letters of authority that specifically address the limits of their underwriting authority and their referral criteria. The Company's current underwriting guidelines and letters of authority include:

- lines of business that a particular underwriter is authorized to write;
- exposure limits by line of business;
- contractual exposures and limits requiring mandatory referrals to the Chief Executive Officer at Validus Re and the Chief Executive Officer at Talbot; and
- level of analysis to be performed by lines of business.

7

Table of Contents

In general, our underwriting approach is to:

- seek high quality clients who have demonstrated superior performance over an extended period;
- evaluate our clients' exposures and make adjustments where their exposure is not adequately reflected;
- apply the comprehensive knowledge and experience of our entire underwriting team to make progressive and cohesive decisions about the business they underwrite;
- employ our well-founded and carefully maintained market contacts within the group to enhance our robust distribution capabilities; and
- refer submissions to the Chief Underwriting Officer at Validus Re, the Chief Executive Officer at Talbot, Chief Executive Officer at Validus Re and the Risk Committee of our Board of Directors according to our underwriting guidelines.

The underwriting guidelines are subject to waiver or change by the Chief Executive Officer at Validus Re or the Chief Executive Officer at Talbot subject to their authority as overseen by their respective Risk Committees.

Our underwriters have the responsibility to analyze all submissions and determine if the related potential exposures meet with both the Company's risk profile line size and aggregate limitations, in line with the business plan. In order to ensure compliance, we run appropriate management information reports and all lines are subject to fully approved regulatory audits. Further, our treaty reinsurance operation has the authority limits of individual underwriters built into VCAPS while Talbot maintains separate compliance procedures to ensure that the appropriate policies and guidelines are followed.

Validus Re: Validus Re has established a referral process whereby business exceeding set exposure or premium limits is referred to the Chief Executive Officer for review. As the reviewer of such potential business, the Chief Executive Officer has the ability to determine if the business meets the Company's overall desired risk profile. The Chief Executive Officer has defined underwriting authority for each underwriter, and risks outside of this authority must be referred to the Company's Chief Executive Officer.

The Risk Committee of our Board of Directors reviews business that is outside the authority of the Chief Executive Officer.

AlphaCat: All of the investment companies managed by AlphaCat are subject to investment or underwriting guidelines. These guidelines are established in the offering documentation of the respective investment company. The AlphaCat management team manages investment portfolios in accordance with the guidelines, which are subject to oversight by the respective investment company's Board of Directors. AlphaCat leverages the Company's underwriting and analytical resources. However, all investment decisions are ultimately made by the AlphaCat management team. When services are provided to AlphaCat by the Company's underwriting teams, the applicable underwriting risk management framework outlined in this section applies.

Talbot: Talbot's risk review and control processes have been designed to ensure that all written risks comply with underwriting and risk control strategies. The workflow system is designed to automate the referral of risks to the relevant reviewer who has an appropriate level of authority to review the risk. These reviews are documented, monitored and reports are prepared on a regular basis.

Collectively, the various peer review procedures serve numerous objectives, including:

- Validating that underwriting decisions are in accordance with risk appetite, authorities, agreed business plans and standards for type, quality and profitability of risk;
- Providing an experienced and suitably qualified second review of individual risks;
- Ensuring that risks identified as significant undergo the highest level of technical underwriting review;
- Elevating technical underwriting queries and/or need for remedial actions on a timely basis; and
- Improving data accuracy and coding for subsequent management reporting.

The principal elements of the underwriting review process are as follows:

Underwriter review: The underwriting team must evidence data entry review by confirming review and agreement on the workflow system within a specified number of working days of entry being completed by the contracted third party.

Risk - based peer review: The majority of risks are peer reviewed by another underwriter within a specified number of working days of data entry being completed. There is an agreed matrix of underwriters authorized to peer review.

Table of Contents

Class of business review: Risks written into a class by an underwriter other than the nominated class underwriter are subsequently forwarded to, and reviewed by, the nominated class underwriter.
Exceptions review: Risks that exceed a set of pre-determined criteria will also be referred to the Active Underwriter or the Director of Underwriting and Operations for review. Such risks are discussed by the underwriters at regular underwriting meetings in the presence of at least one of the above. In certain circumstances, some risks may be referred to the Insurance Management Committee or the Talbot Underwriting Ltd. (“TUL”) Board for final approval. These reviews also commonly include reports of risks renewed where there has been a large loss ratio in the recent past.
Insurance Management Committee: At its regular meetings, the Committee reviews a range of key performance indicators including: premium income written versus budget; movements in syndicate cash and investments; aggregate exposures; together with other highlighted exception reports. The Committee also reviews claim movements over a financial threshold.
Expert Review Committee (“ERC”): The ERC is a committee that meets regularly to review the underwriting activities of Syndicate 1183 and other related activities to provide assurance that the underwriting risks assumed are within the parameters of the business plan. This is achieved with the help of eight external expert reviewers who report their findings to the ERC.
The expert reviewers obtain and review a sample of risks underwritten in each class and report their findings to the quarterly meetings of the ERC. Findings range from general comments on approach and processes to specific points in respect of individual risks.
Within Talbot, the TUL Board is responsible for creating the environment and structures for risk management to operate effectively. The Talbot Chief Executive is responsible for ensuring the risk management process is implemented.
The TUL Board has several committees responsible for monitoring risk. The TUL Board approves the risk appetite as part of the syndicate business plan process which sets targets for premium volume, pricing, line sizes, aggregate exposures and retention by class of business.
The TUL Executive Committee is responsible for establishing and maintaining a comprehensive risk register and key controls for TUL. It is responsible for articulating Talbot's risk appetite for approval by the TUL Board.
The key focuses of each committee are as follows:

- The TUL Executive Committee oversees the management of key risks with regard to strategy and reserves;
- The Insurance Management Committee oversees the management of insurance risks;
- The Operational Risk Committee oversees the management of risks related to people, processes, systems and external events; and
- The Financial Risk Committee oversees the management of credit risks associated with reinsurers, brokers, coverholders and investments, market risk and liquidity risk.

Performance against underwriting targets is measured regularly throughout the year. Risks written are subject to peer review, an internal quality control process. Pricing is controlled by the monitoring of rate movements and the comparison of technical prices to actual prices. Controls over aggregation of claims exposures vary by class of business. They include limiting coastal risks, monitoring aggregation by county/region/blast zones and applying line size limits in all cases. Catastrophe modeling software and techniques are used to model expected loss outcomes for Lloyd’s Realistic Disaster Scenario returns and in-house catastrophe event scenarios. Reserves are reviewed for adequacy on a quarterly basis. The syndicate also purchases reinsurance, with an appropriate number of reinstatements, to arrive at an acceptable net retained risk.
Program Limits
Overall exposure to risk is controlled by limiting the amount of insurance or reinsurance underwritten in a particular program or contract. This helps to diversify risk within and across risk zones. The Risk Committee sets these limits, which may be exceeded only with its approval.
Geographic Diversification
The Company actively manages its aggregate exposures by geographic or risk zone (“zones”) to maintain a balanced and diverse portfolio of underlying risks. The coverage the Company is willing to provide for any risk located in a

particular zone is limited to a predetermined level, thus limiting the net aggregate loss exposure from all contracts covering risks believed to be located in any zone. Contracts that have “worldwide” territorial limits have exposures in several geographic zones. Generally, if a proposed reinsurance program would cause the limit to be exceeded, the program would be declined, regardless of its desirability,

Table of Contents

unless the Company buys retrocessional coverage, thereby reducing the net aggregate exposure to the maximum limit permitted or less. The following table summarizes our gross premiums written by geographic zone:

	Year Ended December 31, 2012 Gross Premiums Written					
	Validus Re	AlphaCat	Talbot	Corporate and Eliminations	Total	%
United States	$468,730	$18,774	$120,086	$(7,285)	$600,305	27.7 %
Worldwide excluding United States (a)	40,168	—	263,597	(16,049)	287,716	13.3 %
Europe	90,673	1,333	50,262	(2,868)	139,400	6.4 %
Latin America and Caribbean	33,031	—	103,543	(6,164)	130,410	6.0 %
Japan	30,781	—	6,630	(396)	37,015	1.7 %
Canada	688	—	12,243	(690)	12,241	0.6 %
Rest of the world (b)	68,754	496	—	—	69,250	3.2 %
Sub-total, non United States	264,095	1,829	436,275	(26,167)	676,032	31.2 %
Worldwide including United States	101,594	1,000	65,084	(3,552)	164,126	7.6 %
Marine and Aerospace (c)	297,540	—	457,191	(28,754)	725,977	33.5 %
Total	$1,131,959	$21,603	$1,078,636	$(65,758)	$2,166,440	100.0 %

(a) Represents risks in two or more geographic zones.
(b) Represents risk in one geographic zone.
(c) Not classified by geographic area as marine and aerospace risks can span multiple geographic areas and are not fixed locations in some instances.

The effectiveness of geographic zone limits in managing risk exposure depends on the degree to which an actual event is confined to the zone in question and on the Company's ability to determine the actual location of the risks believed to be covered under a particular insurance or reinsurance program. Accordingly, there can be no assurance that risk exposure in any particular zone will not exceed that zone's limits. Further control over diversification is achieved through guidelines covering the types and amount of business written in product classes and lines within a class.

Reinsurance Management

Validus Re Retrocession: Validus Re monitors the opportunity to purchase retrocessional coverage on a continual basis and employs the VCAPS modeling system to evaluate the effectiveness of risk mitigation and exposure management relative to the cost. This coverage may be purchased on an indemnity basis as well as on an index basis (e.g., industry loss warranties ("ILWs")). Validus Re also considers alternative retrocessional structures, including collateralized quota share ("sidecar") and other capital markets products.

When Validus Re buys retrocessional coverage on an indemnity basis, payment is for an agreed upon portion of the losses actually suffered. In contrast, when Validus Re buys an ILW cover, which is a reinsurance contract in which the payout is dependent on both the insured loss of the policy purchaser and the measure of the industry-wide loss, payment is made only if both Validus Re and the industry suffer a loss, as reported by one of a number of independent agencies, in excess of specified threshold amounts. With an ILW, Validus Re bears the risk of suffering a loss while receiving no payment under the ILW if the industry loss was less than the specified threshold amount.

Validus Re may use capital markets instruments for risk management in the future (e.g., catastrophe bonds, sidecar facilities and other forms of risk securitization) where the pricing and terms are attractive.

AlphaCat: AlphaCat currently does not cede any premiums to third parties.

Talbot Ceded Reinsurance: Talbot enters into reinsurance agreements in order to mitigate its accumulation of loss, reduce its liability on individual risks and enable it to underwrite policies with higher limits. The ceding of the insurance does not legally discharge Talbot from its primary liability for the full amount of the policies, and Talbot is required to pay the loss and bear collection risk if the reinsurer fails to meet its obligations under the reinsurance agreement.

The following describes the Talbot Group’s process in the purchase and authorization of treaty reinsurance policies only. It does not cover the purchase of facultative reinsurance because these premiums are not significant.

Table of Contents

The reinsurance program is reviewed by the reinsurance purchasing team on an on-going basis in line with the main business planning process. This process incorporates advice and analytical work from our brokers, actuarial and capital modeling teams.

The review and modification is based upon the following:

- budgeted underwriting for the coming year;
- loss experience from prior years;
- loss information from the coming year's individual capital assessment calculations;
- changes to risk limits and aggregation limits expected and any other changes to Talbot's risk tolerance;
- scenario planning;
- changes to capital requirements; and
- Realistic Disaster Scenarios ("RDSs") prescribed by Lloyd's.

The main type of reinsurance purchased is losses occurring; however, for a few lines of business, where the timing of the loss event is less easily verified or where such cover is available, risk attaching policies are purchased.

The type, quantity and cost of cover of the proposed reinsurance program is discussed and reviewed by the Chief Executive Officer of the Talbot group, and ultimately authorized by the TUL Board.

Once this has occurred, the reinsurance program is purchased in the months prior to the beginning of the covered period. All reinsurance contracts arranged are authorized for purchase by the Director of Underwriting and Operations. Slips are developed prior to inception to ensure that optimum cover is achieved. After purchase, cover notes are reviewed by the relevant class underwriters and presentations made to all underwriting staff to ensure they are aware of the boundaries of the cover.

Distribution

Although we conduct some business on a direct basis with our treaty and facultative reinsurance clients, most of our business is derived through insurance and reinsurance intermediaries ("brokers"), who access business from clients and coverholders. We are able to attract business through our recognized lead capability in most classes we underwrite, particularly in classes where such lead ability is rare.

Currently, our largest broker relationships, as measured by gross premiums written, are with Marsh & McLennan, Aon Benfield Group Ltd. and Willis Group Holdings Ltd. The following table sets forth the Company's gross premiums written by broker:

	Year Ended December 31, 2012 Gross Premiums Written					
(Dollars in thousands)	Validus Re	AlphaCat	Talbot	Corporate and Eliminations	Total	%
Name of Broker						
Marsh & McLennan	$399,325	$7,426	$244,776	$ (14,809)	$636,718	29.4 %
Aon Benfield Group Ltd.	400,018	6,133	180,234	(10,904)	575,481	26.5 %
Willis Group Holdings Ltd.	187,353	3,418	167,249	(10,119)	347,901	16.1 %
Sub-total	986,696	16,977	592,259	(35,832)	1,560,100	72.0 %
All Others/Direct	145,263	4,626	486,377	(29,926)	606,340	28.0 %
Total	$1,131,959	$21,603	$1,078,636	$ (65,758)	$2,166,440	100.0 %

Reserve for losses and loss expenses

For insurance and reinsurance companies, a significant judgment made by management is the estimation of the reserve for losses and loss expenses. The Company establishes its reserve for losses and loss expenses to cover the estimated incurred liability for both reported and unreported claims.

The following tables show certain information with respect to the Company's gross and net reserves:

Table of Contents

(Dollars in thousands)	As at December 31, 2012 Gross Case Reserves	Gross IBNR	Total Gross Reserve for Losses and Loss Expenses
Property	$930,553	$892,227	$1,822,780
Marine	522,907	477,948	1,000,855
Specialty	265,638	428,300	693,938
Total	$1,719,098	$1,798,475	$3,517,573

(Dollars in thousands)	As at December 31, 2012 Net Case Reserves	Net IBNR	Total Net Reserve for Losses and Loss Expenses
Property	$768,722	$803,182	$1,571,904
Marine	465,080	438,009	903,089
Specialty	230,584	372,029	602,613
Total	$1,464,386	$1,613,220	$3,077,606

Loss reserves are established due to the significant periods of time that may lapse between the occurrence, reporting and payment of a loss. To recognize liabilities for unpaid losses and loss expenses, the Company estimates future amounts needed to pay claims and related expenses with respect to insured events. The Company’s reserving practices and the establishment of any particular reserve reflects management’s judgment concerning sound financial practice and does not represent any admission of liability with respect to any claim. Unpaid losses and loss expense reserves are established for reported claims (“case reserves”) and IBNR claims.

The nature of the Company’s high excess of loss liability and catastrophe business can result in loss payments that are both irregular and significant. Such loss payments are part of the normal course of business for the Company. Adjustments to reserves for individual years can also be irregular and significant. Conditions and trends that have affected development of liabilities in the past may not necessarily occur in the future. Accordingly, it is inappropriate to extrapolate future redundancies or deficiencies based upon historical experience. See Part I, Item 1A, “Risk Factors” and Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Cautionary Note Regarding Forward-Looking Statements.”

The tables below present the development of the Company’s unpaid losses and loss expense reserves on both a net and gross basis. The cumulative redundancy (deficiency) calculated on a net basis differs from that calculated on a gross basis. As different reinsurance programs cover different underwriting years, net and gross loss experience will not develop proportionately. The top line of the tables shows the estimated liability, net and gross of reinsurance recoveries, as at the year end balance sheet date for each of the indicated years. This represents the estimated amounts of losses and loss expenses, including IBNR, arising in the current and all prior years that are unpaid at the year end balance sheet date of the indicated year. The tables also show the re-estimated amount of the previously recorded reserve liability based on experience as of the year end balance sheet date of each succeeding year. The estimate changes as more information becomes known about the frequency and severity of claims for individual years. The cumulative redundancy (deficiency) represents the aggregate change with respect to that liability originally estimated. The lower portion of each table also reflects the cumulative paid losses relating to these reserves. Conditions and trends that have affected development of liabilities in the past may not necessarily occur in the future. Accordingly, it is not appropriate to extrapolate redundancies or deficiencies into the future, based on the tables below. See Part I, Item 1A, “Risk Factors” and Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Cautionary Note Regarding Forward-Looking Statements.”

Table of Contents

Analysis of Losses and Loss Expense Reserve Development Net of Recoveries

	Years Ended December 31,						
(Dollars in thousands)	2006	2007	2008	2009	2010	2011	2012 (b)
Estimated liability for unpaid losses and loss expense, net of reinsurance recoverable	$77,363	$791,713	$1,096,507	$1,440,369	$1,752,839	$2,258,658	$3,077,606
Liability—estimated as of:							
One year later	60,106	722,010	1,018,930	1,283,759	1,596,720	2,083,378	
Two years later	54,302	670,069	937,696	1,181,987	1,451,448		
Three years later	50,149	606,387	902,161	1,085,664			
Four years later	46,851	584,588	847,935				
Five years later	45,946	547,965					
Six years later	45,199						
Cumulative redundancy (deficiency)(a)	32,164	243,748	248,572	354,705	301,391	175,280	
Cumulative paid losses, net of reinsurance recoveries, as of:							
One year later	$27,180	$216,469	$353,476	$384,828	$476,779	$631,889	
Two years later	34,935	320,803	562,831	634,041	741,940		
Three years later	39,520	350,521	662,319	744,324			
Four years later	41,746	374,788	722,652				
Five years later	41,901	390,895					
Six years later	43,571						

(a) See Part II Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” for further discussion.

(b) The reserves for losses and loss expenses or Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Table of Contents

Analysis of Losses and Loss Expense Reserve Development Gross of Recoveries

	Years Ended December 31,						
(Dollars in thousands)	2006	2007	2008	2009	2010	2011	2012 (b)
Estimated gross liability for unpaid losses and loss expense	$77,363	$926,117	$1,305,303	$1,622,134	$2,035,973	$2,631,143	$3,517,573
Liability—estimated as of:							
One year later	60,106	846,863	1,223,018	1,484,646	1,854,565	2,422,343	
Two years later	54,302	791,438	1,164,923	1,385,533	1,705,995		
Three years later	50,149	745,624	1,134,043	1,288,915			
Four years later	46,851	721,730	1,079,842				
Five years later	45,946	675,884					
Six years later	46,104						
Cumulative redundancy (deficiency)(a)	31,259	250,233	225,461	333,219	329,978	208,800	
Cumulative paid losses, gross of reinsurance recoveries, as of:							
One year later	$27,180	$245,240	$437,210	$455,182	$557,894	$807,296	
Two years later	34,935	394,685	706,249	709,309	878,406		
Three years later	39,520	452,559	825,159	864,918			
Four years later	41,746	480,277	898,338				
Five years later	41,901	496,511					
Six years later	43,571						

(a) See Part II Item 7 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” for further discussion.

(b) The reserves for losses and loss expenses or Flagstone are consolidated only from the November 30, 2012 date of acquisition.

The following table presents an analysis of the Company’s paid, unpaid and incurred losses and loss expenses and a reconciliation of beginning and ending unpaid losses and loss expenses for the years indicated:

Table of Contents

	Years Ended December 31,		
(Dollars in thousands)	2012	2011	2010
Reserve for losses and loss expenses, beginning of year	$2,631,143	$2,035,973	$1,622,134
Losses and loss expenses recoverable	(372,485)	(283,134)	(181,765)
Net reserves for losses and loss expenses, beginning of year	2,258,658	1,752,839	1,440,369
Net loss reserves acquired in Flagstone acquisition	639,641	—	—
Increase (decrease) in net losses and loss expenses incurred in respect of losses occurring in:			
Current year	1,174,415	1,400,520	1,144,196
Prior years	(174,969)	(156,119)	(156,610)
Total incurred losses and loss expenses	999,446	1,244,401	987,586
Less net losses and loss expenses paid in respect of losses occurring in:			
Current year	(182,146)	(266,247)	(288,594)
Prior years	(653,874)	(476,779)	(384,828)
Total net paid losses	(836,020)	(743,026)	(673,422)
Foreign exchange	15,881	4,444	(1,694)
Net reserve for losses and loss expenses, end of year	3,077,606	2,258,658	1,752,839
Losses and loss expenses recoverable	439,967	372,485	283,134
Reserve for losses and loss expenses, end of year	$3,517,573	$2,631,143	$2,035,973

Validus Re and AlphaCat: Validus Re and AlphaCat's loss reserves are established based upon an estimate of the total cost of claims that have been incurred, including estimates of unpaid liability on known individual claims, the costs of additional case reserves on claims reported but not considered to be adequately reserved in such reporting ("ACRs") and amounts that have been incurred but not yet reported. ACRs are used in certain cases and may be calculated based on management's estimate of the required case reserve on an individual claim less the case reserves reported by the client. The Validus Re Loss Reserve Committee follows material catastrophe event ultimate loss reserve estimation procedures for the investigation, analysis, estimation and approval of ultimate loss reserving resulting from any material catastrophe event. U.S. GAAP does not permit the establishment of loss reserves until an event occurs that gives rise to a loss.

For reported losses, Validus Re and AlphaCat establish case reserves within the parameters of the coverage provided in the impacted reinsurance contracts. Where there is a reported claim for which the reported case reserve is determined to be insufficient, Validus Re and AlphaCat may book an ACR or individual claim IBNR estimate that is adjusted as claims notifications are received. Information may be obtained from various sources including brokers, proprietary and third party vendor models and internal data regarding reinsured exposures related to the geographic location of the event, as well as other sources. Validus Re and AlphaCat use generally accepted actuarial techniques in its IBNR estimation process. Validus Re and AlphaCat also use historical insurance industry loss emergence patterns, as well as estimates of future trends in claims severity, frequency and other factors, to aid it in establishing loss reserves.

Loss reserves represent estimates, including actuarial and statistical projections at a given point in time, of the expectations of the ultimate settlement and administration costs of claims incurred. Such estimates are not precise in that, among other things, they are based on predictions of future developments and estimates of future trends in loss severity and frequency and other variable factors such as inflation, litigation and tort reform. This uncertainty is heightened by the short time in which Validus Re has operated, thereby providing limited claims loss emergence patterns that directly pertain to Validus Re's operations. This has necessitated the use of industry loss emergence patterns in deriving IBNR, which despite management's and our actuaries' care in selecting them, will differ from actual experience. Further, expected losses and loss ratios are typically developed using vendor and proprietary computer models and these expected losses and loss ratios are a significant component in the calculation deriving IBNR. Finally, the uncertainty surrounding estimated costs is greater in cases where large, unique events have been reported and the associated claims are in early stages of resolution. As a result of these uncertainties, it is likely that the ultimate liability will differ from such estimates, perhaps materially.

For disclosure purposes, only those loss events which aggregate to over $15.0 million on a consolidated basis ("notable losses") are disclosed separately and included in the reserve for notable loss events and reserve for development on events tables. Notable loss events are first determined at the respective operating segments based on segment thresholds and are then aggregated and disclosed if it is determined that they reach the consolidated threshold for notable loss disclosure.

Table of Contents

During 2010 and 2011, given the complexity and severity of notable loss events in the year, an explicit reserve for potential development on 2010 and 2011 notable loss events ("RDE") was included within the Company’s IBNR reserving process. As uncertainties surrounding initial estimates on notable loss events have developed, this reserve has been and will continue to be allocated to specific notable loss events. No RDE was established for 2012 notable losses.

The requirement for a reserve for potential development on notable loss events in a quarter is a function of (a) the number of significant events occurring in that quarter and (b) the complexity and volatility of those events. Complexity and volatility factors considered are as follows:

• Contract complexity;
• Nature and number of perils arising from an event;
• Limits and sub limits exposed;
• Quality, timing and flow of information received from each loss;
• Timing of receipt of information to the Company;
• Information regarding retrocessional covers;
• Assumptions, both explicit and implicit, regarding future paid and reported loss development patterns;
• Frequency and severity trends;
• Claims settlement practices; and
• Potential changes in the legal environment.

Each of these factors may lead to associated volatility for each notable loss event as well as consideration of the total reserve for loss events in the aggregate. Consequently, all of these factors are considered in the aggregate for the events occurring in the quarter, recognizing that it is more likely that one or some of the events may deteriorate significantly, rather than all deteriorating proportionately. The establishment of each quarter’s requirement for a reserve for potential development on notable loss events takes place as part of the quarterly evaluation of the Company’s overall reserve requirements. It is not directly linked in isolation to any one significant/notable loss in the quarter. The reserve for potential development on notable loss events is evaluated by our in-house actuaries as part of their normal process in setting of indicated reserves for the quarter. In ensuing quarters senior management and the in-house actuaries revisit and re-estimate certain events previously considered in the catastrophe loss event process as well as events that have subsequently emerged in the current quarter. To the extent that there has been adverse development on a notable loss event, if there is RDE remaining from that accident year, an allocation from the respective accident year RDE will be made to the notable loss event. If there is no remaining RDE relating to the accident year of the loss, then adverse development will be recorded for the notable loss event through the Statements of Comprehensive Income.

Changes to the reserve for potential development on notable loss events will be considered in light of changes to previous loss estimates from notable losses in this re-estimation process.To the extent that there are continued complexity and volatility factors relating to notable loss events in the aggregate, additions to the RDE may be established for a specific accident year, as illustrated in the RDE roll forward table which can be found in Item. 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Loss reserves are reviewed regularly and adjustments to reserves, if any, will be recorded in earnings in the period in which they are determined. Even after such adjustments, the ultimate liability may exceed or be less than the revised estimates.

Talbot: Talbot’s loss reserves are established based upon an estimate of the total cost of claims that have been incurred, including case reserves and IBNR. Talbot uses generally accepted actuarial techniques in its IBNR estimation process. ACRs are not generally used.

Talbot performs internal assessments of liabilities on a quarterly basis. Talbot’s loss reserving process involves the assessment of actuarial estimates of gross ultimate losses on both an ultimate basis (i.e., ignoring the period during which premium earns) and an earned basis, split by underwriting year and class of business, and generally also between attritional, large and catastrophe losses. These estimates are made using a variety of generally accepted actuarial projection methodologies, as well as additional qualitative consideration of future trends in frequency, severity and other factors. The gross estimates are used to estimate ceded reinsurance recoveries, which are in turn used to calculate net ultimate losses as the difference between gross and ceded. These figures are subsequently used by Talbot's management to help it assess its best estimate of gross and net ultimate losses.

As with Validus Re and AlphaCat, Talbot's loss reserves represent estimates, including actuarial and statistical projections at a given point in time, of the expectations of the ultimate settlement and administration costs of claims incurred. Such estimates are not precise in that, among other things, they are based on predictions of future developments and estimates of future trends in loss severity and frequency and other variable factors such as inflation, litigation and tort reform. The uncertainty surrounding estimated costs is also greater in cases where large, unique events have been reported and the associated claims are in the early stages of resolution. As a result of these uncertainties, it is likely that the ultimate liability will differ from such estimates, perhaps materially.

Table of Contents

Talbot’s loss reserves are reviewed regularly and adjustments to reserves, if any, will be recorded in earnings in the period in which they are determined. Even after such adjustments, the ultimate liability may exceed or be less than the revised estimates. See Part I, Item 1A, “Risk Factors” and Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Cautionary Note Regarding Forward-Looking Statements.”

Investment Management

The Company manages its investment portfolio on a consolidated basis. As we provide short-tail insurance and reinsurance coverage, we could become liable to pay substantial claims on short notice. Accordingly, we follow a conservative investment strategy designed to emphasize the preservation of invested assets and provide sufficient liquidity for the prompt payment of claims. Our Board of Directors, led by our Finance Committee, oversees our investment strategy, and in consultation with BlackRock Financial Management, Inc., Conning, Inc. and Pinebridge Investments Europe Ltd., our portfolio advisors, has established investment guidelines for us. The investment guidelines dictate the portfolio’s overall objective, benchmark portfolio, eligible securities, duration, use of derivatives, inclusion of foreign securities, diversification requirements and average portfolio rating. Management and the Finance Committee periodically review these guidelines in light of our investment goals and consequently they may change at any time.

Substantially all of the fixed maturity investments held at December 31, 2012 were publicly traded. At December 31, 2012, the average duration of the Company’s fixed maturity portfolio was 1.34 years (December 31, 2011: 1.63 years). Management emphasizes capital preservation for the portfolio and maintains a significant allocation of short-term investments. At December 31, 2012, the average rating of the portfolio was AA- (December 31, 2011: AA-). At December 31, 2012, the total fixed maturity portfolio was $5,085.3 million (December 31, 2011: $4,894.1 million), of which $1,062.8 million (December 31, 2011: $882.9 million) were rated AAA.

Please refer to our Current Report on Form 8-K furnished to the Securities and Exchange Commission (the “SEC”) on January 31, 2013 for additional disclosure with respect to the composition of our investment portfolio.

Claims Management

Claims management includes the receipt of initial loss notifications, generation of appropriate responses to claim reports, identification and handling of coverage issues, determination of whether further investigation is required and, where appropriate retention of legal representation, establishment of case reserves, approval of loss payments and notification to reinsurers.

Validus Re and AlphaCat: The role of our claims department is to investigate, evaluate and, if validated, pay claims efficiently. Our claims director has implemented claims handling guidelines, and reporting and control procedures. The primary objectives of the claims department are to ensure that each claim is evaluated, processed and appropriately documented in a timely and efficient manner and information relevant to the management of the claim is retained.

Talbot: Where Talbot is the lead syndicate on business written, the claims adjusters will, in accordance with the respective policies, assess, investigate, appoint third party experts (including attorneys, loss adjusters or other experts) as required and communicate the Company's actions or findings to the Broker who represents the insured. The Company will also establish adequate reserves and promptly pay valid claims in accordance with the applicable "Lloyd's Claims Scheme" and "Lloyd's Claims Management Principles and Minimum Standards."

Where Talbot is not the lead syndicate, the claims handling and case reserves are established in accordance with the applicable "Lloyd's Claims Scheme" and "Lloyd's Claims Management Principles and Minimum Standards." Material claims and claims movements are reviewed and monitored by the Talbot claims department. Claim financial reports are received daily from the "Xchanging" system pursuant to a centralized contract with Lloyd's.

Competition

The insurance and reinsurance industries are highly competitive. We compete with major U.S., Bermuda, European and other international insurers and reinsurers and certain underwriting syndicates and insurers. We encounter competition in all of our classes of business but there is less competition in those of our lines where we are a specialist underwriter. The Company competes with insurance and reinsurance providers such as:

- Arch Capital Group Limited, Argo Group International Holdings, Ltd., Aspen Insurance Holdings Limited, Alterra Capital Holdings, Ltd., Allied World Assurance Company Holdings Limited, Alleghany Corporation, Axis Capital

Holdings Limited, Endurance Specialty Holdings Limited, Everest Re Group Limited, Montpelier Re Holdings Ltd, PartnerRe Ltd., Platinum Underwriters Holdings Ltd., and Renaissance Reinsurance Holdings Ltd.;

- Amlin plc, Catlin Group Limited, Hiscox and others in the Lloyd’s market;

Table of Contents

- Treaty and direct insurers, in not only the global but also the London Market, that compete with Lloyd's on a worldwide basis;
- Various capital markets participants who access insurance and reinsurance business in securitized form, through special purpose entities or derivative transactions; and
- Government-sponsored insurers and reinsurers.

Competition varies depending on the type of business being insured or reinsured and whether the Company is in a leading or following position. Competition in the types of business that the Company underwrites is based on many factors, including:

- Premiums charged and other terms and conditions offered;
- Services provided;
- Financial ratings assigned by independent rating agencies;
- Speed of claims payment;
- Reputation;
- Perceived financial strength; and
- The experience of the underwriter in the line of insurance or reinsurance written.

Increased competition could result in fewer submissions, lower premium rates, lower share of allocated cover, and less favorable policy terms, which could adversely impact the Company's growth and profitability. Capital market participants have created alternative products such as catastrophe bonds that are intended to compete with reinsurance products. The Company is unable to predict the extent to which these new, proposed or potential initiatives may affect the demand for products or the risks that may be available to consider underwriting.

Regulation

Bermuda

General. As a holding company, Validus Holdings, Ltd. is not subject to Bermuda insurance regulation. However, the Insurance Act 1978 (the "Insurance Act") regulates the Company's operating subsidiaries in Bermuda, and it provides that no person may carry on any insurance business in or from within Bermuda unless registered as an insurer by the Bermuda Monetary Authority (the "BMA") under the Insurance Act. The Insurance Act makes no distinction between insurance and reinsurance business. The Company has nine Bermuda based subsidiaries, Validus Re, a Class 4 insurer, Validus Re Americas, Ltd., a Class 4 insurer, Flagstone Reassurance Suisse SA (Bermuda Branch), a Class 4 insurer, PaCRe, Ltd., a Class 4 insurer, Talbot Insurance (Bermuda), Ltd., a Class 3 insurer, AlphaCat Reinsurance, Ltd., a Class 3 insurer , Mont Fort Re Ltd., a Class 3 insurer, AlphaCat Re 2011, Ltd., a Special Purpose Insurer ("SPI") and AlphaCat Re 2012, Ltd., an SPI, each registered under the Insurance Act.

Principal Representative. The Insurance Act requires that every insurer, including the Bermuda insurance subsidiaries of the Company, appoint and maintain a principal representative resident in Bermuda and maintain a principal office in Bermuda. It is the duty of the principal representative on his reaching a view that there is a likelihood of the insurer for which the principal representative acts becoming insolvent or that a reportable "event" has, to the principal representative's knowledge, occurred, to immediately notify the BMA and to make a report in writing to the BMA within 14 days of the prior notification setting out all the particulars of the case that are available to the principal representative.

Where there has been a significant loss which is reasonably likely to cause the insurer to fail to comply with its enhanced capital requirement, the principal representative must also furnish the BMA with a capital and solvency return reflecting an enhanced capital requirement prepared using post-loss data. The principal representative must provide this within 45 days of notifying the BMA regarding the loss.

Furthermore, where a notification has been made to the BMA regarding a material change to an insurer's business or structure (including merger or amalgamation), the principal representative has 30 days from the date of such notification to furnish the BMA with unaudited interim statutory financial statements in relation to such period as the Authority may require, together with a general business solvency certificate in respect of those statements.

Approved Independent Auditor. Every registered insurer must appoint an independent auditor who will annually audit and report on the statutory financial statements and the statutory financial return of the insurer, all of which, in the case of all registered insurers in Bermuda, are required to be filed annually with the BMA. The independent auditor must be approved by the BMA.

Table of Contents

Approved Loss Reserve Specialist. Every registered insurer is required to submit an opinion of its approved loss reserve specialist with its statutory financial return in respect of its loss and loss expense provisions in respect to all licensed entities. The loss reserve specialist, who will normally be a qualified casualty actuary, must be approved by the BMA.

Annual Financial Statements, Annual Statutory Financial Return and Annual Capital and Solvency Return. Every registered insurer must prepare annual statutory financial statements as prescribed in the Insurance Act with respect to all licensed entities. The statutory financial statements are separate from the annual GAAP basis financial statements discussed further below. All licensed entities are also required to prepare and file with the BMA statutory financial returns with respect to its general business unless granted an exemption under section 56 of the Insurance Act. The statutory financial return includes, among other items, a report of the approved independent auditor on the statutory financial statement of such insurer, solvency certificates, the statutory financial statements for the general business, the opinion of the loss reserve specialist and a schedule of reinsurance ceded (Class 4 only). Validus Re and PaCRe are also required to file audited GAAP basis annual financial statements, which are made available to the public. In addition, Validus Re and PaCRe are required to file a capital and solvency return in respect of its general business which shall include the regulatory risk based capital model, a schedule of fixed income investments by rating categories, a schedule of net reserves for losses and loss expense provisions by line of business, a schedule of premiums written by line of business, a schedule of risk management and a schedule of fixed income securities.

Minimum Solvency Margins. The value of the general business assets of licensed insurers must exceed the amount of its general business liabilities by an amount greater than the prescribed minimum solvency margin “MSM,” being equal to the greater of:

Class 3:

(a)$1,000,000;

(b)20% of net premiums written (not to exceed $6,000,000 in net premium written) (being gross premiums written less any premiums ceded by the insurer, but the insurer may not deduct more than 25% of gross premiums when computing net premiums written); or $1,200,000 plus 15% of amount which exceeds $6,000,000; or

(c)15% of net losses and loss expense reserves.

Class 4:

(a)$100,000,000;

(b)50% of net premiums written (being gross premiums written less any premiums ceded by the insurer, but the insurer may not deduct more than 25% of gross premiums when computing net premiums written); or

(c)15% of net losses and loss expense reserves.

Enhanced Capital Requirement. A Class 4 insurer is required to maintain available statutory capital and surplus in regards to its general business at level equal to or in excess of its enhanced capital requirement (“ECR”) which is calculated at the end of its relevant year by reference to the Bermuda Solvency Capital Requirement model (“BSCR”) or an approved internal capital model. The BSCR employs a standard mathematical model that correlates risk underwritten by Bermuda insurers to the capital that is dedicated to the business. The ECR is equal to the higher of each insurer's MSM or the BSCR/approved internal capital model. A Class 4 insurer is also expected to hold a safety margin or buffer above the ECR, which is at least in total equivalent to 120% of its ECR, the target capital level (“TCL”). The TCL will serve as an early warning signal for the BMA, and failure to maintain capital at least equal to the TCL may result in additional reporting requirements or other enhanced regulatory oversight. Presently the BSCR model applies to Validus Re and PaCRe.

Eligible Capital: The tiered capital system (Tiers 1, 2, and 3) classify capital instruments into a given tier based on their loss absorbency characteristics. Eligibility limits are then applied to each tier in determining the amounts eligible to cover regulatory capital requirement levels. The highest capital will be classified Tier 1 Capital, lesser quality capital will be classified as either Tier 2 Capital or Tier 3 Capital. Under this regime, not less than 80% of Tier 1 Capital and up to 20% of Tier 2 Capital may be used to support a company' s minimum solvency margin for its general business. Thereafter, a minimum of 60% of Tier 1 Capital and a maximum of 15% of Tier 3 Capital may be used to satisfy the Company's ECR. Any combination of Tier 1, 2, or 3 Capital may be used to meet the TCL. Eligible Capital Rules currently apply to Validus Re and PaCRe.

Group Supervision. The BMA may, in respect of an insurance group, determine whether it is appropriate for it to be the group supervisor of that group. For purposes of the Insurance Act, an insurance group is defined as a group of companies that conducts exclusively, or mainly, insurance business. The BMA may make such determination where it ascertains that (i) the group is headed by a "specified insurer" (that is to say, it is headed by either a Class 4, 3A, 3B or Class E insurer or another class of insurer designated by order of the BMA); or (ii) where the insurance group is not headed by a "specified insurer" where it is headed by a parent company which is incorporated in Bermuda; or (iii) where the parent company of the group is not a Bermuda company, where the BMA is satisfied that the insurance group is directed and managed from Bermuda or the insurer with the largest balance sheet total is a specified insurer. Where the BMA determines that it should act as the group supervisor, it shall designate a specified insurer that is a member of the insurance group to be the "designated insurer" and it shall give written notice to the designated insurer and other competent authorities of its intention to act as group supervisor.

In 2011, the BMA notified the Company that it intended to act as group supervisor and that it had designated Validus Re as the "designated insurer" of our group of insurance and reinsurance companies. Pursuant to its powers under the Insurance Act, the BMA will maintain a register of particulars for every insurance group for which it acts as the group supervisor detailing, among other things, the names and addresses of the designated insurer; each member company of the insurance group falling within the scope of group supervision; the principal representative of the insurance group in Bermuda; other competent authorities supervising other member companies of the insurance group; and the insurance group auditors. The designated insurer must notify the BMA of any changes to the above details entered on the register of an insurance group.

As group supervisor, the BMA will perform a number of supervisory functions including (i) coordinating the gathering and dissemination of information which is of importance for the supervisory task of other competent authorities; (ii) carrying out a supervisory review and assessment of the financial situation of the insurance group; (iii) carrying out an assessment of the insurance group's compliance with the rules on solvency, risk concentration, intra-group transactions and governance procedures; (iv) planning and coordinating, with other competent authorities, supervisory activities in respect of the insurance group, (v) coordinating any enforcement action that may need to be taken against the insurance group or any of its members; and (vi) planning and coordinating meetings of colleges of supervisors (consisting of insurance regulators) in order to facilitate the carrying out of the functions described above.

Group Solvency. The Insurance (Prudential Standards) (Insurance Group Solvency Requirement) Rules and Insurance (Group Supervision) Rules (together, "Group Rules"), will apply to the Company so long as the BMA remains our group supervisor. The BMA has implemented and imposed many of the additional requirements described in this section as part of its efforts to gain equivalence under Solvency II. The BMA will now wait until further notice to implement Solvency II as a result of the delay in the implementation of Solvency II in Europe. In addition, through the Group Rules, the BMA may take action which affects the Company. A summary of the Group Rules is set forth below.

Group Financial Statements. Every insurance group must prepare and submit, on an annual basis, audited financial statements prepared under GAAP or IFRS ("Group Financial Statements") and group statutory financial statements. The Group Financial Statements must be audited annually by the group's approved auditor who must prepare an auditor's report in accordance with generally accepted auditing standards. The designated insurer is required to file with the BMA annually the audited Group Financial Statements within five months from the end of the relevant financial year (unless specifically extended). The Group Financial Statements are available for public inspection.

Group Statutory Financial Return and Annual Capital and Solvency Return. Every insurance group is required to prepare an annual group statutory financial return which must be submitted to the BMA by the designated insurer within five months after its financial year end (unless specifically extended). The Group Rules prescribe the rules pertaining to the preparation and substance of the group statutory financial statements (which include, in statutory form, a group balance sheet, a group income statement, a group statement of capital and surplus, and notes thereto). The designated insurer of the group is required to file with the BMA the group statutory financial statements with the BMA within five months from the end of the relevant financial year (unless specifically extended). The statutory financial return shall include, among other items, a report of the approved group auditor, an insurance group business solvency certificate, an insurance group capital and solvency certificate, particulars of ceded reinsurance comprising the top ten unaffiliated reinsurers for which the group has the highest recoverable balances, a list of non-insurance financial regulated entities owned by the group and summary details of all adjustments applied to the group financial statements in the form of a reconciliation of amounts reported as total assets, total liabilities, net income and total statutory capital and surplus.

Every insurance group must also prepare and submit a group capital and solvency return (the "Group Capital and Solvency Return") which comprises the group BSCR model or an approved group internal capital model, along with the returns prescribed in the applicable schedules to the Group Rules. The Group Capital and Solvency Return is submitted by the designated insurer on behalf of the group and must include a declaration signed by two directors of the insurer, one of which may be the chief executive; and either the chief risk officer of the parent company , or the chief financial officer of the parent company

Quarterly Financial Returns. In addition to the annual filings, the designated insurer is required to prepare and file, on behalf of the group, quarterly financial returns no later than the end of the month of each May, August and November for the first, second and third quarters, respectively. The quarterly financial return shall consist of (a) quarterly unaudited (consolidated) group financial statements in respect of its business for each financial statements in respect of its business for each financial quarter, where such statements are the most recent produced by the group, and must not reflect a financial position that exceeds two months and (b) details of material intra-group transactions and risk concentrations, including among other things, details surrounding reinsurance and retrocession arrangements and the ten largest exposures to counterparty and other counterparty exposures exceeding 10% of the insurer's statutory capital and surplus.

Restrictions on Dividends and Distributions. A Class 3B insurer and Class 4 insurer shall not declare or pay any dividend during the financial year if it is in breach of its enhanced capital requirement or its general business solvency margins or its minimum liquidity ratio or if the declaration or payment of such dividends would cause such a breach. If it failed to meet its minimum solvency margins or minimum liquidity ratio on the last day of any financial year, a Class 4 insurer, will be prohibited, without the approval of the BMA, from declaring or paying in any financial year dividends of more than 25% of its total statutory capital and surplus (as shown on its previous financial year's statutory balance sheet) unless it files (at least seven days before payment of such dividends) with the BMA an affidavit stating that it will continue to meet the required margins.

Furthermore, Validus may only declare or pay a dividend, or make a distribution out of contributed surplus as the case may be, if the Company has no reasonable grounds for believing that it is, or would after the payment be, unable to pay its liabilities as they become due, or if the realizable value of its assets would not be less than its liabilities.

Insurance Code of Conduct. The BMA Insurance Code of Conduct establishes duties and standards which must be complied with by all insurers registered under the Insurance Act. The Code is divided into six categories, including:

- Proportionality principle;
- Corporate Governance;
- Risk Management;
- Governance Mechanism;
- Outsourcing; and
- Market Discipline and Disclosure.

Failure to comply with the requirements under the Code will be a factor taken into account by the BMA in determining whether an insurer is conducting its business in a sound and prudent manner as prescribed by the Insurance Act.

Notification of Material Changes. All registered insurers are required to give notice to the BMA of their intention to effect a material change within the meaning of the Insurance Act. For the purposes of the Insurance Act, the following changes are material: (i) the acquisition or transfer of insurance business being part of a scheme falling under section 25 of the Insurance Act or section 99 of the Companies Act 1981; (ii) the amalgamation with or acquisition of another firm; (iii) engaging in non-insurance business and activities related thereto where such business is not ancillary to its insurance business; and (iv) engaging in unrelated business that is retail business. Designated insurers are also required to give notice to the BMA if any member of its group intends to give effect to any material change.

No registered insurer shall take any steps to give effect to a material change, and no designated insurer shall, subject to the immediately following paragraph, permit any member of its group to take steps to give effect to a material change, unless it has first served notice on the BMA that it intends to effect such material change and before the end of 14 days, either the BMA has notified such company in writing that it has no objection to such change or that period has lapsed without the BMA having issued a notice of objection.

A designated insurer shall not be required to serve notice of a material change if the member of the group in question is regulated by a competent authority in an equivalent jurisdiction and has within 90 days of the event filed written notice of the material change with the BMA.

Any insurer who fails to give the required notice or which effects a material change, or allows such material change to be effected, before the prescribed period has elapsed or after having received a notice of objection from the BMA shall be guilty of an offense. A designated insurer that is guilty of an offense shall neither be liable to criminal proceedings nor any penalties but may be subject to directions issued by the BMA.

Securities: Securities may be offered or sold in Bermuda only in compliance with the provisions of the Investment Business Act 2003, and Exchange Control Act 1972, and related regulations of Bermuda which regulate the sale of securities in Bermuda. In addition, specific permission is required from the BMA, pursuant to the provisions of the Exchange Control Act 1972 and related regulations, for all issuances and transfers of securities of Bermuda companies, other than in cases where the BMA has granted a general permission. The BMA, in its policy dated June 1, 2005, provides that where any equity securities, which would include our ordinary shares, of a Bermuda company are listed on an appointed stock exchange (the New York Stock Exchange is deemed to be an appointed stock exchange under Bermuda law), general permission is given for the issue and subsequent transfer of any securities of a company from and/or to a non-resident, for as long as any equity securities of the company remain so listed. The ordinary shares of the Company are listed on the New York Stock Exchange.

Notwithstanding the above general permission, the BMA has granted us permission to, subject to our ordinary or voting shares being listed on an appointed stock exchange, issue, grant, create, sell and transfer any of our shares, stock, bonds, notes (other than promissory notes), debentures, debenture stock, units under a unit trust scheme, shares in an oil royalty, options, warrants, coupons, rights and depository receipts, collectively, the "Securities", to and among persons who are either resident or non-resident of Bermuda for exchange control purposes, whether or not the Securities (excluding, for the avoidance of doubt, our ordinary or voting shares) are listed on an appointed stock exchange.

Shareholder Controller and other Notifications. Under the Insurance Act each shareholder or prospective shareholder will be responsible for notifying the BMA in writing of his becoming a controller, directly or indirectly, of 10%, 20%, 33% or 50% of the Company and/or any of the Company's Bermuda insurance subsidiaries within 45 days of becoming such a controller. The BMA may serve a notice of objection on any controller of the Company or any of the Company's Bermuda insurance subsidiaries if it appears to the BMA that the person is no longer fit and proper to be such a controller. The Company's Bermuda insurance subsidiaries are also required to notify the BMA in writing in the event of any person becoming or ceasing to be a controller or officer, a controller or officer being a managing director, chief executive, director, secretary, chief executive or senior executive or other person in accordance with whose directions or instructions the directors of the Bermuda insurance subsidiaries are accustomed to act, including any person who holds, or is entitled to exercise, 10% or more of the voting shares or voting power or is able to exercise a significant influence over the management of any of the Bermuda insurance subsidiaries.

United States

Talbot operates primarily within the Lloyd's insurance market through Syndicate 1183, and Lloyd's operations are subject to regulation in the United States in addition to being regulated in the United Kingdom, as discussed below. The Lloyd's market is licensed to engage in insurance business in Illinois, Kentucky and the U.S. Virgin Islands and operates as an eligible excess and surplus lines insurer in all states and territories except Kentucky and the U.S. Virgin Islands. Lloyd's is also an accredited reinsurer in all states and territories of the United States. Lloyd's maintains various trust funds in the state of New York to protect its United States business and is therefore subject to regulation by the New York Department of Financial Services, which acts as the domiciliary department for Lloyd's U.S. trust funds. There are deposit trust funds in other states to support Lloyd's reinsurance and excess and surplus lines insurance business.

Talbot is subject to a Closing Agreement between Lloyd's and the U.S. Internal Revenue Service pursuant to which Talbot is subject to U.S. federal income tax to the extent its income is attributable to U.S. agents who have authority to bind Talbot. Specifically, U.S. federal income tax is imposed on 35% of its income attributable to U.S. binding authorities (70% for Illinois or Kentucky business).

We currently conduct our business in a manner such that we expect that Validus Re will not be subject to insurance and/or reinsurance licensing requirements or regulations in the United States. Although we do not currently intend for Validus Re to engage in activities which would require it to comply with insurance and reinsurance licensing requirements in the United States, should we choose to engage in activities that would require Validus Re to become licensed in the United States, we cannot assure you that we will be able to do so or that we will be able to do so in a timely manner. Furthermore, the laws and regulations applicable to direct insurers could indirectly affect us, such as collateral requirements in various U.S. states to enable such insurers to receive credit for reinsurance ceded to us.

In addition, the insurance and reinsurance regulatory framework of Bermuda and the insurance of U.S. risk by companies based in Bermuda and not licensed or authorized in the United States recently has become the subject of increased scrutiny in many jurisdictions, including the United States. We are not able to predict the future impact of changes in the laws and regulation to which we are or may become subject on the Company's financial condition or results of operations.

United Kingdom

The financial services industry in the U.K. is regulated by the Financial Services Authority ("FSA"). The FSA is an independent non-governmental body, given statutory powers by the Financial Services and Markets Act 2000.

Although accountable to treasury ministers and through them to Parliament, it is funded entirely by the firms it regulates. The FSA has wide ranging powers in relation to rule-making, investigation and enforcement to enable it to meet its four statutory objectives, which are summarized as one overall aim: “to promote efficient, orderly and fair markets and to help retail consumers achieve a fair deal.”

In relation to insurance business, the FSA regulates insurers, insurance intermediaries and Lloyd’s itself. The FSA and Lloyd’s have common objectives in ensuring that Lloyd’s market is appropriately regulated and, to minimize duplication, the FSA has agreed arrangements with Lloyd’s for co-operation on supervision and enforcement.

Talbot's underwriting activities are therefore regulated by the FSA as well as being subject to the Lloyd's "franchise". Both FSA and Lloyd's have powers to remove their respective authorization for Talbot to manage Lloyd's syndicates. Lloyd's approves annually Syndicate 1183's business plan and any subsequent material changes, and the amount of capital required to support that plan. Lloyd's may require changes to any business plan presented to it or additional capital to be provided to support the underwriting (known as Funds as Lloyd's).

The U.K. government has set out proposals to replace the current system of financial regulation, which it believes has weaknesses, with a new regulatory framework. The key weakness it identified was that no single institution has the responsibility, authority and tools to monitor the financial system as a whole, and respond accordingly. That power will be given to the Bank of England. The U.K. government intends to create a new Financial Policy Committee ("FPC") within the Bank, which will look at the wider economic and financial risks to the stability of the system.

In addition, the FSA will cease to exist in its current form, and the U.K. government will create two new focused financial regulators:

- A new Prudential Regulation Authority ("PRA") will be responsible for the day-to-day supervision of financial institutions that are subject to significant prudential regulation. It will adopt a more judgment-focused approach to regulation so that business models can be challenged, risks identified and action taken to preserve financial stability.
- A new Financial Conduct Authority ("FCA") will have a strong mandate for promoting confidence and transparency in financial services and to give greater protection for consumers of financial services.

The Financial Services Bill was introduced to Parliament on January 26, 2012 and received Royal Assent in December 2012. "Legal cutover," when the new system will be operational, is expected to be April 2013.

In November 2007 Talbot established Talbot Risk Services Pte Ltd in Singapore to source business in the Far East under the Lloyd's Asia Scheme. The Lloyd's Asia Scheme was established by the Monetary Authority of Singapore to encourage members of Lloyd's to expand insurance activities in Asia.

An EU directive covering the capital adequacy, risk management and regulatory reporting for insurers, known as Solvency II was adopted by the European Parliament in April 2009. A directive, known as Omnibus II, which will amend certain of the Solvency II proposals, including the implementation date, was due to be considered by the European Parliament in 2012. On December 3, 2012, the European Parliament rescheduled the plenary vote of the Omnibus II Directive to June 10 2013. Consequently, the proposed Solvency II insurance directive is now widely expected not to come into force before January 1, 2016 at the earliest. Insurers and reinsurers are undertaking a significant amount of work to ensure that they meet the new requirements and this may divert resources from other operational roles. The Company's implementation plans are well underway, although final Solvency II guidelines have not been fully published.

Switzerland

Our Swiss reinsurance subsidiary, Flagstone Réassurance SA ("Flagstone Suisse"), is a société anonyme headquartered in Martigny, Switzerland.

Regulation and Supervision. The conduct of reinsurance business by a company headquartered in Switzerland requires a license granted by FINMA. In principle, licensing and supervision requirements are imposed on Flagstone Suisse as a standalone legal entity. However, in certain circumstances FINMA may issue a decision to exercise supplementary supervision over a group of companies. FINMA had been the group supervisor of Flagstone Group since July 1, 2011 until December 31, 2012.

Flagstone Suisse obtained its reinsurance license from the Swiss Federal Office of Private Insurance in December 2006. On January 1, 2009, Swiss financial services regulation was reformed institutionally pursuant to the law of June 22, 2007 ("FINMALaw"), creating a single regulator ("FINMA") covering all financial services and integrating the supervision of financial crime, professional audit firms and rating agencies. The function of the Swiss Federal Office of Private Insurance ("FOPI") was replaced by this new single regulator.

In general FINMALaw is an overarching statute applying in as far as there is no contrary provision in the sectoral laws for insurance and reinsurance. Sectoral laws are those laws germane to a particular industry sector such as, for example, insurance, reinsurance and banking. Aside from some inconsequential amendments under FINMALaw unifying cross sectoral issues, the existing sectoral laws governing insurance and reinsurance continue in force, substantially unchanged.

The various legal and regulatory requirements that must be satisfied, are set forth primarily by the three following sets of rules and regulations: the Federal Insurance Supervisory Law (“ISL”); the Federal Private Insurance Supervision Ordinance

(“ISO”); and the FINMA Insurance Supervision Ordinance, as well as by various implementing directives and circulars. In general, the approach is principles based and allows for consideration of a justified application by management in relation to such principles.

Under Swiss rules and regulations, Swiss reinsurance companies are generally subject to many, but not all, of the same provisions that apply to direct insurers, and include the following obligations:

Adequacy of Financial Resources. ISL Article 9 and ISO, sets out the minimum capital requirements and solvency requirements. The minimum capital for a reinsurance firm is CHF 10 million. Firms are also obliged to constitute and maintain an organizational fund. In the case of Flagstone Suisse this was fixed at CHF 10 million by the Swiss Federal Office of Private Insurance prior to commencement of Flagstone Suisse's operations.

In addition Flagstone Suisse must keep adequate disposable and unencumbered capital resources to cover its entire activities. In calculating the solvency margin, account is taken of the risks to which the firm is exposed, the insurance classes involved, the extent of the business, the geographical scope and internationally recognized principles (ISL Article 9). Solvency is determined based on two independent methodologies:

Solvency I: This involves calculating a margin applying defined percentages to a base of the higher of gross annual premium or gross claims for the last three available years and comparing coverage in terms of admissible “own funds” as determined under ISL Article 37.

The Swiss Solvency Test or SST: Under this approach, capital adequacy is given if risk bearing capital exceeds Target Capital. This involves a more sophisticated analysis providing for a market-consistent valuation of all assets and liabilities in the firm with a methodological approach to risk categories (insurance risk, credit risk etc.) subjecting them to scenario stress tests at a basic level in the context of the standard regulatory approach but, where appropriate (for instance mandatory for reinsurance companies), permitting the use of internal models in the overall management of risk, once such models are validated. The validation of internal models is a general process which FINMA has pursued with all regulated firms over the past year and is ongoing.

The SST is very close to the “Solvency II” standard of the European Union. We expect that the Swiss regulation will achieve mutual recognition in other parts of the world. On February 1, 2010, Switzerland was formally recognized as equivalent by the EU committee of supervisors, the Committee of European Insurance and Occupational Pensions Supervisors (“CEIOPS”), firstly as regards the EU Reinsurance Directive of 2005 regulating pure reinsurers and secondly as regards its supervisory regime.

For the SST all assets of Flagstone Suisse are considered. There is no direct constraint on permitted investments since the provisions regarding assets linked to reserves in the ISL do not apply to reinsurance firms. However, the use of derivative instruments is required to be fully considered as part of the risk management processes and limited to reducing investment or insurance risk or to secure investment efficiencies.

Sound Corporate Governance, Risk Management and Internal Control System. In addition to quantitative risk measures, FINMA requires full qualitative governance and control of risk in the firm. This includes requirements as to the ongoing fitness, propriety and competence of the directors and senior management, observance of ethical standards, objective and appropriate remuneration procedures, management of conflicts of interests, the institution of a compliance function, independence and adequate resourcing of control functions (including the responsible actuary, the risk management function and the internal audit function), as well as clear terms of reference and systems of delegation and report throughout.

ISL and ISO each require the appointment of a Responsible Actuary - an independent and properly qualified actuary responsible for ensuring that solvency margins are calculated correctly, proper accounting principles are used, and adequate technical reserves are established and that he report to the Board periodically.

Insurance companies are required to implement documented procedures for risk management and internal control. While FINMA does not require a specific quantitative outcome in relation to operational risk, the firm is expected to undertake proper analysis and to account for it.

Supervisory Process. The supervisory process includes the following requirements:

Annual Reporting: Flagstone Suisse is required to prepare an annual report at the end of each financial year on the solvency margins available, as well as an annual report on the calculation of target capital and on risk bearing capital. Flagstone Suisse files a corporate report incorporating financial statements prepared and audited in accordance with Swiss accounting rules and a supervisory report in the prescribed format. The supervisory report is to be submitted to FINMA by June 30 of each year in electronic form together with the annual report.

Table of Contents

Ad Hoc Notifications: FINMA requires ad hoc notifications of all changes to the firm's scheme of operations which include the following: any changes to company statutes, details of its organizational structure or business activities (including expansion into new jurisdictions; changes involving at least a 10% equity holding or at least 10% of votes in the Company, or where there is a change of control allowing persons to exert a significant influence on the Company's commercial activities; changes in management personnel, including the Responsible Actuary).

In addition, Flagstone Suisse is required to notify changes in levels of control of it (upstream) or by it (downstream) at 10%, 20%, 33% or 50% in terms of capital or voting rights.

There is a general duty to notify FINMA of all matters of which it might want to be advised (FINMALaw Article 29). This includes all solvency material matters, which are specified by circular to include a breach of solvency requirements, fluctuations of 10% or more in terms of assets, technical provisions, or of a significant retrocession contract of the company as well as redemption of any hybrid debt instruments; and any regulatory or criminal investigations brought against the company or the senior management or other significant events.

External Auditor Involvement. Audit firms are subjected to approval and supervision by FINMA and are a significant agent in the supervisory process applying to reinsurance companies (FINMALaw 24 et seq.). Auditors report both to the governing body of the company and to FINMA. They report to the Board on the financial statements of the company and on regulatory shortcomings with a requirement for remediation. Material shortcomings are reported directly to FINMA. A standardized audit report on these topics is prescribed by FINMA Directive. Failure to have an audit conducted in accordance with legal requirements, to fulfill the legal duty of cooperation with auditors or for the auditors to perform their role properly (including whistle blowing or failing to identify regulatory breaches) all attract criminal sanctions.

Intervention and Enforcement by the Regulator. FINMALaw provides for a wider range of supervisory intervention tools than previously provided for under the ISL such as the commencement of formal proceedings, including orders to comply with the law, leading up to withdrawal of license, declarations of unfitness for individuals, disgorgement and the appointment of independent specialists to investigate and implement remediation.

Capital Structure and Dividends. Flagstone Suisse is funded by equity in the form of paid in capital by shares and in share premium. Under Swiss corporate law as modified by insurance supervisory law, a non-life insurance company is obliged to contribute to statutory legal reserves a minimum of 20% of any annual profit up to 50% of statutory capital, being paid in share capital. Flagstone Suisse has been substantially funded by share premium. As of the date of this Annual Report we are advised that, as of 2011, share premium can be distributed to shareholders without being subject to withholding tax. However the distribution of any special dividend to shareholders remain subject to the approval of FINMA which has regard to the maintenance of solvency and the interests of reinsureds and creditors.

Table of Contents

Employment Practices

The following table details our personnel by geographic location as at December 31, 2012:

Location	Validus Re	Talbot	AlphaCat	Corporate	Total	%	
London, England	—	302	—	—	302	48.0	%
Pembroke, Bermuda	65	—	5	50	120	19.0	%
Halifax, Canada	60	—	—	—	60	9.5	%
Hyderabad, India	28	—	—	—	28	4.4	%
Waterloo, Canada	—	—	—	26	26	4.1	%
Republic of Singapore	9	13	—	—	22	3.5	%
New York, United States	—	11	—	9	20	3.2	%
Miami, United States	17	—	—	—	17	2.7	%
Martigny, Switzerland	12	—	—	—	12	1.9	%
Dubai, United Arab Emirates	—	7	—	—	7	1.1	%
Santiago, Chile	6	—	—	—	6	1.0	%
Toronto, Canada	—	—	—	5	5	0.8	%
Luxembourg City, Luxembourg	4	—	—	—	4	0.6	%
Hamburg, Germany	1	—	—	—	1	0.2	%
Total	202	333	5	90	630	100.0	%

Included within the total above are 110 former Flagstone employees. We expect this number to be reduced in 2013. We believe our relations with our employees are excellent.

Available Information

The Company files periodic reports, proxy statements and other information with the SEC. The public may read and copy any materials filed with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains a website that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The SEC's website address is http://www.sec.gov. The Company's common shares are traded on the NYSE with the symbol "VR." Similar information concerning the Company can be reviewed at the office of the NYSE at 20 Broad Street, New York, New York, 10005. The Company's website address is http://www.validusholdings.com. Information contained in this website is not part of this report.

The Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are available free of charge, including through our website, as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC. Copies of the charters for the audit committee, the compensation committee, the corporate governance and nominating committee, the finance committee and the risk committee, as well as the Company's Corporate Governance Guidelines, Code of Business Conduct and Ethics for Directors, Officers and Employees (the "Code"), which applies to all of the Company's Directors, officers and employees, and Code of Ethics for Senior Officers, which applies to the Company's principal executive officer, principal accounting officer and other persons holding a comparable position, are available free of charge on the Company's website at http://www.validusholdings.com or by writing to Investor Relations, Validus Holdings, Ltd., 29 Richmond Road, Pembroke, HM 08, Bermuda. The Company will also post on its website any amendment to the Code and any waiver of the Code granted to any of its directors or executive officers to the extent required by applicable rules.

Table of Contents

Item 1A. Risk Factors

Risks Related to Our Company

Claims on policies written under our short-tail insurance lines that arise from unpredictable and severe catastrophic events could adversely affect our financial condition or results of operations.

Substantially all of our gross premiums written to date are in short-tail lines, many of which have the potential to accumulate, which means we could become liable for a significant amount of losses in a brief period. The short-tail policies we write expose us to claims arising out of unpredictable natural and other catastrophic events, whether arising from natural causes such as hurricanes, windstorms, tsunamis, severe winter weather, earthquakes and floods, or man-made causes such as fires, explosions, acts of terrorism, war or political unrest. Many observers believe that the Atlantic basin is in the active phase of a multi-decade cycle in which conditions in the ocean and atmosphere, including warmer-than-average sea-surface temperatures and low wind shear, enhance hurricane activity. This increase in the number and intensity of tropical storms and hurricanes can span multiple decades (approximately 20 to 30 years). These conditions may translate to a greater potential for hurricanes to make landfall in the U.S. at higher intensities over the next five years. In addition, climate change may be causing changes in global temperatures, which may in the future increase the frequency and severity of natural catastrophes and the losses resulting therefrom. Although the frequency and severity of catastrophes are inherently unpredictable, we use state-of-science understanding of climate change and other climate signals for pricing and risk aggregation.

The extent of losses from catastrophes is a function of both the number and severity of the insured events and the total amount of insured exposure in the areas affected. Increases in the value and concentrations of insured property, the effects of inflation and changes in cyclical weather patterns may increase the severity of claims from natural catastrophic events in the future. Similarly, changes in global political and economic conditions may increase both the frequency and severity of man-made catastrophic events in the future. Claims from catastrophic events could reduce our earnings and cause substantial volatility in our results of operations for any fiscal quarter or year, which could adversely affect our financial condition, possibly to the extent of eliminating our shareholders' equity. Our ability to write new reinsurance policies could also be affected as a result of corresponding reductions in our capital. Underwriting is inherently a matter of judgment, involving important assumptions about matters that are unpredictable and beyond our control, and for which historical experience and probability analysis may not provide sufficient guidance. One or more catastrophic or other events could result in claims that substantially exceed our expectations and which would become due in a short period of time, which could materially adversely affect our financial condition, liquidity or results of operations.

Emerging claim and coverage issues could adversely affect our business.

As industry practices and legal, judicial, social and other environmental conditions change, unexpected and unintended issues related to claims and coverage may emerge. These issues may adversely affect our business by either extending coverage beyond our underwriting intent or by increasing the number or size of claims. In some instances, these changes may not become apparent until sometime after we have issued insurance or reinsurance contracts that are affected by the changes. For example, a (re)insurance contract might limit the amount that can be recovered as a result of flooding. However, if the flood damage was caused by an event that also caused extensive wind damage, the quantification of the two types of damage is often a matter of judgment. Similarly, one geographic zone could be affected by more than one catastrophic event. In this case, the amount recoverable from an insurer or reinsurer may in part be determined by the judgmental allocation of damage between the storms. Given the magnitude of the amounts at stake, these types of issues occasionally necessitate judicial resolution. In addition, our actual losses may vary materially from our current estimate of the loss based on a number of factors, including receipt of additional information from insureds or brokers, the attribution of losses to coverages that had not previously been considered as exposed and inflation in repair costs due to additional demand for labor and materials. As a result, the full extent of liability under an insurance or reinsurance contract may not be known for many years after such contract is issued and a loss occurs. Our exposure to this uncertainty is greater in our longer tail lines (marine and energy liabilities and financial institutions).

We depend on ratings from third party rating agencies. Our financial strength rating could be revised downward, which could affect our standing among brokers and customers, cause our premiums and earnings to decrease and limit our ability to pay dividends on our common shares.

Third-party rating agencies assess and rate the financial strength of insurers and reinsurers based upon criteria established by the rating agencies, which criteria are subject to change. The financial strength ratings assigned by rating agencies to insurance and reinsurance companies represent independent opinions of financial strength and ability to meet policyholder obligations and are not directed toward the protection of investors. Ratings have become an increasingly important factor in establishing the competitive position of insurance and reinsurance companies. Insurers and intermediaries use these ratings as one measure by which to assess the financial strength and quality of insurers and reinsurers. These ratings are often a key factor in the decision by

Table of Contents

an insured or intermediary of whether to place business with a particular insurance or reinsurance provider. These ratings are not an evaluation directed toward the protection of investors or a recommendation to buy, sell or hold our common shares.

If our financial strength rating is reduced from current levels, our competitive position in the reinsurance industry would suffer, and it would be more difficult for us to market our products. A downgrade could result in a significant reduction in the number of reinsurance contracts we write and in a substantial loss of business as our customers and brokers that place such business, move to other competitors with higher financial strength ratings. The substantial majority of reinsurance contracts issued through reinsurance brokers contain provisions permitting the ceding company to cancel such contracts in the event of a downgrade of the reinsurer by A.M. Best below “A-” (Excellent). We cannot predict in advance the extent to which this cancellation right would be exercised, if at all, or what effect any such cancellations would have on our financial condition or future operations, but such effect could be material and adverse. Consequently, substantially all of Validus Re’s business could be affected by a downgrade of our A.M. Best rating below “A-”.

The indenture governing our Junior Subordinated Deferrable Debentures would restrict us from declaring or paying dividends on our common shares if we are downgraded by A.M. Best to a financial strength rating of “B” (Fair) or below or if A.M. Best withdraws its financial strength rating on any of our material insurance subsidiaries. A downgrade of the Company’s A.M. Best financial strength rating below “B++” (Fair) would also constitute an event of default under our credit facilities. Either of these events could, among other things, reduce the Company’s financial flexibility.

If our risk management and loss limitation methods fail to adequately manage exposure to losses from catastrophic events, our financial condition and results of operations could be adversely affected.

We manage exposure to catastrophic losses by analyzing the probability and severity of the occurrence of catastrophic events and the impact of such events on our overall (re)insurance and investment portfolio. We use various tools to analyze and manage the reinsurance exposures assumed from insureds and ceding companies and risks from a catastrophic event that could have an adverse effect on our investment portfolio. VCAPS, a proprietary risk modeling software, enables us to assess the adequacy of reinsurance risk pricing and to monitor the overall exposure to insurance and reinsurance risk in correlated geographic zones. There can be no assurance that the models and assumptions used by the software will accurately predict losses. Further, there can be no assurance that the models are free of defects in the modeling logic or in the software code. In addition, we have not sought copyright or other legal protection for VCAPS.

In addition, much of the information that we enter into the risk modeling software is based on third-party data that may not be reliable, as well as estimates and assumptions that are dependent on many variables, such as assumptions about building material and labor demand surge, storm surge, the expenses of settling claims (known as loss adjustment expenses), insurance-to-value and storm intensity. Accordingly, if the estimates and assumptions that are entered into the proprietary risk model are incorrect, or if the proprietary risk model proves to be an inaccurate forecasting tool, the losses we might incur from an actual catastrophe could be materially higher than its expectation of losses generated from modeled catastrophe scenarios, and its financial condition and results of operations could be adversely affected.

A modeled outcome of net loss from a single event also relies in significant part on the reinsurance and retrocessional arrangements in place, or expected to be in place at the time of the analysis, and may change during the year. Modeled outcomes assume that the reinsurance in place responds as expected with minimal reinsurance failure or dispute. Reinsurance and retrocessional coverage is purchased to protect the inwards exposure in line with our risk appetite, but it is possible for there to be a mismatch or gap in cover which could result in higher than modeled losses. In addition, many parts of the reinsurance program are purchased with limited reinstatements and, therefore, the number of claims or events which may be recovered from second or subsequent events is limited. It should also be noted that renewal dates of the reinsurance and retrocessional program do not necessarily coincide with those of the inwards business written. Where inwards business is not protected by risks attaching reinsurance and retrocessional programs, the programs could expire resulting in an increase in the possible net loss retained and as such, could have a material adverse effect on our financial condition and results of operations.

We also seek to limit loss exposure through loss limitation provisions in its policies, such as limitations on the amount of losses that can be claimed under a policy, limitations or exclusions from coverage and provisions relating to choice of forum, which are intended to assure that its policies are legally interpreted as intended. There can be no assurance that these contractual provisions will be enforceable in the manner expected or that disputes relating to coverage will be resolved in our favor. If the loss limitation provisions in the policies are not enforceable or disputes arise concerning the application of such provisions, the losses we might incur from a catastrophic event could be materially higher than expected and our financial condition and results of operations could be adversely affected.

The insurance and reinsurance business is historically cyclical and we expect to experience periods with excess underwriting capacity and unfavorable premium rates and policy terms and conditions, which could materially adversely affect our financial condition and results of operations.

Table of Contents

The insurance and reinsurance industry has historically been cyclical. Insurers and reinsurers have experienced significant fluctuations in operating results due to competition, frequency of occurrence or severity of catastrophic events, levels of underwriting capacity, underwriting results of primary insurers, general economic conditions and other factors. The supply of insurance and reinsurance is related to prevailing prices, the level of insured losses and the level of industry surplus which, in turn, may fluctuate, including in response to changes in rates of return on investments being earned in the reinsurance industry.

The insurance and reinsurance pricing cycle has historically been a market phenomenon, driven by supply and demand rather than by the actual cost of coverage. The upward phase of a cycle is often triggered when a major event forces insurers and reinsurers to make large claim payments, thereby drawing down capital. This, combined with increased demand for insurance against the risk associated with the event, pushes prices upwards. Over time, insurers' and reinsurers' capital is replenished with the higher revenues. At the same time, new entrants flock to the industry seeking a part of the profitable business. This combination prompts a slide in prices—the downward cycle—until a major insured event restarts the upward phase. As a result, the insurance and reinsurance business has been characterized by periods of intense competition on price and policy terms due to excessive underwriting capacity, which is the percentage of surplus or the dollar amount of exposure that a reinsurer is willing to place at risk, as well as periods when shortages of capacity result in favorable premium rates and policy terms and conditions.

Premium levels may be adversely affected by a number of factors which fluctuate and may contribute to price declines generally in the reinsurance industry. For example, as premium levels for many products increased subsequent to the significant natural catastrophes of 2004 and 2005, the supply of reinsurance increased, either as a result of capital provided by new entrants or by the commitment of additional capital by existing reinsurers. Increases in the supply of insurance and reinsurance may have consequences for the reinsurance industry generally and for us including fewer contracts written, lower premium rates, increased expenses for customer acquisition and retention, and less favorable policy terms and conditions. As a consequence, the Company may experience greater competition on most insurance and reinsurance lines. This could adversely affect the rates we receive for our (re)insurance and our gross premiums written.

The cyclical trends in the industry and the industry's profitability can also be affected significantly by volatile and unpredictable developments, such as natural disasters (such as catastrophic hurricanes, windstorms, tornados, earthquakes and floods), courts granting large awards for certain damages, fluctuations in interest rates, changes in the investment environment that affect market prices of investments and inflationary pressures that may tend to affect the size of losses experienced by insureds and primary insurance companies. We expect to experience the effects of cyclicality, which could materially adversely affect our financial condition and results of operations.

Competition for business in our industry is intense, and if we are unable to compete effectively, we may not be able to retain market share and our business may be materially adversely affected.

The insurance and reinsurance industries are highly competitive. We face intense competition, based upon (among other things) global capacity, product breadth, reputation and experience with respect to particular lines of business, relationships with (re)insurance intermediaries, quality of service, capital and perceived financial strength (including independent rating agencies' ratings), innovation and price. We compete with major global insurance and reinsurance companies and underwriting syndicates, many of which have extensive experience in (re)insurance and may have greater financial, marketing and employee resources available to them than us. Other financial institutions, such as banks and hedge funds, now offer products and services similar to our products and services through alternative capital markets products that are structured to provide protections similar to those provided by reinsurers. These products, such as catastrophe-linked bonds, compete with our products. In the future, underwriting capacity will continue to enter the market from these identified competitors and perhaps other sources. Increased competition could result in fewer submissions and lower rates, which could have an adverse effect on our growth and profitability. If we are unable to compete effectively against these competitors, we may not be able to retain market share.

Insureds have been retaining a greater proportion of their risk portfolios than previously, and industrial and commercial companies have been increasingly relying upon their own subsidiary insurance companies, known as captive insurance companies, self-insurance pools, risk retention groups, mutual insurance companies and other mechanisms for funding their risks, rather than risk transferring insurance. This has also put downward pressure on

insurance premiums.
Consolidation in the (re)insurance industry could adversely affect our business.
We believe that several (re)insurance industry participants are seeking to consolidate. These consolidated entities may try to use their enhanced market power to negotiate price reductions for our products and services and/or obtain a larger market share through increased line sizes. If competitive pressures reduce our prices, we would expect to write less business. As the insurance industry consolidates, competition for customers will become more intense and the importance of acquiring and properly servicing each customer will become greater. We could incur greater expenses relating to customer acquisition and retention, further reducing our operating margins. In addition, insurance companies that merge may be able to spread their risks across a consolidated, larger capital base so that they require less reinsurance. The number of companies offering retrocessional reinsurance may decline.

Table of Contents

Reinsurance intermediaries could also continue to consolidate, potentially adversely impacting our ability to access business and distribute our products. We could also experience more robust competition from larger, better capitalized competitors. Any of the foregoing could adversely affect our business or our results of operations.

If we underestimate our reserve for losses and loss expenses, our financial condition and results of operations could be adversely affected.

Our success depends on our ability to accurately assess the risks associated with the businesses and properties that we insure/reinsure. If unpredictable catastrophic events occur, or if we fail to adequately manage our exposure to losses or fail to adequately estimate our reserve requirements, our actual losses and loss expenses may deviate, perhaps substantially, from our reserve estimates.

We estimate the risks associated with our outstanding obligations, including the risk embedded within our unearned premiums. To do this, we establish reserves for losses and loss expenses (or loss reserves), which are liabilities that we record to reflect the estimated costs of claim payment and the related expenses that we will ultimately be required to pay in respect of premiums written and include case reserves and IBNR reserves. However, under U.S. GAAP, we are not permitted to establish reserves for losses until an event which gives rise to a claim occurs. As a result, only reserves applicable to losses incurred up to the reporting date may be set aside on our financial statements, with no allowance for the provision of loss reserves to account for possible other future losses. Case reserves are reserves established with respect to specific individual reported claims. IBNR reserves are reserves for estimated losses that we have incurred but that have not yet been reported to us.

Our reserve estimates do not represent an exact calculation of liability. Rather, they are estimates of what we expect the ultimate settlement and administration of claims will cost. These estimates are based upon actuarial and statistical projections and on our assessment of currently available data, predictions of future developments and estimates of future trends and other variable factors such as inflation. Establishing an appropriate level for our loss reserve estimates is an inherently uncertain process. It is likely that the ultimate liability will be greater or less than these estimates and that, at times, this variance will be material. Our reserve estimates are regularly refined as experience develops and claims are reported and settled. In addition, as we operate largely through intermediaries, reserving for our business can involve added uncertainty arising from our dependence on information from ceding companies which, in addition to the risk of receiving inaccurate information involves an inherent time lag between reporting information from the primary insurer to us. Additionally, ceding companies employ differing reserving practices which add further uncertainty to the establishment of our reserves. Moreover, these uncertainties are greater for reinsurers like us than for reinsurers with a longer operating history, because we do not yet have an established loss history. The lack of historical information for the Company has necessitated the use of industry loss emergence patterns in deriving IBNR. Loss emergence patterns are development patterns used to project current reported or paid loss amounts to their ultimate settlement value or amount. Further, expected losses and loss ratios are typically developed using vendor and proprietary computer models and these expected loss ratios are a material component in the calculation deriving IBNR. Actual loss ratios will deviate from expected loss ratios and ultimate loss ratios will be greater or less than expected loss ratios. Because of these uncertainties, it is possible that our estimates for reserves at any given time could prove inadequate.

To the extent we determine that actual losses and loss adjustment expenses from events which have occurred exceed our expectations and the loss reserves reflected in our financial statements, we will be required to reflect these changes in the current reporting period. This could cause a sudden and material increase in our liabilities and a reduction in our profitability, including operating losses and reduction of capital, which could materially restrict our ability to write new business and adversely affect our financial condition and results of operations and potentially our A.M. Best rating.

The preparation of our financial statements requires us to make many estimates and judgments, which are even more difficult than those made in a mature company, and which, if inaccurate, could cause volatility in our results.

Our consolidated financial statements have been prepared in accordance with U.S. GAAP. Management believes the item that requires the most subjective and complex estimates is the reserve for losses and loss expenses. Due to the Company’s relatively short operating history, loss experience is limited and reliable evidence of changes in trends of numbers of claims incurred, average settlement amounts, numbers of claims outstanding and average losses per claim will necessarily take many years to develop. Following a major catastrophic event, the possibility of future litigation or legislative change that may affect interpretation of policy terms further increases the degree of uncertainty in the reserving process. The uncertainties inherent in the reserving process, together with the potential for unforeseen developments, including changes in laws and the prevailing interpretation of policy terms, may result in losses and loss expenses materially different than the reserves initially established. Changes to prior year reserves will affect current underwriting results by increasing net income if the prior year reserves prove to be redundant or by decreasing net income if the prior year reserves prove to be insufficient. We expect volatility in results in periods in which significant loss events occur because U.S. GAAP does not permit insurers or reinsurers to reserve for loss events until they have occurred and are expected to give rise to a claim. As a result, we are not allowed to record contingency reserves to account for expected future losses. We anticipate that claims arising from future events will require the establishment of substantial reserves from time to time.

Table of Contents

We rely on key personnel and the loss of their services may adversely affect us. The Bermuda location of our head office may be an impediment to attracting and retaining experienced personnel.

Various aspects of our business depend on the services and skills of key personnel of the Company. We believe there are only a limited number of available qualified executives in the business lines in which we compete. We rely substantially upon the services of Edward J. Noonan, Chairman of our Board of Directors and Chief Executive Officer; Jeffrey D. Sangster, Executive Vice President and Chief Accounting Officer (Incoming Executive Vice President and Chief Financial Officer); John H. Hendrickson, incoming Director of Strategy, Corporate Development and Risk Management; Kean Driscoll, Executive Vice President and Chief Executive Officer of Validus Reinsurance, Ltd.; C.N. Rupert Atkin, Chief Executive Officer of the Talbot Group; Robert F. Kuzloski, Executive Vice President and General Counsel; Andrew E. Kudera, Executive Vice President and Chief Actuary; Lixin Zeng, Executive Vice President and Chief Executive Officer of AlphaCat Managers, Ltd.; Stuart W. Mercer, Executive Vice President and Chief Risk Officer; and Jonathan P. Ritz, Executive Vice President, Chief Operating Officer, among other key employees. The loss of any of their services or the services of other members of our management team or any difficulty in attracting and retaining other talented personnel could impede the further implementation of our business strategy, reduce our revenues and decrease our operational effectiveness. Although we have an employment agreement with each of the above named executives, there is a possibility that these employment agreements may not be enforceable in the event any of these employees leave. The employment agreements for each of the above-named executives provide that the terms of the agreement will continue for a defined period after either party giving notice of termination, and will terminate immediately upon the Company giving notice of termination for cause. We do not currently maintain key man life insurance policies with respect to them or any of our other employees. In addition, changes in employment laws, taxation and remuneration practices within our operating jurisdiction may adversely impact the retention or recruitment of key personnel.

The operating location of our head office and our Validus Re subsidiary may be an impediment to attracting and retaining experienced personnel. Under Bermuda law, non-Bermudians (other than spouses of Bermudians) may not engage in any gainful occupation in Bermuda without an appropriate governmental work permit. Our success may depend in part on the continued services of key employees in Bermuda. A work permit may be granted or renewed upon demonstrating that, after proper public advertisement, no Bermudian (or spouse of a Bermudian or a holder of a permanent resident's certificate or holder of a working resident's certificate) is available who meets the minimum standards reasonably required by the employer. A work permit is issued with an expiry date (up to ten years for senior executives) and no assurances can be given that any work permit will be issued or, if issued, renewed upon the expiration of the relevant term. If work permits are not obtained, or are not renewed, for our principal employees, we would lose their services, which could materially affect our business. Work permits are currently required for 47 of our Bermuda employees, the majority of whom have obtained three- or five-year work permits.

Certain of our directors and officers may have conflicts of interest with us.

Entities affiliated with some of our directors have sponsored or invested in, and may in the future sponsor or invest in, other entities engaged in or intending to engage in insurance and reinsurance underwriting, some of which compete with us. They have also entered into, or may in the future enter into, agreements with companies that compete with us. We have a policy in place applicable to each of our directors and officers which provides for the resolution of potential conflicts of interest. However, we may not be in a position to influence any party's decision to engage in activities that would give rise to a conflict of interest, and they may take actions that are not in our shareholders' best interests.

We may require additional capital or credit in the future, which may not be available or only available on unfavorable terms.

We monitor our capital adequacy on a regular basis. The capital requirements of our business depend on many factors, including our premiums written, loss reserves, investment portfolio composition and risk exposures, as well as satisfying regulatory and rating agency capital requirements. Our ability to underwrite is largely dependent upon the quality of our claims paying and financial strength ratings as evaluated by independent rating agencies. To the extent that our existing capital is insufficient to fund our future operating requirements and/or cover claim losses, we may need to raise additional funds through financings or limit our growth. Any equity or debt financing, if available at all,

may be on terms that are unfavorable to us. In the case of equity financings, dilution to our shareholders could result, and, in any case, such securities may have rights, preferences and privileges that are senior to those of our outstanding securities. In addition, the capital and credit markets have recently been experiencing extreme volatility and disruption. In some cases, the markets have exerted downward pressure on the availability of liquidity and credit capacity for certain issuers. If we are not able to obtain adequate capital, our business, results of operations and financial condition could be adversely affected.
In addition, as an alien insurer and reinsurer (not licensed in the U.S.), we are required to post collateral security with respect to any (re)insurance liabilities that we assume from insureds or ceding insurers domiciled in the U.S. in order for U.S. ceding companies to obtain full statutory and regulatory credit for our reinsurance. Other jurisdictions may have similar collateral requirements. Under applicable statutory provisions, these security arrangements may be in the form of letters of credit, insurance

Table of Contents

or reinsurance trusts maintained by trustees or funds-withheld arrangements where assets are held by the ceding company. We intend to satisfy such statutory requirements by maintaining the trust fund requirements for Talbot's underwriting at Lloyd's and by providing to primary insurers letters of credit issued under our credit facilities. To the extent that we are required to post additional security in the future, we may require additional letter of credit capacity and there can be no assurance that we will be able to obtain such additional capacity or arrange for other types of security on commercially acceptable terms or on terms as favorable as under our current letter of credit facilities. Our inability to provide collateral satisfying the statutory and regulatory guidelines applicable to insureds and primary insurers would have a material adverse effect on our ability to provide (re)insurance to third parties and negatively affect our financial position and results of operations.

Security arrangements may subject our assets to security interests and/or require that a portion of our assets be pledged to, or otherwise held by, third parties. Although the investment income derived from our assets while held in trust typically accrues to our benefit, the investment of these assets is governed by the investment regulations of the state of domicile of the ceding insurer and therefore the investment returns on these assets may not be as high as they otherwise would be.

Loss of business from one or more major brokers could adversely affect us.

We market our insurance and reinsurance on a worldwide basis primarily through brokers, and we depend on a small number of brokers for a large portion of our revenues. For the year ended December 31, 2012, our business was primarily sourced from the following brokers: Marsh & McLennan 29.4%, Aon Benfield Group Ltd. 26.5% and Willis Group Holdings Ltd. 16.1%. These three brokers provided a total of 72.0% of our gross premiums written for the year ended December 31, 2012. Loss of all or a substantial portion of the business provided by one or more of these brokers could adversely affect our business.

We assume a degree of credit risk associated with substantially all of our brokers.

In accordance with industry practice, we frequently pay amounts owed on claims under our policies to brokers and the brokers, in turn, pay these amounts over to the ceding insurers and reinsurers that have reinsured a portion of their liabilities with us. In some jurisdictions, if a broker fails to make such a payment, we might remain liable to the ceding insurer or reinsurer for the deficiency notwithstanding the broker's obligation to make such payment. Conversely, in certain jurisdictions, when the ceding insurer or reinsurer pays premiums for these policies to reinsurance brokers for payment to us, these premiums are considered to have been paid and the ceding insurer or reinsurer will no longer be liable to us for these premiums, whether or not we have actually received them. Consequently, we assume a degree of credit risk associated with substantially all of our brokers.

Our utilization of brokers, managing general agents and other third parties to support our business exposes us to operational and financial risks

Talbot's business at Lloyd's relies upon brokers, managing general agents and other third parties to produce and service a proportion of its operations. In these arrangements, we typically grant the third party the right to bind us to new and renewal policies, subject to underwriting guidelines we provide and other contractual restrictions and obligations. Should these third parties issue policies that contravene these guidelines, restrictions or obligations, we could nonetheless be deemed liable for such policies. Although we would intend to resist claims that exceed or expand on our underwriting intention, it is possible that we would not prevail in such an action, or that our managing general agent would be unable to adequately indemnify us for their contractual breach.

We also rely on managing general agents, third party administrators or other third parties we retain, to collect premiums and to pay valid claims. We could also be exposed to their or their producer's operational risk, including, but not limited to, contract wording errors, technological and staffing deficiencies and inadequate disaster recovery plans. We could also be exposed to potential liabilities relating to the claims practices of the third party administrators we have retained to manage the claims activity on this business. Although we have implemented monitoring and other oversight protocols, we cannot assure you that these measures will be sufficient to mitigate all of these exposures.

Our success depends on our ability to establish and maintain effective operating procedures and internal controls. Failure to detect control issues and any instances of fraud could adversely affect us.

Our success is dependent upon our ability to establish and maintain operating procedures and internal controls (including the timely and successful implementation of information technology systems and programs) to effectively support our business and our regulatory and reporting requirements. We may not be successful in such efforts. Even when implemented, as a result of the inherent limitations in all control systems, no evaluation of controls can provide full assurance that all control issues and instances of fraud, if any, within the Company will be detected.

We may be unable to purchase reinsurance or retrocessional reinsurance in the future, and if we do successfully purchase reinsurance or retrocessional reinsurance, we may be unable to collect on claims submitted under such policies, which could adversely affect our business, financial condition and results of operations.

Table of Contents

We purchase reinsurance and retrocessional reinsurance in order that we may offer insureds and cedants greater capacity, and to mitigate the effect of large and multiple losses on our financial condition. Reinsurance is a transaction whereby an insurer or reinsurer cedes to a reinsurer all or part of the insurance it has written or reinsurance it has assumed. A reinsurer's or retrocessional reinsurer's insolvency or inability or refusal to make timely payments under the terms of its reinsurance agreement with us could have an adverse effect on us because we remain liable to our client. From time to time, market conditions have limited, and in some cases have prevented, insurers and reinsurers from obtaining the types and amounts of reinsurance or retrocessional reinsurance that they consider adequate for their business needs. Accordingly, we may not be able to obtain our desired amounts of reinsurance or retrocessional reinsurance or negotiate terms that we deem appropriate or acceptable or obtain reinsurance or retrocessional reinsurance from entities with satisfactory creditworthiness.

Our investment portfolio may suffer reduced returns or losses which could adversely affect our results of operations and financial condition. Any increase in interest rates or volatility in the fixed income markets could result in significant unrealized losses in the fair value of our investment portfolio which would reduce our net income.

Our operating results depend in part on the performance of our investment portfolio, which currently consists largely of fixed maturity securities, as well as the ability of our investment managers to effectively implement our investment strategy. Our Board of Directors, led by our Finance Committee, oversees our investment strategy, and in consultation with our portfolio advisors, has established investment guidelines. The investment guidelines dictate the portfolio's overall objective, benchmark portfolio, eligible securities, duration, limitations on the use of derivatives and inclusion of foreign securities, diversification requirements and average portfolio rating. Management and the Finance Committee periodically review these guidelines in light of our investment goals and consequently they may change at any time.

The investment return, including net investment income, net realized gains (losses) on investments, net unrealized (losses) gains on investments, on our invested assets was $126.5 million, or 2.0% for the year ended December 31, 2012. While we follow a conservative investment strategy designed to emphasize the preservation of invested assets and to provide sufficient liquidity for the prompt payment of claims, we will nevertheless be subject to market-wide risks including illiquidity and pricing uncertainty and fluctuations, as well as to risks inherent in particular securities. Our investment performance may vary substantially over time, and there can be no assurance that we will achieve our investment objectives. See "Business—Investment Management."

Investment results will also be affected by general economic conditions, market volatility, interest rate fluctuations, liquidity and credit risks beyond our control. In addition, our need for liquidity may result in investment returns below our expectations. Also, with respect to certain of our investments, we are subject to prepayment or reinvestment risk. In particular, our fixed income portfolio is subject to reinvestment risk, and as at December 31, 2012, 21.8% of our fixed income portfolio is comprised of mortgage backed and asset backed securities which are subject to prepayment risk. Although we attempt to manage the risks of investing in a changing interest rate environment, a significant increase in interest rates could result in significant losses, realized or unrealized, in the fair value of our investment portfolio and, consequently, could have an adverse affect on our results of operations.

Investment methodologies and assumptions are subject to differing interpretations and impairments taken on our investments are subjective which could both adversely affect our results of operations and financial condition.

The valuation of our investments may include methodologies, estimations and assumptions that are subject to differing interpretations and could result in changes to our investment valuations. During periods of market disruptions, it may be difficult to value certain securities if trading becomes less frequent or market data less observable. There may also be certain asset classes that become illiquid due to the financial environment. As a result, valuation of securities in our investment portfolio may require more subjectivity and management judgment. Valuation methods that require greater estimation may result in values which may be greater or less than the value at which the investments may be ultimately sold. In addition, rapidly changing and unpredictable credit and equity market conditions could materially affect the valuation of securities as reported in our consolidated financial statements.

The determination of the impairments taken on our investments are also highly subjective and could materially impact our financial position. Impairments vary by investment type and are based upon our periodic evaluations and assessments of known and inherent risks associated with the respective asset class. Evaluations are revised as conditions change, and management reflects impairments in operations on a quarterly basis as such evaluations are revised. Furthermore, additional impairments may need to be taken in the future. Subjective impairments could adversely affect our financial conditions and our results of operations.

Certain of our investments are illiquid and may be difficult to sell, or to sell in significant amounts at acceptable prices, to generate cash to meet our needs

Investments in certain securities in funds attributed to utilizing the equity method, may be illiquid due to contractual provisions or investment market conditions. If we require significant amounts of cash on short notice in excess of anticipated cash obligations, then we may have difficulty selling these investments in a timely manner or we may be forced to sell or terminate them at unfavorable values.

33

Table of Contents

Our operating results may be adversely affected by currency fluctuations.

Our functional currency is the U.S. dollar. Many of our companies maintain both assets and liabilities in local currencies. Therefore, we are exposed to foreign exchange risk on the assets and liabilities denominated in those foreign currencies. Foreign exchange risk is reviewed as part of our risk management process. Locally required capital levels may be invested in home currencies in order to satisfy regulatory requirements and to support local insurance operations. The principal currencies creating foreign exchange risk are the British pound sterling and the Euro. As of December 31, 2012, $1,264.7 million, or 12.6% of our total assets and $1,217.9 million, or 21.9% of our total liabilities were held in foreign currencies. As of December 31, 2012, $152.3 million, or 2.7% of our total net liabilities held in foreign currencies was non-monetary items which do not require revaluation at each reporting date. We look to manage our foreign currency exposure through the use of currency derivatives as well as matching of our major foreign denominated assets and liabilities. However, there is no guarantee that we will effectively mitigate our exposure to foreign exchange losses. Please refer to Part II, Item 7A “Quantitative and Qualitative Disclosures About Market Risk” for further discussion of foreign currency risk.

Heightened European sovereign debt risk could adversely affect our results of operations and financial condition.

Our fixed income portfolio contains certain Eurozone non-U.S. Government and Government Agency securities and Eurozone non-U.S. corporate securities which are subject to increased liquidity risk, interest rate risk and default risk as a result of heightened European sovereign debt risk. As of December 31, 2012, our fixed income portfolio contains $101.4 million or 2.0% of Eurozone Non-U.S. Government securities and $233.6 million or 4.6% of Eurozone non-U.S. corporate securities. Increased defaults, and or a significant increase in interest rates could result in losses, realized or unrealized, in the fair value of our investment portfolio and, consequently, could have an adverse effect on our results of operations.

We are subject to cybersecurity risks and may incur increasing costs in an effort to minimize those risks.

We depend on the proper functioning and availability of our information technology platform, including communications and data processing systems, in operating our business. These systems consist of proprietary software programs that are integral to the efficient operation of our business, including our proprietary pricing and exposure management system. We are also required to effect electronic transmissions with third parties including brokers, clients vendors and others with whom we do business, and to facilitate the oversight conducted by our Board of Directors. Security breaches could expose us to a risk of loss or misuse of our information, litigation and potential liability. In addition, cyber incidents that impact the availability, reliability, speed, accuracy or other proper functioning of these systems could have a significant impact on our operations, and potentially on our results. We may not have the resources or technical sophistication to anticipate or prevent rapidly evolving types of cyber attacks. A significant cyber incident, including system failure, security breach, disruption by malware or other damage could interrupt or delay our operations, result in a violation of applicable privacy and other laws, damage our reputation, cause a loss of customers or give rise to monetary fines and other penalties, which could be significant.

Risks Related to Acquisitions and New Ventures

Any future acquisitions or new ventures may expose us to operational risks.

We may in the future make strategic acquisitions, either of other companies or selected books of business, or grow our business organically. Any future acquisitions or new ventures may expose us to operational challenges and risks, including:

- integrating financial and operational reporting systems;
- integration into new geographical regions;
- establishing satisfactory budgetary and other financial controls;
- funding increased capital needs and overhead expenses;
- obtaining management personnel required for expanded operations;
- obtaining necessary regulatory permissions;
- funding cash flow shortages that may occur if anticipated sales and revenues are not realized or are delayed, whether by general economic or market conditions or unforeseen internal difficulties;
- the value of assets related to acquisitions or new ventures may be lower than expected or may diminish due to credit defaults or changes in interest rates and liabilities assumed may be greater than expected;

- the assets and liabilities related to acquisitions or new ventures may be subject to foreign currency exchange rate fluctuation; and

- financial exposures in the event that the sellers of the entities we acquire are unable or unwilling to meet their indemnification, reinsurance and other obligations to us.

Our failure to manage successfully these operational challenges and risks may adversely impact our results of operations.
We may be exposed to risk in connection with our management of third party capital.
Our operating subsidiaries may owe certain legal duties and obligations to third party investors (including reporting obligations) and are subject to a variety of often complex laws and regulations relating to the management of third party capital. Compliance with some of these laws and regulations requires significant management time and attention. Although we seek to continually monitor our policies and procedures to attempt to ensure compliance, there could be faulty judgments, simple errors or mistakes, or the failure of our personnel to adhere to established policies and procedures which could result in our failure to comply with applicable laws or regulations which could result in significant liabilities, penalties or other losses to the Company, and seriously harm our business and results of operations. In addition to the forgoing, our third party capital providers may redeem their interests in our managed funds, which could materially impact the financial condition of such funds, and could in turn materially impact our financial condition and results of operations. Moreover, we can provide no assurance that we may be able to attract and raise additional third party capital for our existing funds or for potential new funds and therefore we may forego existing and/or potential fee income and other income generating opportunities.
Risks Relating to Lloyd’s and Other U.K. Regulatory Matters
The regulation of Lloyd’s members and of Lloyd’s by the U.K. Financial Services Authority (“FSA”) and under European Directives and other local laws may result in intervention that could have a significant negative impact on Talbot.
Talbot operates in a regulated jurisdiction. Its underwriting activities are regulated by the FSA and franchised by Lloyd’s. The FSA has substantial powers of intervention in relation to the Lloyd’s managing agents (such as Talbot Underwriting Ltd.) which it regulates, including the power to remove their authorization to manage Lloyd’s syndicates. In addition, the Lloyd’s Franchise Board requires annual approval of Syndicate 1183’s business plan, including a maximum underwriting capacity, and may require changes to any business plan presented to it or additional capital to be provided to support underwriting (known as Funds at Lloyd’s or “FAL”). An adverse determination in any of these cases could lead to a change in business strategy which may have an adverse effect on Talbot’s financial condition and operating results.
An EU directive covering the capital adequacy, risk management and regulatory reporting for insurers, known as Solvency II was adopted by the European Parliament in April 2009. A directive, known as Omnibus II, which will amend certain of the Solvency II proposals, including the implementation date, was due to be considered by the European Parliament in 2012. On December 3 2012, the European Parliament rescheduled the plenary vote of the Omnibus II Directive to June 10, 2013. Consequently the proposed Solvency II insurance directive is now widely expected not to come into force before January 1, 2016 at the earliest. Insurers and reinsurers are undertaking a significant amount of work to ensure that they meet the new requirements and this may divert resources from other operational roles. The Company's implementation plans are well underway, although final Solvency II guidelines have not been fully published.
Additionally, Lloyd’s worldwide insurance and reinsurance business is subject to local regulation. Changes in such regulation may have an adverse effect on Lloyd’s generally and on Talbot.
The future structure of U.K. financial regulation
The U.K. government has set out proposals to replace the current system of financial regulation, which it believes has weaknesses, with a new regulatory framework. The key weakness it identified was that no single institution has the responsibility, authority and tools to monitor the financial system as a whole, and respond accordingly. That power will be given to the Bank of England. The U.K. government will create a new Financial Policy Committee (“FPC”) within the Bank, which will look at the wider economic and financial risks to the stability of the system.
In addition, the FSA will cease to exist in its current form, and the Government will create two new focused financial regulators:

- A new Prudential Regulation Authority (“PRA”) will be responsible for the day-to-day supervision of financial institutions that are subject to significant prudential regulation. It will adopt a more judgment-focused approach to regulation so that business models can be challenged, risks identified and action taken to preserve financial stability.

- A new Financial Conduct Authority (“FCA”) will have a strong mandate for promoting confidence and transparency in financial services and to give greater protection for consumers of financial services.

Table of Contents

The Financial Services Bill was introduced to Parliament on January 26, 2012 and received Royal Assent in December 2012. “Legal cutover,” when the new system will be operational, is expected to be April 1, 2013.
Lloyd’s is keeping abreast of these developments and lobbying on behalf of the market when necessary. It is likely that Lloyd’s itself and managing agency businesses will come under the day-to-day supervision of the PRA in due course although Talbot will also have to interact with the FCA. We are unable to determine the impact, if any, the change in U.K. financial regulation will have on Talbot’s financial condition and results of operations.
Should Lloyd’s Council decide additional levies are required to support the central fund, this could adversely affect Talbot.
The central fund, which is funded by annual contributions and loans from Lloyd’s members, acts as a policyholders’ protection fund to make payments where any Lloyd’s member has failed to pay, or is unable to pay, valid claims. The Lloyd’s Council may resolve to make payments from the central fund for the advancement and protection of policyholders, which could lead to additional or special contributions being payable by Lloyd’s members, including Talbot. This, in turn, could adversely affect Talbot and the Company.
Lloyd’s 1992 and prior liabilities.
Lloyd’s currently has a number of contingent liabilities in respect of risks under certain policies allocated to 1992 or prior years of account.
Notwithstanding the “firebreak” introduced when Lloyd’s implemented the Reconstruction and Renewal Plan in 1996, and the phase II completion which was effective June 30, 2009 which, as a result Equitas and relevant policyholders now benefit from $7.0 billion of reinsurance cover provided under this arrangement, Lloyd’s members, including Talbot subsidiaries, remain indirectly exposed in a number of ways to 1992 and prior business then reinsured by Equitas, including through the application of overseas deposits and the central fund.
The statutory transfer of 1992 and prior non-life business from Names to Equitas Insurance Limited, relieved the members and former members concerned from those liabilities under U.K. law and the law of every other state within the EEA, however, if the limit of retrocessional cover from National Indemnity Company in respect of that business proves to be insufficient and as a consequence Equitas is unable to pay the 1992 and prior liabilities in full, Lloyd’s will be liable to meet any shortfall arising in respect of certain policies. The central fund, which Lloyd’s can replenish, subject to its Bye-laws, by issuing calls on current underwriting members of Lloyd’s (which will include Talbot subsidiaries), may be applied for these purposes. Lloyd’s also has contingent liabilities under indemnities in respect of claims against certain persons.
The failure of Lloyd’s to satisfy the FSA’s annual solvency test could result in limitations on managing agents’ ability, including Talbot’s ability to underwrite or to commence legal proceedings against Lloyd’s.
The FSA requires Lloyd’s to satisfy an annual solvency test. The solvency requirement in essence measures whether Lloyd’s has sufficient assets in the aggregate to meet all outstanding liabilities of its members, both current and in run-off. If Lloyd’s fails to satisfy the test in any year, the FSA may require Lloyd’s to cease trading and/or its members to cease or reduce underwriting. In the event of Lloyd’s failing to meet any solvency requirement, either the Society of Lloyd’s or the FSA may apply to the court for a Lloyd’s Market Reorganisation Order (“LMRO”). On the making of an order a “reorganisation controller” is appointed, and for its duration, a moratorium is imposed preventing any proceedings or legal process from being commenced or continued against any party that is the subject of such an order, which, if made, would apply to the market as a whole, including members, former members, managing agents, members’ agents, Lloyd’s brokers, approved run-off companies and managing general agents unless individual parties are specifically excluded.
A downgrade in Lloyd’s ratings would have an adverse effect on Syndicate 1183’s standing among brokers and customers and cause its premiums and earnings to decrease.
The ability of Lloyd’s syndicates to trade in certain classes of business at current levels is dependent on the maintenance of a satisfactory credit rating issued by an accredited rating agency. The financial security of the Lloyd’s market is regularly assessed by three independent rating agencies, A.M. Best, Standard & Poor’s and Fitch Ratings. Syndicate 1183 benefits from Lloyd’s current ratings and would be adversely affected if the current ratings were downgraded from their present levels.

An increase in the charges paid by Talbot to participate in the Lloyd’s market could adversely affect Talbot’s financial and operating results.

Lloyd’s imposes a number of charges on businesses operating in the Lloyd’s market, including, for example, annual subscriptions and central fund contributions for members and policy signing charges. The basis and amounts of charges may be varied by Lloyd’s and could adversely affect Talbot and the Company.

Table of Contents

An increase in the level or type of deposits required by U.S. Situs Trust Deeds to be maintained by Lloyd's syndicates could result in Syndicate 1183 being required to make a cash call which could adversely affect Talbot's financial performance.

The U.S. Situs Trust Deeds require syndicates transacting certain types of business in the United States to maintain minimum deposits as protection for U.S. policyholders. These deposits represent the syndicates' estimates of unpaid claims liabilities (less premiums receivable) relating to this business, adjusted for provisions for potential bad debt on premiums earned but not received and for any anticipated profit on unearned premiums. No credit is generally allowed for potential reinsurance recoveries. The New York Insurance Department and the U.S. National Association of Insurance Commissioners currently require funding of 30% of gross liabilities in relation to insurance business classified as "Surplus Lines." The "Credit for Reinsurance" trust fund is usually required to be funded at 100% of gross liabilities. The funds contained within the deposits are not ordinarily available to meet trading expenses. U.S. regulators may increase the level of funding required or change the requirements as to the nature of funding. Accordingly, in the event of a major claim arising in the United States, for example from a major catastrophe, syndicates participating in such U.S. business may be required to make cash calls on their members to meet claims payments and deposit funding obligations. This could adversely affect Talbot.

Risks Related to Taxation

We may be subject to U.S. tax.

We intend to operate in such a manner that none of our non-U.S. companies would be considered engaged in a U.S. trade or business. No definitive standards, however, are provided by the Internal Revenue Code of 1986, as amended (the "Code"), U.S. Treasury regulations or court decisions regarding activities that constitute the conduct of a U.S. trade or business. Because that determination is essentially factual, we cannot assure that the Internal Revenue Service (the "IRS") will not contend that we are engaged in a U.S. trade or business. If we were found to be so engaged, we could be subject to U.S. corporate income and branch profits tax on our earnings that are effectively connected to such U.S. trade or business.

If the group company involved is entitled to the benefits of a U.S. income tax treaty (the "Treaty"), it would not be subject to U.S. income tax on any income protected by the Treaty unless that income is attributable to a permanent establishment in the U.S. The income tax treaty between the U.S. and Bermuda (the "Bermuda Treaty") clearly applies to premium income, but may be construed as not protecting other income such as investment income. If Validus Re were found to be engaged in a trade or business in the U.S. and were entitled to the benefits of the Bermuda Treaty in general, but the Bermuda Treaty was found not to protect investment income, a portion of Validus Re's investment income could be subject to U.S. tax.

U.S. persons who hold common shares may be subject to U.S. income taxation at ordinary income rates on our undistributed earnings and profits.

Controlled Foreign Corporation Status: The Company should not be a controlled foreign corporation ("CFC") because its organizational documents provide that if the common shares owned, directly, indirectly or by attribution, by any person would otherwise represent more than 9.09% of the aggregate voting power of all the Company's common shares, the voting rights attached to those common shares will be reduced so that such person may not exercise and is not attributed more than 9.09% of the total voting power of the common shares. We cannot assure, however, that the provisions of the Organizational Documents will operate as intended and that the Company will not be considered a CFC. If the Company were considered a CFC, any shareholder that is a U.S. person that owns directly, indirectly or by attribution, 10% or more of the voting power of the Company may be subject to current U.S. income taxation at ordinary income tax rates on all or a portion of the Company's undistributed earnings and profits attributable to Validus Re's insurance and reinsurance income, including underwriting and investment income. Any gain realized on sale of common shares by such shareholder may also be taxed as a dividend to the extent of the Company's earnings and profits attributed to such shares during the period that the shareholder held the shares and while the Company was a CFC (with certain adjustments).

Related Person Insurance Income: If the related person insurance income ("RPII") of any of the Company's non-U.S. insurance subsidiaries were to equal or exceed 20% of that subsidiary's gross insurance income in any taxable year, and U.S. persons were treated as owning 25% or more of the subsidiary's stock, by vote or value, a U.S. person who directly or indirectly owns any common shares on the last day of such taxable year on which the 25% threshold is met would be required to include in income for U.S. federal income tax purposes that person's ratable share of that subsidiary's RPII for the taxable year. The amount to be included in income is determined as if the RPII were distributed proportionately to U.S. shareholders on that date, regardless of whether that income is distributed. The amount of RPII to be included in income is limited by such shareholder's share of the subsidiary's current-year earnings and profits, and possibly reduced by the shareholder's share of prior year deficits in earnings and profits. The amount of RPII earned by a subsidiary will depend on several factors, including the identity of persons directly or indirectly insured or reinsured by that subsidiary. Although we do not believe that the 20% threshold will be met for our non-U.S. insurance subsidiaries, some of the factors that might affect that determination in any period may be beyond our control. Consequently, we cannot assure that we will not exceed the RPII threshold in any taxable year.

Table of Contents

If a U.S. person disposes of shares in a non-U.S. insurance corporation that had RPII (even if the 20% threshold was not met) and the 25% threshold is met at any time during the five-year period ending on the date of disposition, and the U.S. person owned any shares at such time, any gain from the disposition will generally be treated as a dividend to the extent of the holder's share of the corporation's undistributed earnings and profits that were accumulated during the period that the holder owned the shares (possibly whether or not those earnings and profits are attributable to RPII). In addition, the shareholder will be required to comply with specified reporting requirements, regardless of the amount of shares owned. We believe that those rules should not apply to a disposition of common shares because the Company is not itself directly engaged in the insurance business. We cannot assure, however, that the IRS will not successfully assert that those rules apply to a disposition of common shares.

U.S. persons who hold common shares will be subject to adverse tax consequences if the Company is considered a passive foreign investment company for U.S. federal income tax purposes.

If the Company is considered a passive foreign investment company ("PFIC") for U.S. federal income tax purposes, a U.S. holder who owns common shares will be subject to adverse tax consequences, including a greater tax liability than might otherwise apply and an interest charge on certain taxes that are deferred as a result of the Company's non-U.S. status. We currently do not expect that the Company will be a PFIC for U.S. federal income tax purposes in the current taxable year or the foreseeable future because, through Validus Re, Talbot 2002 Underwriting Capital Ltd. and Talbot Underwriting Ltd., it intends to be predominantly engaged in the active conduct of a global insurance and reinsurance business. We cannot assure you, however, that the Company will not be deemed to be a PFIC by the IRS. No regulations currently exist regarding the application of the PFIC provisions to an insurance company.

Changes in U.S. tax laws may be retroactive and could subject a U.S. holder of our common shares to other adverse tax consequences.

The tax treatment of non-U.S. companies and their U.S. and non-U.S. insurance and reinsurance subsidiaries has been the subject of Congressional discussion and legislative proposals in the U.S. We cannot assure that future legislative action will not increase the amount of U.S. tax payable by us.

In addition, the U.S. federal income tax laws and interpretations, including those regarding whether a company is engaged in a U.S. trade or business or is a PFIC, or whether U.S. holders would be required to include "subpart F income" or RPII in their gross income, are subject to change, possibly on a retroactive basis. No regulations regarding the application of the PFIC rules to insurance companies are currently in effect, and the regulations regarding RPII are still in proposed form. New regulations or pronouncements interpreting or clarifying such rules may be forthcoming. We cannot be certain if, when, or in what form, such regulations or pronouncements may be provided, and whether such guidance will have a retroactive effect.

The American Taxpayer Relief Act of 2012

Under previous U.S. law, non-corporate U.S. holders of our common shares generally are taxed on dividends at a capital gains tax rate of 15% rather than ordinary income tax rates. The American Taxpayer Relief Act of 2012 raises the top rate for capital gains and dividends to 20%, up from the maximum 15% rate. That top rate will apply to the extent that a taxpayer's income exceeds the thresholds set for the 39.6% rate ($400,000 for single filers; $450,000 for joint filers and $425,000 for heads of households).

The Obama administration's proposed budget for Fiscal Year 2013 could disallow a deduction for premiums paid for reinsurance.

Insurance companies are generally allowed a deduction for premiums paid for reinsurance. The proposed budget for fiscal year 2013 contains a proposal that denies an insurance company a deduction for premiums and other amounts paid to affiliated foreign companies with respect to reinsurance of property and casualty risks to the extent that the foreign reinsurer (or its parent company) is not subject to U.S. income tax with respect to the premiums received. Furthermore, the proposed law would exclude from the insurance company's income (in the same proportion in which the premium deduction was denied) any return premiums, ceding commissions, reinsurance recovered, or other amounts received with respect to reinsurance policies for which a premium deduction is wholly or partially denied. The current proposal would only apply to policies issued in tax years beginning after December 31, 2012. Based on the information currently available to us, it is uncertain to what extent this legislation will adversely impact us.

We may become subject to taxes in Bermuda after March 31, 2035, which may have a material adverse effect on our results of operations.
Under current Bermuda law, we are not subject to tax on income or capital gains. We have received from the Minister of Finance under The Exempted Undertaking Tax Protection Act 1966, as amended, an assurance that, in the event that Bermuda enacts legislation imposing tax computed on profits, income, any capital asset, gain or appreciation, or any tax in the nature of estate duty or inheritance, then the imposition of any such tax shall not be applicable to us or to any of our operations or shares,

debentures or other obligations, until March 31, 2035. We could be subject to taxes in Bermuda after that date. This assurance is subject to the proviso that it is not to be construed to prevent the application of any tax or duty to such persons as are ordinarily resident in Bermuda or to prevent the application of any tax payable in accordance with the provisions of the Land Tax Act 1967 or otherwise payable in relation to any property leased to us. We and Validus Re each pay annual Bermuda government fees; Validus Re pays annual insurance license fees. In addition, all entities employing individuals in Bermuda are required to pay a payroll tax and there are other sundry taxes payable, directly or indirectly, to the Bermuda government.

Our non-U.K. companies may be subject to U.K. tax.

We intend to operate in such a manner that none of our non-U.K. companies would be resident in the U.K. for tax purposes. A company incorporated outside the U.K. will be resident in the U.K. if its business is centrally managed and controlled from the U.K.. Because the concept of central management and control is not defined in statute but derives from case law and the determination of residence is subjective, the U.K. Inland Revenue might contend successfully that one or more of our companies is resident in the U.K..

Furthermore, we intend to operate in such a manner that none of our non-U.K. companies carry on a trade wholly or partly in the U.K.. Case law has held that whether or not a trade is being carried on is a matter of fact and emphasis is placed on where operations take place from which the profits in substance arise. This judgment is subjective. U.K. Inland Revenue might contend successfully that one or more of our non-U.K. companies, is conducting business in the U.K. For U.K. tax purposes, a non-U.K. tax resident company will only be subject to U.K. corporation tax if it carries on a trade in the U.K. through a U.K. permanent establishment. However, that company will still have an income tax liability in the U.K. if it carries on a trade in the U.K., even absent a permanent establishment, unless that company is treaty-protected.

On July 19, 2011, the U.K. government passed the Finance Act 2011 which reduced the U.K. corporate income tax rate from 27% to 26% (as of April 1, 2011) and provided for a further reduction in the U.K. corporate income tax rate from 26% to 25% (effective April 1, 2012)

On December 6, 2011, the U.K. government released draft legislation for a number of key tax reforms which includes a further reduction in U.K. corporation tax rate to 24% (effective April 1, 2013) and 23% (effective April 1, 2014). The effect of a change in an enacted tax law should be recognized through an adjustment to income from continuing operations in the period that legislation is enacted.

The deferred tax liability for underwriting profit taxable in future periods arises because of a difference in timing, for tax payment purposes, between when Talbot syndicate underwriting income is subject to tax and when corresponding corporate name reinsurance premiums are allowable for tax. Under previous U.K. tax legislation, syndicate underwriting income for a particular underwriting year of account is taxed in the year the syndicate closes. However the corresponding corporate name reinsurance premiums are allowable for tax as they are accounted for on an accruals basis. On December 6, 2011, HM Revenue & Customs announced that this timing difference will be eliminated by legislating that the corporate name reinsurance premiums will only allowable for tax in the same period that the syndicate underwriting income for the corresponding underwriting year of account is subject to tax. This change only applies to the 2012 and future underwriting years of account. Therefore, it is expected that the deferred tax liability will be eliminated in future accounting periods as a result of this change.

Our non-Swiss companies may be subject to taxation in Switzerland.

None of our newly acquired companies, except for Flagstone Reassurance Suisse SA and Flagstone Management S.A. are incorporated or managed in Switzerland. Accordingly, none of our other companies should be liable for Swiss corporation taxation unless it carries on business through a permanent establishment in Switzerland. From a Swiss tax perspective, a permanent establishment is a fixed place of business through which a company performs business activities that are considered as being quantitatively and qualitatively significant by the tax authorities, and may include a branch, office, agency or place of management. As of the date of this Annual Report, each of our companies intends to operate in such a manner so that none of our companies, apart from Flagstone Suisse and Flagstone Management S.A., will carry on business through a permanent establishment in Switzerland. If any of our companies were to be treated as carrying on business in Switzerland through a branch or agency or of having a permanent establishment in Switzerland, our results of operations could be adversely affected.

We may be subject to taxation in Luxembourg.

Flagstone Reinsurance (Luxembourg) SARL, Flagstone Finance S.A. and Flagstone Capital Management Luxembourg SICAF are incorporated and carry on business in Luxembourg. However, none of our other companies should be subject to taxation in Luxembourg. If any of our companies were to be treated as carrying on business in Luxembourg through a branch or agency or having a permanent establishment in Luxembourg, our results of operations could be adversely affected.

Table of Contents

We may be subject to taxation in India.

None of our companies, except for Flagstone Underwriting Support Services (India) Pvt Ltd, should be treated as being resident in India for corporate tax purposes. Accordingly, none of our other companies should be liable for corporate tax in India unless it receives or is deemed to receive income, from whatever source derived, in India or it has income that arises or accrues (or is deemed to arise or accrue) in India. As of the date of this Annual Report, each of our companies intends to operate in such a manner so that none of our companies, apart from Flagstone Underwriting Support Services (India) Pvt Ltd, receives or is deemed to receive income in India or has income that arises or accrues in India for purposes of corporate tax in India. If any of our companies were to be treated as receiving income in India or earning income that arises or accrues in India, our results of operations could be affected adversely.

Risks Related to Laws and Regulations Applicable to Us

If we become subject to insurance statutes and regulations in addition to the statutes and regulations that currently apply to us, there could be a significant and negative impact on our business.

We currently conduct our business in a manner such that we expect the Company will not be subject to insurance and/or reinsurance licensing requirements or regulations in any jurisdiction other than Bermuda, in limited circumstances, the United States, and, with respect to Talbot, the U.K. and jurisdictions to which Lloyd’s is subject. See “Business—Regulation—United States and Bermuda.” Although we do not currently intend to engage in activities which would require us to comply with insurance and reinsurance licensing requirements of other jurisdictions, should we choose to engage in activities that would require us to become licensed in such jurisdictions, we cannot assure that we will be able to do so or that we will be able to do so in a timely manner. Furthermore, the laws and regulations applicable to direct insurers could indirectly affect us, such as collateral requirements in various U.S. states to enable such insurers to receive credit for reinsurance ceded to us.

The insurance and reinsurance regulatory framework of Bermuda and the insurance of U.S. risk by companies based in Bermuda that are not licensed or authorized in the U.S. have recently become subject to increased scrutiny in many jurisdictions, including the United States. In the past, there have been U.S. Congressional and other initiatives in the United States regarding increased supervision and regulation of the insurance industry, including proposals to supervise and regulate offshore reinsurers. Government regulators are generally concerned with the protection of policyholders rather than other constituencies, such as our shareholders. We are not able to predict the future impact on our operations of changes in the laws and regulations to which we are or may become subject.

Risks Related to Ownership of Our Common Shares

Because we are a holding company and substantially all of our operations are conducted by our main operating subsidiaries, Validus Re and Talbot, our ability to meet any ongoing cash requirements and to pay dividends will depend on our ability to obtain cash dividends or other cash payments or obtain loans from Validus Re and Talbot.

We conduct substantially all of our operations through subsidiaries. Our ability to meet our ongoing cash requirements, including any debt service payments or other expenses, and pay dividends on our common shares in the future, will depend on our ability to obtain cash dividends or other cash payments or obtain loans from these subsidiaries and as a result will depend on the financial condition of these subsidiaries. The inability of these subsidiaries to pay dividends in an amount sufficient to enable us to meet our cash requirements could have a material adverse effect on us and the value of our common shares. Each of these subsidiaries is a separate and distinct legal entity that has no obligation to pay any dividends or to lend or advance us funds and may be restricted from doing so by contract, including other financing arrangements, charter provisions or applicable legal and regulatory requirements or rating agency constraints. The payment of dividends by these subsidiaries to us is limited under Bermuda law and regulations. The Insurance Act provides that our Bermuda subsidiaries may not declare or pay in any financial year dividends of more than 25% of its total statutory capital and surplus (as shown on its statutory balance sheet in relation to the previous financial year) unless it files an affidavit with the BMA at least seven days prior to the payment signed by at least two directors and such subsidiary’s principal representative, stating that in their opinion such subsidiaries will continue to satisfy the required margins following declaration of those dividends, though there is no additional requirement for BMA approval. In addition, before reducing its total statutory capital by 15% or more (as set out in its previous years' statutory financial statements) each of these subsidiaries must make application to the BMA for permission to do so, such application to consist of an affidavit signed by at least two directors and such subsidiary's principal representative stating that in their opinion the proposed reduction in capital will not cause such subsidiaries to fail to meet its relevant margins, and such other information as the BMA may require. The amounts that are unrestricted net assets and which are available from the Company's subsidiaries for distribution as dividend payments to Validus Holdings, Ltd. without approval of the BMA for Validus Re, Validus Re Americas, Ltd., Talbot Insurance (Bermuda) Ltd. ("TIBL"), AlphaCat Reinsurance, Ltd., PaCRe, Ltd., Flagstone Reassurance Suisse SA (Bermuda Branch) and Mont Fort Re Ltd. were $826.2 million, $nil, $467.3 million, $0.0 million, $nil, $349.4 million and $0.1 million respectively.

The timing and amount of any cash dividends on our common shares are at the discretion of our Board of Directors and will depend upon our results of operations and cash flows, our financial position and capital requirements, general business conditions, legal, tax, regulatory, rating agency and contractual constraints or restrictions and any other factors that our Board of Directors deems relevant. In addition, the indenture governing our Junior Subordinated Deferrable Debentures would restrict us from declaring or paying dividends on our common shares if we are downgraded by A.M. Best to a financial strength rating of “B” (Fair) or below or if A.M. Best withdraws its financial strength rating on any of our material insurance subsidiaries.

Future sales of our common shares and grants of restricted shares may affect the market price of our common shares and the future exercise of options and warrants may result in immediate and substantial dilution of the common shares.

As of February 13, 2013 (but without giving effect to unvested restricted shares), we had 107,468,544 common shares outstanding and 6,410,472 shares issuable upon exercise of outstanding warrants. Approximately 7,875,859 of these outstanding shares were subject to the volume limitations and other conditions of Rule 144 under the Securities Act of 1933, as amended, which we refer to as the “Securities Act.” Furthermore, certain of our sponsoring shareholders and their transferees have the right to require us to register these common shares under the Securities Act for sale to the public, either in an independent offering pursuant to a demand registration or in conjunction with a public offering, subject to a “lock-up” agreement of no more than 90 days. Following any registration of this type, the common shares to which the registration relates will be freely transferable. In addition, we have filed one or more registration statements on Form S-8 under the Securities Act to register common shares issued or reserved for issuance under our 2005 Long Term Incentive Plan (the “Plan”). The number of common shares that have been reserved for issuance under the Plan is equal to 13,126,896 of which 3,128,443 shares remain available as of December 31, 2012. We cannot predict what effect, if any, future sales of our common shares, or the availability of common shares for future sale, will have on the market price of our common shares. Sales of substantial amounts of our common shares in the public market, or the perception that sales of this type could occur, could depress the market price of our common shares and may make it more difficult for our shareholders to sell their common shares at a time and price that they deem appropriate.

Our Bye-laws authorize our Board of Directors to issue one or more series of common shares and preferred shares without stockholder approval. Specifically, we have an authorized share capital of 571,428,571 shares ($0.175 par value per share), which can consist of common shares and/or preference shares, as determined by our Board of Directors. The Board of Directors has the right to issue the remaining shares without obtaining any approval from our stockholders and to fix the rights, preferences, privileges and restrictions thereof, including dividend rights, conversion rights, voting rights, terms of redemption, liquidation preferences and the number of shares constituting any series or designation of such series. Any issuance of our preferred stock could adversely affect the voting power of the holders of our common shares and could have the effect of delaying, deferring, or preventing the payment of any dividends (including any liquidating dividends) and any change in control of us. If a significant number of either common or preferred shares are issued, it may cause the market price of our common shares to decline.

Our classified board structure may prevent a change in our control.

Our board of directors is divided into three classes of directors. Each year one class of directors is elected by the shareholders for a three year term. The staggered terms of our directors may reduce the possibility of a tender offer or an attempt at a change in control, even though a tender offer or change in control might be in the best interest of our shareholders.

There are provisions in our Bye-laws that reduce the voting rights of voting common shares that are held by a person or group to the extent that such person or group holds more than 9.09% of the aggregate voting power of all common shares entitled to vote on a matter.

In general, and except as provided below, shareholders have one vote for each voting common share held by them and are entitled to vote at all meetings of shareholders. However, if, and for so long as, the common shares of a shareholder, including any votes conferred by “controlled shares” (as defined below), would otherwise represent more than 9.09% of the aggregate voting power of all common shares entitled to vote on a matter, including an election of directors, the votes conferred by such shares will be reduced by whatever amount is necessary such that, after giving effect to any such reduction (and any other reductions in voting power required by our Bye-laws), the votes conferred by such shares represent 9.09% of the aggregate voting power of all common shares entitled to vote on such matter. “Controlled shares” include, among other things, all shares that a person is deemed to own directly, indirectly or constructively (within the meaning of Section 958 of the Code, or Section 13(d)(3) of the Securities and Exchange Act of 1934, as amended (the “Exchange Act”)). At December 31, 2012, there were 109,365,642 voting common shares, of which 9,941,336 voting common shares would confer votes that represent 9.09% of the aggregate voting power of all common shares entitled to vote generally at an election of directors. An investor who does not hold, and is not deemed under the provisions of our Bye-laws to own, any of our common shares may therefore purchase up to such amount without being subject to voting cutback provisions in our Bye-laws.

In addition, we have the authority under our Bye-laws to request information from any shareholder for the purpose of determining ownership of controlled shares by such shareholder.

Table of Contents

There are regulatory limitations on the ownership and transfer of our common shares which could result in the delay or denial of any transfers shareholders might seek to make.

The BMA must approve all issuances and transfers of securities of a Bermuda exempt company. We have received permission from the BMA to issue our common shares, and for the free transferability of our common shares as long as the common shares are listed on the New York Stock Exchange or other appointed exchange, to and among persons who are residents and non-residents of Bermuda for exchange control purposes. Any other transfers remain subject to approval by the BMA and such approval may be denied or delayed.

A shareholder of our company may have greater difficulties in protecting its interests than as a shareholder of a U.S. corporation.

The Companies Act 1981 (the "Companies Act"), which applies to us, differs in material respects from laws generally applicable to U.S. corporations and their shareholders. Taken together with the provisions of our Bye-laws, some of these differences may result in a shareholder having greater difficulties in protecting its interests as a shareholder of our company than it would have as a shareholder of a U.S. corporation. This affects, among other things, the circumstances under which transactions involving an interested director are voidable, whether an interested director can be held accountable for any benefit realized in a transaction with our company, what approvals are required for business combinations by our company with a large shareholder or a wholly owned subsidiary, what rights a shareholder may have as a shareholder to enforce specified provisions of the Companies Act or our Bye-laws, and the circumstances under which we may indemnify our directors and officers.

We are a Bermuda company and it may be difficult for our shareholders to enforce judgments against us or against our directors and executive officers.

We were incorporated under the laws of Bermuda and our business is based in Bermuda. In addition, certain of our directors and officers reside outside the United States, and a portion of our assets and the assets of such persons may be located in jurisdictions outside the United States. As such, it may be difficult or impossible to effect service of process within the United States upon us or those persons, or to recover against us or them on judgments of U.S. courts, including judgments predicated upon the civil liability provisions of the U.S. federal securities laws. Further, no claim may be brought in Bermuda against us or our directors and officers in the first instance for violation of U.S. federal securities laws because these laws have no extraterritorial application under Bermuda law and do not have force of law in Bermuda; however, a Bermuda court may impose civil liability, including the possibility of monetary damages, on us or our directors and officers if the facts alleged in a complaint constitute or give rise to a cause of action under Bermuda law. Currently, of our executive officers, Joseph E. (Jeff) Consolino, C. Jerome Dill, Jeffrey Sangster, Robert Kuzloski and Lixin Zeng reside in Bermuda, Edward Noonan, Stuart Mercer and Jonathan Ritz maintain residences in both Bermuda and the United States and Rupert Atkin resides in the United Kingdom. Of our directors, Edward Noonan maintains residences in both Bermuda and the United States, Jean-Marie Nessi resides in France, Michael Carpenter resides in the United Kingdom and the remainder reside in the United States.

We have been advised by Bermuda counsel, that there is doubt as to whether the courts of Bermuda would enforce judgments of U.S. courts obtained in actions against us or our directors and officers, as well as the experts named herein, predicated upon the civil liability provisions of the U.S. federal securities laws, or original actions brought in Bermuda against us or such persons predicated solely upon U.S. federal securities laws. Further, we have been advised by Bermuda counsel that there is no treaty in effect between the United States and Bermuda providing for the enforcement of judgments of U.S. courts in civil and commercial matters, and there are grounds upon which Bermuda courts may decline to enforce the judgments of U.S. courts. Some remedies available under the laws of U.S. jurisdictions, including some remedies available under the U.S. federal securities laws, may not be allowed in Bermuda courts as contrary to public policy in Bermuda. Because judgments of U.S. courts are not automatically enforceable in Bermuda, it may be difficult for our shareholders to recover against us based upon such judgments.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Company and its subsidiaries currently occupy office space as described below. As a result of the Flagstone acquisition, we own office space and buildings in Hyderabad, India, Martigny, Switzerland and Luxembourg. We believe our current facilities and the leaseholds with respect thereto are sufficient for us to conduct our operations.

Table of Contents

Legal entity	Location	Expiration date
Validus Holdings, Ltd. and Validus Reinsurance, Ltd.	Pembroke, Bermuda	December 31, 2021
Validus Reinsurance, Ltd.	Hamburg, Germany	January 1, 2014
Validus Research Inc.	Waterloo, Canada	March 31, 2015
Validus Research Inc.	Toronto, Canada	March 31, 2013
Validus Reaseguros, Inc.	Miami, Florida, USA	April 1, 2018
Validus Services, Inc.	New York, New York, USA	November 8, 2015
Talbot Underwriting Services (U.S.) Ltd.	New York, New York, USA	November 8, 2015
Validus Re Americas (New Jersey), Inc.	Princeton, New Jersey, USA	June 30, 2022
Talbot Holdings Ltd. and Talbot Underwriting Services Ltd.	London, England	June 22, 2024
Validus Reinsurance, Ltd.	Republic of Singapore	August 31, 2013
Talbot Risk Services PTE Ltd.	Republic of Singapore	December 31, 2015
Talbot Underwriting Services (MENA) Ltd.	Dubai, United Arab Emirates	January 31, 2014
Validus Re Chile S.A.	Santiago, Chile	May 1, 2014
Flagstone Management Services (Halifax)	Halifax, Canada	July 31, 2014
Flagstone Bermuda Holdings	Hamilton, Bermuda	June 1, 2016
Flagstone Reinsurance (Africa)	South Africa	August 31, 2014
Flagstone Reinsurance Holdings Limited	Hamilton, Bermuda	September 30, 2015

Item 3. Legal Proceedings

Similar to the rest of the insurance and reinsurance industry, we are subject to litigation and arbitration in the ordinary course of business.

Executive Officers of the Company

The following table provides information regarding our executive officers and key employees as of February 15, 2013:

Name	Age	Position
Edward J. Noonan	54	Chairman of the Board of Directors and Chief Executive Officer of the Validus Group
Joseph E. (Jeff) Consolino	46	Director, President and Chief Financial Officer
Jeffrey D. Sangster	40	Executive Vice President and Chief Accounting Officer
C.N. Rupert Atkin	54	Chief Executive Officer of the Talbot Group
Kean D. Driscoll	39	Executive Vice President and Chief Executive Officer of Validus Reinsurance, Ltd.
Andrew E. Kudera	53	Executive Vice President and Chief Actuary
Robert F. Kuzloski	49	Executive Vice President and General Counsel
Stuart W. Mercer	53	Executive Vice President and Chief Risk Officer
Jonathan P. Ritz	45	Executive Vice President and Chief Operating Officer
Lixin Zeng	44	Executive Vice President and Chief Executive Officer of AlphaCat Managers, Ltd. and Validus Research Inc.

Edward J. Noonan has been Chairman of our Board and the Chief Executive Officer of the Company since its formation. Mr. Noonan has 30 years of experience in the insurance and reinsurance industry, serving most recently as the acting Chief Executive Officer of Global Indemnity plc (Nasdaq: GBLI) from February 2005 through October 2005 and as a member of the Board of Directors from December 2003 to May 2007. Mr. Noonan served as President and Chief Executive Officer of American Re-Insurance Company from 1997 to 2002, having joined American Re in 1983. Mr. Noonan also served as Chairman of Inter-Ocean

Table of Contents

Reinsurance Holdings of Hamilton, Bermuda from 1997 to 2002. Mr. Noonan is also a Director of Central Mutual Insurance Company and All American Insurance Company, both of which are property and casualty companies based in Ohio.

Joseph E. (Jeff) Consolino was appointed a director of the Company on October 31, 2012 and is currently President and Chief Financial Officer of the Company, a position that he has held since November 2010 and March 2006, respectively. Mr. Consolino has over 18 years of experience in the financial services industry, specifically in providing investment banking services to the insurance industry, and most recently served as a managing director in Merrill Lynch’s Financial Institutions Group specializing in insurance company advisory and financing transactions. He serves as a Director of American Financial Group and of National Interstate Corporation, Ohio based insurance companies, and of AmWINS Group, Inc., a wholesale insurance broker based in North Carolina. Mr. Consolino will be stepping down as President and Chief Financial Officer of the Company effective as of end of day February 15, 2013.

Jeffrey D. Sangster joined the Company in October 2006 and has served in various finance positions during that time, including Executive Vice President and Chief Accounting Officer as well as Chief Financial Officer of Validus Reinsurance, Ltd. and will be appointed as Executive Vice President and Chief Financial Officer of Validus Holdings, Ltd., effective February 16, 2013. Mr. Sangster has served as Executive Vice President and Chief Accounting Officer of the Company since May 2012. Mr. Sangster is a member of the Institute of Chartered Accountants in Bermuda and the Institute of Chartered Accountants in Manitoba.

C. N. Rupert Atkin began his career at the Alexander Howden Group in 1980 before moving to Catlin Underwriting Agencies in 1984. After six years at Catlin he left to join Talbot, then Venton Underwriting Ltd to start Syndicate 1183 as Active Underwriter. In November 2001, Mr. Atkin was made Director of Underwriting. Following the sale of Talbot to Validus in the summer of 2007 Mr. Atkin was appointed as Chief Executive Officer of Talbot. Mr. Atkin has served or is still serving on a variety of market bodies including chairing the Lloyd's Underwriters' Association and Joint War Risk Committee and being a member of the Lloyd's Insurance Services Board, Lloyd's Regulatory Board, Lloyd's Professional Standards Committee and Lloyd's Charities Trust Committee. Mr. Atkin was appointed to the Council of Lloyd's in 2007 and appointed as the Chairman of the Lloyd's Market Association in 2012.

Kean D. Driscoll is the Chief Executive Officer of Validus Reinsurance, Ltd., the reinsurance segment for the Validus Group. He was a founding member of the Company, and previously served as Chief Underwriting Officer. Mr. Driscoll has 17 years of experience as a reinsurance underwriter, and was previously with Quanta Re, and Zurich Re N.A. (Converium). Mr. Driscoll holds a B.A. in Literature from Colgate University, and an M.B.A. from Columbia University, where he graduated with Honors.

Andrew E. Kudera has served as Chief Actuary of the Company since January 2010. Previously, Mr. Kudera operated an independent actuarial consulting firm which served as corporate actuary and loss reserve specialist for Validus Re from its inception through to the end of 2008. Prior to establishing his own consulting firm, Mr. Kudera was the Chief Reserving Actuary for Endurance Specialty Holdings Ltd., a large international insurance and reinsurance company. Mr. Kudera has over 30 years of actuarial and financial management experience in the insurance industry, primarily in a consulting capacity. Mr. Kudera is a Fellow of the Casualty Actuarial Society, a Member of the American Academy of Actuaries, an Associate of the Society of Actuaries, and a Fellow of the Canadian Institute of Actuaries.

Robert F. Kuzloski joined the company in January 2009 and served as Executive Vice President and Chief Corporate Legal Officer of the Company until August of 2012 when he was appointed Executive Vice President and General Counsel of the Company. Prior to joining the Company in January of 2009, Mr. Kuzloski served as Senior Vice President and Assistant General Counsel of XL Capital Ltd. Prior to that, Mr. Kuzloski worked as an attorney at the law firm of Cahill Gordon & Reindel LLP where he specialized in general corporate and securities law, mergers and acquisitions and corporate finance.

Stuart W. Mercer has been Executive Vice President of the Company since its formation. Mr. Mercer has over 20 years of experience in the financial industry focusing on structured derivatives, energy finance and reinsurance. Previously, Mr. Mercer was a senior advisor to DTE Energy Trading.

Jonathan P. Ritz serves as Executive Vice President and Chief Operating Officer of the Company. Mr. Ritz has over 20 years of experience in the (re)insurance and brokerage industries. Most recently, Mr. Ritz served as Chief Operating Officer of IFG Companies-Burlington Insurance Group. Prior to IFG, Mr. Ritz served as Chief Operating Officer of the specialty lines division of ICAT Holdings LLC. From 2007 to 2008, Mr. Ritz was a Managing Director at Guy Carpenter and from 1997 to 2007 he held various positions with United America Insurance Group including Chief Operating Officer and Senior Vice President of ceded reinsurance.

Lixin Zeng, Ph.D., CFA serves as Executive Vice President and Chief Executive Officer of AlphaCat Managers, Ltd. and has played a key role in AlphaCat since its formation in 2008. Prior to this role, he was Executive Risk Officer of Validus Reinsurance, Ltd., responsible for developing and executing the catastrophe risk strategy of the entire Validus Group. Mr. Zeng was one of the original eight employees at the founding of the Company in 2005. His prior positions include: Chief Catastrophe Risk Officer at

Table of Contents

the ACE Group from 2004 to 2005, Head of Development at Willis Re Inc. from 2001 to 2004, Analyst at EW Blanch Co. from 1998 to 2001 and Research Scientist at Arkwright Mutual Insurance Co from 1996 to 1998. Mr. Zeng has expertise in insurance portfolio optimization and risk management and has published multiple articles in professional journals on related topics. He has a Ph.D. in atmospheric sciences from the University of Washington where he graduated in 1996. He received a B.S. in Meteorology from Beijing University, graduating in 1990 and is a CFA charterholder.

Item 4. Mine Safety Disclosure—Not Applicable

Table of Contents

PART II

All amounts presented in this part are in U.S. dollars except as otherwise noted.

Item 5. Market for Registrants, Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities

The Company's common shares, $0.175 par value per share, are listed on the New York Stock Exchange under the symbol "VR."

The following tables sets forth the high and low sales prices per share, as reported on the New York Stock Exchange Composite Tape, of the Company's common shares per fiscal quarter for the two most recent fiscal years.

	High	Low
2012:		
1st Quarter	$32.51	$29.97
2nd Quarter	$33.25	$30.41
3rd Quarter	$34.91	$31.62
4th Quarter	$37.63	$33.11

	High	Low
2011:		
1st Quarter	$33.72	$28.86
2nd Quarter	$34.95	$29.44
3rd Quarter	$31.35	$23.24
4th Quarter	$31.77	$23.87

There were approximately 45 record holders of our common shares as of December 31, 2012. This figure does not represent the actual number of beneficial owners of our common shares because such shares are frequently held in "street name" by securities dealers and others for the benefit of individual owners who may vote the shares.

Table of Contents

Performance Graph

Set forth below is a line graph comparing the percentage change in the cumulative total shareholder return, assuming the reinvestment of dividends, over the period from the Company's IPO on July 25, 2007, through December 31, 2012 as compared to the cumulative total return of the S&P 500 Stock Index and the cumulative total return of an index of the Company's peer group. The peer group index is comprised of the following companies*: Allied World Assurance Company Holdings, Ltd., Alterra Capital Holdings Limited, Arch Capital Group, Ltd., Argo Group International Holdings, Ltd., Aspen Insurance Holdings Limited, AXIS Capital Holdings Limited, Endurance Specialty Holdings Ltd., Everest Re Group, Ltd., Montpelier Re Holdings Ltd., PartnerRe Ltd., Platinum Underwriters Holdings Ltd., and RenaissanceRe Holdings Ltd.

Dividend Policy

On February 6, 2013, the Company announced that its Board of Directors had increased the Company's annual dividend by 20% from $1.00 to $1.20 per common share and per common share equivalent. The first quarterly cash dividend of $0.30 per common share and $0.30 per common share equivalent is payable on March 29, 2013 to holders of record on March 15, 2013. In addition, the Company announced a special dividend in the amount of $2.00 per common share and $2.00 per common share equivalent for which each outstanding warrant is exercisable, payable on February 26, 2013 to shareholders and warrant holders of record as of February 19, 2013.

We are a holding company and have no direct operations. Our ability to pay dividends depends, in part, on the ability of Validus Re and Talbot to pay dividends to us. As a holding company, Validus Holdings, Ltd.'s principal source of income is dividends or other sources of permitted payments from its subsidiaries. These funds provide the cash flow required for dividend payments to the Company's shareholders. The amount of retained earnings that is unrestricted for the payment of dividends by Validus Holdings, Ltd., to its shareholders was $1,643.0 million as at December 31, 2012. The Bermuda Companies Act 1981 (the "Companies Act") limits the Company's ability to pay dividends and distributions to shareholders. Total statutory capital and surplus and total statutory capital of our subsidiaries are relevant to the calculation of retained earnings that are free of restriction for the payment of dividends to Validus Holdings Ltd.

The ability of certain of these subsidiaries to pay dividends to us is limited under Bermuda law and regulations. The Insurance Act provides that each of our Bermuda subsidiaries may not declare or pay, in any financial year, dividends of more than 25% of

Table of Contents

its total statutory capital and surplus (as shown on its statutory balance sheet in relation to the previous financial year) unless it files with the BMA at least seven days prior to the payment, an affidavit signed by at least two directors and such subsidiary's principal representative, stating that in their opinion such subsidiary will continue to satisfy the required margins following declaration of those dividends, however, there is no additional requirement for BMA approval. In addition, before reducing its total statutory capital by 15% or more (as set out in its previous years' statutory financial statements) each of these subsidiaries must make application to the BMA for permission to do so, such application to consist of an affidavit signed by at least two directors and such subsidiary's principal representative stating that in their opinion the proposed reduction in capital will not cause such subsidiaries to fail to meet its relevant margins, and such other information as the BMA may require. The Company's primary restrictions on net assets of subsidiaries consist of regulatory requirements placed upon the regulated (re)insurance subsidiaries to hold minimum amounts of total statutory capital and surplus and there were no other material restrictions on net assets in place as of December 31, 2012. These amounts are available for distribution as dividend payments to the Company, subject to approval of the BMA. The amounts that are unrestricted net assets and which are available from the Company's subsidiaries for distribution as dividend payments to Validus Holdings, Ltd. without approval of the BMA for Validus Re, Validus Re Americas, Ltd., TIBL, AlphaCat Reinsurance, Ltd., PaCRe, Ltd., Flagstone Reassurance Suisse SA (Bermuda Branch) and Mont Fort Re Ltd. were $826.2 million, $nil, $467.3 million, $nil, $nil, $349.4 million and $0.1 million respectively.

Talbot manages Syndicate 1183 (the “Syndicate”) at Lloyd’s. Lloyd’s requires Talbot to hold cash and investments in trust for the benefit of policyholders either as Syndicate trust funds or as Funds at Lloyd’s (“FAL”). Talbot may not distribute funds from the Syndicate into its corporate member’s trust accounts unless, firstly, they are represented by audited profits and, secondly, the Syndicate has adequate future cash flow to service its policyholders. Talbot’s corporate member may not distribute funds to Talbot’s unregulated bank or investment accounts unless they are represented by a surplus of cash and investments over the FAL requirement. Additionally, U.K. company law prohibits Talbot’s corporate name from declaring a dividend to the Company unless it has “profits available for distribution”. The determination of whether a company has profits available for distribution is based on its accumulated realized profits less its accumulated realized losses. While the U.K. insurance regulatory laws do not impose statutory restrictions on a corporate name’s ability to declare a dividend, the U.K. Financial Services Authority’s (“FSA”) rules require maintenance of each insurance company’s solvency margin within its jurisdiction.

In addition, the indenture governing our Junior Subordinated Deferrable Debentures would restrict us from declaring or paying dividends on our common shares if we are downgraded by A.M. Best to a financial strength rating of “B” (Fair) or below or if A.M. Best withdraws its financial strength rating on any of our material insurance subsidiaries.

See “Business—Regulation—Bermuda,” “Risk Factors—Risks Related to Ownership of Our Common Shares—Because we ar holding company and substantially all of our operations are conducted by our main operating subsidiaries, Validus Re and Talbot, our ability to meet any ongoing cash requirements and to pay dividends will depend on our ability to obtain cash dividends or other cash payments or obtain loans from Validus Re and Talbot,” “Risk Factors—Risks Related to Our Company—We depend on ratings by A.M. Best Company. Our financial strength rating could be revised downward, which could affect our standing among brokers and customers, cause our premiums and earnings to decrease and limit our ability to pay dividends on our common shares.”

Share Repurchase Program

The Company has repurchased approximately 43.7 million common shares for an aggregate purchase price of $1,227.1 million from the inception of the share repurchase program to February 13, 2013.

The Company expects the purchases under its share repurchase program to be made from time to time in the open market or in privately negotiated transactions. The timing, form and amount of the share repurchases under the program will depend on a variety of factors, including market conditions, the Company’s capital position relative to internal and rating agency targets, legal requirements and other factors.

On February 6, 2013, the Board of Directors of the Company authorized an increase to the Company's common share repurchase authorization to $500.0 million. This amount is in addition to, and in excess of, the $1,206.8 million of common shares repurchased by the Company through February 6, 2013 under its previously authorized share repurchase program.

The repurchase program may be modified, extended or terminated by the Board of Directors at any time. The remaining amount available under the current authorizations is $479.8 million as of February 13, 2013.

Share repurchases include repurchases by the Company of shares, from time to time, from employees in order to facilitate the payment of withholding taxes on restricted shares granted and the exercise of stock appreciation rights. We purchased these shares at their fair market value, as determined by reference to the closing price of our common shares on the day the restricted shares vested or the stock appreciation rights were exercised.

Table of Contents

Effect of share repurchases:	As at December 31, 2011 (cumulative)	Share Repurchase Activity by Quarter Quarter ended March 31, 2012	Quarter ended June 30, 2012	Quarter ended September 30, 2012	Quarter ended December 31, 2012
	(Dollars in thousands, except share and per share amounts)				
Aggregate purchase price(a)	$947,170	$11,308	$209,944	$38,423	$—
Shares repurchased	35,031,985	372,560	6,558,884	1,174,628	—
Average price(a)	$27.04	$30.35	$32.01	$32.71	$—
Estimated net cumulative accretive (dilutive) impact on:					
Diluted BV per common share(b)		$1.49	$1.87	$2.42	$1.93
Diluted EPS—Quarter(c)		0.29	$0.42	$0.63	$0.32

Effect of share repurchases:	As at December 31, 2012 (cumulative)	Share Repurchase Activity Post Year End January	February	As at February 13, 2013	Cumulative to Date Effect
	(Dollars in thousands, except share and per share amounts)				
Aggregate purchase price(a)	$1,206,845	$—	$20,218	$20,218	$ 1,227,063
Shares repurchased	43,138,057	—	550,576	550,576	43,688,633
Average price(a)	$27.98	$—	$36.72	$36.72	$ 28.09

(a) Share transactions are on a trade date basis through February 13, 2013 and are inclusive of commissions. Average share price is rounded to two decimal places.

(b) As the average price per share repurchased during the periods 2010, 2011 and 2012 was lower than the book value per common share, the repurchase of shares increased the ending book value per share.

(c) The estimated impact on diluted earnings per share was calculated by comparing reported results versus i) net income per share plus an estimate of lost net investment income on the cumulative share repurchases divided by ii) weighted average diluted shares outstanding excluding the weighted average impact of cumulative share repurchases. The impact of cumulative share repurchases was accretive to diluted earnings per share.

Table of Contents

Item 6. Selected Financial Data

The summary Consolidated Statements of Comprehensive Income data for the years ended December 31, 2012, December 31, 2011, December 31, 2010, December 31, 2009 and December 31, 2008 and the summary consolidated balance sheet data as of December 31, 2012, December 31, 2011, December 31, 2010, December 31, 2009 and December 31, 2008 are derived from our audited consolidated financial statements. The Company was formed on October 19, 2005 and completed the acquisitions of Talbot, IPC and Flagstone on July 2, 2007, September 4, 2009 and November 30, 2012, respectively. IPC is included in the Company's consolidated results only for the four months ended December 31, 2009 and subsequent fiscal year ends. IPC is not included in the consolidated results for the year ended December 31, 2008. Flagstone is included in the Company's consolidated results only for the one month ended December 31, 2012. Flagstone is not included in the consolidated results for the years ended December 31, 2011, December 31, 2010, December 31, 2009 or December 31, 2008.

You should read the following summary consolidated financial information together with the other information contained in this Annual Report on Form 10-K, including "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and related notes included elsewhere herein.

Table of Contents

	Years Ended December 31, 2012	2011	2010	2009	2008
	(Dollars in thousands, except share and per share amounts)				
Revenues					
Gross premiums written	$2,166,440	$2,124,691	$1,990,566	$1,621,241	$1,362,484
Reinsurance premiums ceded	(307,506)	(289,241)	(229,482)	(232,883)	(124,160)
Net premiums written	1,858,934	1,835,450	1,761,084	1,388,358	1,238,324
Change in unearned premiums	14,282	(33,307)	39	61,219	18,194
Net premiums earned	1,873,216	1,802,143	1,761,123	1,449,577	1,256,518
Gain on bargain purchase, net of expenses (a)	17,701	—	—	287,099	—
Net investment income	107,936	112,296	134,103	118,773	139,528
Realized gain on repurchase of debentures	—	—	—	4,444	8,752
Net realized gains (losses) on investments	18,233	28,532	32,498	(11,543)	(1,591)
Net unrealized gains (losses) on investments	17,585	(19,991)	45,952	84,796	(79,707)
(Loss) from investment affiliate	(964)	—	—	—	—
Other income	22,396	5,718	5,219	4,634	5,264
Foreign exchange gains (losses)	4,798	(22,124)	1,351	(674)	(49,397)
Total revenues	2,060,901	1,906,574	1,980,246	1,937,106	1,279,367
Expenses					
Losses and loss expenses	999,446	1,244,401	987,586	523,757	772,154
Policy acquisition costs	334,698	314,184	292,899	262,966	234,951
General and administrative expenses	263,652	197,497	209,290	185,568	123,948
Share compensation expenses	26,709	34,296	28,911	27,037	27,097
Finance expenses	53,857	54,817	55,870	44,130	57,318
Transaction expenses (b)	—	17,433	—	—	—
Total expenses	1,678,362	1,862,628	1,574,556	1,043,458	1,215,468
Net income before taxes and income from operating affiliates	382,539	43,946	405,690	893,648	63,899
Tax (expense) benefit	(2,501)	(824)	(3,126)	3,759	(10,788)
Income from operating affiliates	12,580	—	—	—	—
Net income	392,618	43,122	402,564	897,407	53,111
Net loss (income) attributable to noncontrolling interest	15,820	(21,793)	—	—	—
Net income available to Validus	408,438	21,329	402,564	897,407	53,111
Comprehensive income					
Foreign currency translation adjustments	3,648	(1,146)	(604)	3,007	(7,809)
Comprehensive income	$412,086	$20,183	$401,960	$900,414	$45,302
Earnings per share					
Weighted average number of common shares and common share equivalents outstanding					
Basic	97,184,110	98,607,439	116,018,364	93,697,194	74,677,903

Diluted	102,384,923	100,928,284	120,630,945	97,168,409	75,819,413
Basic earnings per share available to common shareholders	$4.13	$0.14	$3.41	$9.51	$0.62
Diluted earnings per share available to common shareholders	$3.99	$0.14	$3.34	$9.24	$0.61
Cash dividends declared per share	$1.00	$1.00	$0.88	$0.80	$0.80
Selected financial ratios					
Losses and loss expenses (c)	53.4 %	69.1 %	56.1 %	36.1 %	61.5 %
Policy acquisition cost (d)	17.9 %	17.4 %	16.6 %	18.1 %	18.7 %
General and administrative expense (e)	15.5 %	12.9 %	13.5 %	14.7 %	12.0 %
Expense ratio (f)	33.4 %	30.3 %	30.1 %	32.8 %	30.7 %
Combined ratio (g)	86.8 %	99.4 %	86.2 %	68.9 %	92.2 %
Annualized return on average equity (h)	11.3 %	0.6 %	10.8 %	31.8 %	2.7 %

Table of Contents

The following table sets forth summarized balance sheet data as of December 31, 2012, 2011, 2010, 2009 and 2008:

	As at December 31,				
	2012	2011	2010	2009	2008
	(Dollars in thousands, except share and per share amounts)				
Summary Balance Sheet Data:					
Investments at fair value	$6,764,032	$5,191,123	$5,118,859	$5,388,759	$2,831,537
Cash and cash equivalents	1,219,379	832,844	620,740	387,585	449,848
Total assets	10,020,264	7,618,471	7,060,878	7,019,140	4,322,480
Reserve for losses and loss expenses	3,517,573	2,631,143	2,035,973	1,622,134	1,305,303
Unearned premiums	894,362	772,382	728,516	724,104	539,450
Senior notes payable	247,090	246,982	246,874	—	—
Debentures payable	540,709	289,800	289,800	289,800	304,300
Total shareholders’ equity	4,455,107	3,448,425	3,504,831	4,031,120	1,938,734
Book value per common share (i)	37.26	34.67	35.76	31.38	25.64
Diluted book value per common share (j)	35.22	32.28	32.98	29.68	23.78

(a) The gain on bargain purchase, net of expenses, arises from the acquisition of Flagstone on November 30, 2012 and IPC on September 4, 2009 and is net of transaction related expenses.

(b) The transaction expenses relate to cost incurred in connection with the Company’s proposed acquisition of Transatlantic Holdings, Inc. Transaction expenses are primarily comprised of legal, financial advisory and audit related services.

(c) The loss and loss expense ratio is calculated by dividing losses and loss expenses by net premiums earned.

(d) The policy acquisition cost ratio is calculated by dividing policy acquisition costs by net premiums earned.

(e) The general and administrative expense ratio is calculated by dividing the sum of general and administrative expenses and share compensation expenses by net premiums earned.

(f) The expense ratio is calculated by combining the policy acquisition cost ratio and the general and administrative expense ratio.

(g) The combined ratio is calculated by combining the loss ratio, the policy acquisition cost ratio and the general and administrative expense ratio.

(h) Return on average equity is calculated by dividing the net income available to Validus for the period by the average shareholders’ equity available to Validus during the period. Quarterly average shareholders’ equity is the average of the beginning and ending shareholders’ equity balances. Annual average shareholders’ equity is the average of the beginning, ending and intervening quarter end shareholders’ equity balances.

(i) Book value per common share is defined as total shareholders’ equity available to Validus divided by the number of common shares outstanding as at the end of the period, giving no effect to dilutive securities.

(j) Diluted book value per common share is calculated based on total shareholders’ equity available to Validus plus the assumed proceeds from the exercise of outstanding options and warrants, divided by the sum of common shares, unvested restricted shares, options and warrants outstanding (assuming their exercise).

Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following is a discussion and analysis of the Company’s consolidated results of operations for the three months ended December 31, 2012 and 2011 and for years ended December 31, 2012, 2011 and 2010 and the Company’s consolidated financial condition, liquidity and capital resources at December 31, 2012 and 2011. This discussion and analysis should be read in conjunction with the Company’s audited consolidated financial statements and related notes thereto included elsewhere within this filing.

For a variety of reasons, the Company’s historical financial results may not accurately indicate future performance. See “Cautionary Note Regarding Forward-Looking Statements.” The Risk Factors set forth in Item 1A above present a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained herein.

52

Table of Contents

Executive Overview

The Company conducts its operations worldwide through three operating segments which have been determined under U.S. GAAP segment reporting, Validus Re, Talbot and AlphaCat. The Company, provides reinsurance, insurance and insurance linked securities fund management. Validus Re is a Bermuda based reinsurer focused on short tail lines of reinsurance. Talbot is the Bermuda parent of the specialty insurance group primarily operating within the Lloyd's insurance market through Syndicate 1183. AlphaCat is a Bermuda based investment adviser, managing third-party capital in insurance linked securities and other investments in the property catastrophe reinsurance space.

The Company's strategy has been to concentrate primarily on short-tail risks, which has been an area where management believes current prices and terms provide an attractive risk adjusted return and the management team has proven expertise. The Company's profitability in any given period is based upon premium and investment revenues, less net losses and loss expenses, acquisition expenses and operating expenses. Financial results in the insurance and reinsurance industry are influenced by the frequency and/or severity of claims and losses, including as a result of catastrophic events, changes in interest rates, financial markets and general economic conditions, the supply of insurance and reinsurance capacity and changes in legal, regulatory and judicial environments.

On April 2, 2012, the Company capitalized PaCRe, a new Class 4 Bermuda reinsurer formed for the purpose of writing high excess property catastrophe reinsurance. PaCRe was funded with $500.0 million of contributed capital. Validus invested $50.0 million in PaCRe's common equity. The Company will underwrite business for PaCRe, for which it will be paid a profit commission based on PaCRe's underwriting results. As Validus Re holds a majority of PaCRe's outstanding voting rights, the financial statements of PaCRe are included in the consolidated financial statements for the Company. The portion of PaCRe's earnings attributable to third party investors for the year ended December 31, 2012 is recorded in the consolidated Statements of Comprehensive Income as "Net loss (income) attributable to noncontrolling interest."

On May 29, 2012, the Company announced that it has joined with other investors in capitalizing AlphaCat Re 2012. AlphaCat Re 2012 is a new special purpose reinsurer formed for the purpose of writing collateralized reinsurance with a particular focus on windstorm risks for Florida domiciled insurance companies. AlphaCat Re 2012 was funded with $70.0 million of equity capital. The Company will underwrite business for AlphaCat Re 2012, for which it will be paid a commission for originating the business and a profit commission based on underwriting results. Validus Re has an equity interest and voting rights in AlphaCat Re 2012 which is below 50%, therefore the investment in AlphaCat Re 2012 is included as an equity method investment in the consolidated financial statements of the Company.

On November 30, 2012, the Company acquired all of the outstanding shares of Flagstone, strengthening the Company's leading property catastrophe reinsurance and short-tail specialty insurance platform. For segmental reporting purposes, the results of Flagstone's operations since the acquisition date have been included within the Validus Re segment in the consolidated financial statements.

On December 17, 2012, the Company joined with other investors in capitalizing AlphaCat 2013, a new special purpose vehicle formed for the purpose of investing in collateralized reinsurance. AlphaCat 2013 was funded with $230.0 million of contributed capital. Validus Re has an equity interest and voting rights in AlphaCat 2013 which is below 50%, therefore the investment in AlphaCat 2013 is included as an equity method investment in the consolidated financial statements of the Company.

On December 17, 2012, the Company also received $219.4 million of third party subscriptions for AlphaCat Insurance Linked Securities ("ILS") Funds.

Written premiums are a function of the number and type of contracts written and the prevailing market prices. Renewal dates for reinsurance business tend to be concentrated at the beginning of quarters, with the timing of premiums written varying by line of business. Most property catastrophe business incepts January 1, April 1, June 1 and July 1 with an annual policy, while most insurance and specialty lines renewals are more evenly spread throughout the year. Written premiums are generally highest in the first quarter and lowest during the fourth quarter of the year. Gross premiums written for pro rata programs are initially recorded as estimates and are then adjusted as actual results become known. Pro rata reinsurance is a type of reinsurance whereby the reinsurer indemnifies the policyholder against a predetermined portion of losses in return for a proportional share of the direct premiums.

Premiums are then generally earned over a 24 month period and paid in monthly or quarterly installments.
The following are the primary lines in which the Company conducts business:
Property: Validus Re underwrites property catastrophe reinsurance, property per risk reinsurance and property pro rata reinsurance. Property catastrophe includes reinsurance for insurance companies' exposures to an accumulation of property and related losses from separate policies, typically relating to natural disasters or other catastrophic events. Property per risk provides reinsurance for insurance companies' excess retention on individual property and related risks, such as highly-valued buildings. In property pro rata contracts the reinsurer shares the premiums as well as the losses and expenses in an agreed proportion with

the cedant. AlphaCat underwrites property catastrophe reinsurance. Talbot primarily writes direct and facultative property insurance, lineslips and binding authorities and property treaty. The business written is principally onshore energy, commercial and industrial insurance. The business is short-tail with premiums generally earned within one year and claims generally paid within two years.

Marine: The Company underwrites insurance and reinsurance on marine risks covering damage to or losses of marine vessels or cargo, yachts and marinas, third-party liability for marine accidents and physical loss and liability from principally offshore energy properties. Talbot underwrites both marine treaty reinsurance and insurance on a direct and facultative basis. Validus Re underwrites marine reinsurance on an excess of loss basis, and to a lesser extent, on a pro rata basis.

Specialty: The Company underwrites other specialty lines with very limited exposure correlation with its property, marine and energy portfolios. Validus Re underwrites other lines of business depending on an evaluation of pricing and market conditions, which include aerospace, terrorism, life and accident & health and workers' compensation catastrophe. With the exception of the aerospace line of business, which has a meaningful portion of its gross premiums written volume on a proportional basis, Validus Re's other specialty lines are primarily written on an excess of loss basis. Talbot underwrites war, political risks, political violence, financial institutions, contingency, accident and health, and aviation. Most of the Talbot specialty business is written on a direct or facultative basis or through a binding authority or coverholder in conjunction with a significant aviation treaty account.

Income from the Company's investment portfolio primarily comprises interest income on fixed maturity investments net of investment expenses and net realized/unrealized gains/losses on investments. A significant portion of the Company's contracts provide short-tail coverage for damages resulting mainly from natural and man-made catastrophes, which means that the Company could become liable for a significant amount of losses on short notice. Accordingly, the Company has structured its investment portfolio to preserve capital and maintain a high level of liquidity, which means that the large majority of the Company's investment portfolio consists of short-term fixed maturity investments. The Company's fixed income investments are classified as trading. Under U.S. GAAP, these securities are carried at fair value, and unrealized gains and losses are included in net income in the Company's Consolidated Statements of Comprehensive Income.

The Company's expenses consist primarily of losses and loss expenses, acquisition costs, general and administrative expenses, and finance expenses related to debentures, senior notes and our credit facilities.

Losses and loss expenses are a function of the amount and type of insurance and reinsurance contracts written and of the loss experience of the underlying risks. Reserves for losses and loss expenses include a component for outstanding case reserves for claims which have been reported and a component for losses incurred but not reported. The uncertainties inherent in the reserving process, together with the potential for unforeseen developments, may result in losses and loss expenses materially different than the reserve initially established. Changes to prior year loss reserves will affect current underwriting results by increasing net income if a portion of the prior year reserves prove to be redundant or decreasing net income if the prior year reserves prove to be insufficient. Adjustments resulting from new information will be reflected in income in the period in which they become known. The Company's ability to estimate losses and loss expenses accurately, and the resulting impact on contract pricing, is a critical factor in determining profitability.

Since most of the lines of business underwritten have large aggregate exposures to natural and man-made catastrophes, the Company expects that claims experience will often be the result of irregular and significant events. The occurrence of claims from catastrophic events is likely to result in substantial volatility in, and could potentially have a material adverse effect on, the Company's financial condition, results of operations, and ability to write new business. The business written by Talbot helps to mitigate these risks by providing us with significant benefits in terms of product line and geographic diversification.

Acquisition costs consist principally of brokerage expenses and commissions which are driven by contract terms on reinsurance contracts written, and are normally a specific percentage of premiums. Under certain contracts, cedants may also receive profit commissions which will vary depending on the loss experience on the contract. Acquisition costs are presented net of commissions or fees received on any ceded premium.

General and administrative expenses are generally comprised of expenses which do not vary with the amount of premiums written or losses incurred. Applicable expenses include salaries and benefits, professional fees, office expenses, risk management, and stock compensation expenses. Stock compensation expenses include costs related to the Company’s long-term incentive plan, under which restricted stock are granted to certain employees.

Business Outlook and Trends

We underwrite global specialty property insurance and reinsurance and have large aggregate exposures to natural and man-made disasters. The occurrence of claims from catastrophic events results in substantial volatility, and can have material adverse effects on the Company’s financial condition and results and ability to write new business. This volatility affects results for the

Table of Contents

period in which the loss occurs because U.S. accounting principles do not permit reinsurers to reserve for such catastrophic events until they occur. Catastrophic events of significant magnitude historically have been relatively infrequent, although management believes the property catastrophe reinsurance market has experienced a higher level of worldwide catastrophic losses in terms of both frequency and severity in the period from 1992 to the present. We also expect that increases in the values and concentrations of insured property will increase the severity of such occurrences in the future. The Company seeks to reflect these trends when pricing contracts.

Property and other reinsurance premiums have historically risen in the aftermath of significant catastrophic losses. As loss reserves are established, industry surplus is depleted and the industry’s capacity to write new business diminishes. At the same time, management believes that there is a heightened awareness of exposure to natural catastrophes on the part of cedants, rating agencies and catastrophe modeling firms, resulting in an increase in the demand for reinsurance protection. The global property and casualty insurance and reinsurance industry has historically been highly cyclical. Since 2007, increased capital provided by new entrants or by the commitment of capital by existing insurers and reinsurers increased the supply of insurance and reinsurance which resulted in a softening on rates on most lines. During 2010 there was an increased level of catastrophe activity, principally the Chilean earthquake and the Deepwater Horizon events but the Company continued to see increased competition and decreased premium rates in most classes of business.

During the January 2011 renewal season, Validus Re increased gross premiums written on its U.S. Cat XOL lines and decreased gross premiums written in the proportional lines. In addition, Validus Re decreased gross premiums written in the International Property lines as market conditions dictated. In the aftermath of 2010’s Deepwater Horizon loss, Validus Re saw additional opportunities and rate increases in the marine lines. Within its specialty lines, Validus Re increased gross premiums written in the terrorism lines among other sub-classes. Until the third quarter of 2011, premiums within Talbot remained relatively stable, then significant price increases were seen across offshore energy, onshore energy and property classes. Most other classes also experienced low level rate increases as the Lloyd’s market responded to the year’s highly publicized catastrophes (including the Christchurch earthquake, Brisbane floods, Tohuku earthquake and the Thailand floods) together with high frequency risk losses. These increases were offset by some pricing pressure remaining in places, resulting in an overall price increase at a whole account level of 3.1% for the year.

During the January 2012 renewal season, the Validus Re segment showed rate improvement relative to 2011. This improvement was largely due to the large catastrophe loss activity during 2011. During the first quarter of 2012, Talbot experienced rate increases in loss affected lines without seeing a systemic rise in rates across all lines. During the July 2012 renewal period, the Validus Re segment experienced rate improvements in the U.S. property lines while European and Latin American property rates were unchanged. The Talbot segment experienced a rate increase of 2.7% against a planned rate movement of 2% across the portfolio, with marine treaty, property and energy related lines outperforming the plan.

During the January 2013 renewal season, the Validus Re and AlphaCat segments underwrote $655.7 million in gross premiums written, an increase of 12.7% from the prior year period. This increase is driven primarily by an increase in gross premiums written in the specialty lines. This renewal data does not include Talbot’s operations as its business is distributed relatively evenly throughout the year.

Financial Measures

The Company believes the following financial indicators are important in evaluating performance and measuring the overall growth in value generated for shareholders:

Annualized return on average equity represents the level of net income available to shareholders generated from the average shareholders’ equity during the period. Annualized return on average equity is calculated by dividing the net income available to Validus for the period by the average shareholders’ equity available to Validus during the period. Average shareholders’ equity is the average of the beginning, ending and intervening quarter end shareholders’ equity balances. The Company’s objective is to generate superior returns on capital that appropriately reward shareholders for the risks assumed and to grow revenue only when returns meet or exceed internal requirements. Details of annualized return on average equity are provided below.

	Three Months Ended December 31,		Years Ended December 31,		
	2012	2011	2012	2011	2010
Annualized return on average equity	(9.5)%	3.2 %	11.3 %	0.6 %	10.8 %

The decrease in annualized return on average equity was driven primarily by a decrease in net income available to Validus for the three months ended December 31, 2012. Net income available to Validus for the three months ended December 31, 2012 decreased by $118.0 million, or 432.0% compared to the three months ended December 31, 2011 due primarily to losses incurred

55

on Hurricane Sandy. Net income available to Validus for the year ended December 31, 2012 increased by $387.1 million, compared to the year ended December 31, 2011 due primarily to the decreased impact of notable loss events for the year ended December 31, 2012 as compared to the year ended December 31, 2011.

Diluted book value per common share is considered by management to be an appropriate measure of our returns to common shareholders, as we believe growth in our book value on a diluted basis ultimately translates into growth of our stock price. Diluted book value per common share after dividends paid, increased by $2.94, or 9.1%, from $32.28 at December 31, 2011 to $35.22 at December 31, 2012. The increase was due to the income generated during the year ended December 31, 2012. Diluted book value per common share is a Non-GAAP financial measure. The most comparable U.S. GAAP financial measure is book value per common share. Diluted book value per common share is calculated based on total shareholders' equity plus the assumed proceeds from the exercise of outstanding options and warrants, divided by the sum of common shares, unvested restricted shares, options and warrants outstanding (assuming their exercise). A reconciliation of diluted book value per common share to book value per common share is presented below in the section entitled "Other Non-GAAP Financial Measures."

Cash dividends per common share are an integral part of the value created for shareholders. The Company declared quarterly cash dividends of $0.25 per common share and common share equivalent in each of the four quarters of 2012. On February 6, 2013, the Company announced an increase in the quarterly cash dividend to $0.30 per common share and $0.30 per common share equivalent for which each outstanding warrant is exercisable, payable on March 29, 2013 to holders of record on March 15, 2013. In addition, the Company announced a special dividend in the amount of $2.00 per common share and $2.00 per common share equivalent for which each outstanding warrant is exercisable, payable on February 26, 2013 to shareholders and warrant holders of record as of February 19, 2013.

Underwriting income measures the performance of the Company's core underwriting function, excluding revenues and expenses such as net investment income (loss), other income, finance expenses, net realized and unrealized gains (losses) on investments, foreign exchange gains (losses), gain on bargain purchase, net of expenses and transaction expenses. The Company believes the reporting of underwriting income enhances the understanding of our results by highlighting the underlying profitability of the Company's core insurance and reinsurance operations. Underwriting loss for the three months ended December 31, 2012 was $(113.1) million and underwriting income for the three months ended December 31, 2011 was $12.8 million. Underwriting income for the year ended December 31, 2012 and 2011 was $248.7 million and $11.8 million, respectively. Underwriting income is a Non-GAAP financial measure as described in detail and reconciled to net income in the section below entitled "Underwriting (Loss) Income."

Critical Accounting Policies and Estimates

The Company's consolidated financial statements have been prepared in accordance with U.S. GAAP. The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect reported and disclosed amounts of assets and liabilities, as well as disclosure of contingent assets and liabilities as at the balance sheet date and the reported amounts of revenues and expenses during the reporting period. Management believes the following accounting policies are critical to the Company's financial reporting as the application of these policies requires management to make significant judgments. Management believes the items that require the most subjective and complex estimates are (1) reserve for losses and loss expenses, (2) premiums, (3) reinsurance premiums ceded and reinsurance recoverable and (4) investment valuation.

Reserve for Losses and Loss Expenses

Description: We believe that the most significant accounting judgment made by management is our estimate of reserve for losses and loss expenses. The Company establishes its reserve for losses and loss expenses to cover the estimated remaining liability incurred for both reported claims ("case reserves") and unreported amounts ("incurred but not reported" or "IBNR reserves"). For insurance and reinsurance business, the IBNR reserves include provision for loss incidents that have occurred but have not yet been reported to the Company as well as for future variation in case reserves (where the claim has been reported but the ultimate cost is not yet known). The provision for future variation in current case reserves is generally calculated using actuarial estimates of total IBNR at the aggregated line of business level. Additional individual claim IBNR amounts are sometimes calculated for larger claims within our insurance and reinsurance businesses.Within the reinsurance business, the portion of total IBNR related to future variation on known claims is calculated at the individual claim level in some instances (either as an additional case reserve or individual claim IBNR). Within the insurance business, the provision for future variation in current case reserves is generally calculated using actuarial estimates of total IBNR, while individual claim IBNR amounts are sometimes calculated for larger claims. For AlphaCat, Talbot and Validus Re, IBNR is established separately for certain large or catastrophe losses and smaller "attritional" losses. The Company has procedures in place to aggregate large or catastrophe losses on a consolidated basis for financial reporting and disclosure purposes. For disclosure purposes, only those loss events which aggregate to over $15.0 million on a consolidated basis are disclosed separately and included in the reserve for notable loss events and reserve for development

56

Table of Contents

on events tables. Notable loss events are first determined at the respective operating segments based on segment thresholds and are then aggregated and disclosed if it is determined that they reach the consolidated threshold for notable loss disclosure.

For all lines of business, the Company's reserve for losses and loss adjustment expenses and loss reserves recoverable consist of three categories: (1) case reserves, (2) in certain circumstances, additional case reserves (ACR), and (3) IBNR reserves. The reserves and recoverables for attritional and large or catastrophe losses are established on an annual and interim basis as follows:

1.Case reserves: Case reserves generally are analyzed and established by each segment's claims department on all lines, making use of third party input where appropriate (including, for the reinsurance business, reports of losses from ceding companies). For insurance business where Talbot is not the lead underwriter on the business, the case reserves are established by the lead underwriter and validated by the central Lloyd's market claims bureau, with a sample reviewed by Talbot.

2.ACR reserves: ACRs are established for AlphaCat and Validus Re business by our claims department in cases where we believe the case reserves reported by the cedant require adjustment. ACRs supplement case reserves based on information obtained through ceding company audits or other sources. ACRs are not generally used at Talbot as claim volumes are generally greater and thus the potential for future variation in case reserve estimates on known claims often can be analyzed at an aggregate level using historical data.

3.IBNR reserves:

a.Large or catastrophe events—IBNR reserves are established for all lines based on each segment's estimates for known loss events for which not all claims have been reported to the Company. In establishing such IBNR reserves, the Company accumulates loss information from modeling agencies, where possible, publicly available sources and information contained in client reports and estimates. The loss information is applied to the Company's book of in-force contracts to establish an estimate of the Company's ultimate exposure to the loss event. For some large loss events, the Company estimates an ultimate loss expectation for the individual event. Paid losses, case reserves and any additional case reserves are then deducted from the ultimate loss to ascertain the IBNR estimate for these individual large claims or catastrophe events. The size of event for which the Company establishes a separate ultimate loss estimate may vary based on an assessment of the materiality of the event, as well as on other factors.

b.Attritional losses—IBNR reserves are established using some combination of the actuarial methods described above, including the Chain Ladder method, the Generalized Cape Cod method and the Bornhuetter-Ferguson method. In situations where limited historic development data is available and/or the year being analyzed is more recent (less mature), the expected loss method and the Bornhuetter-Ferguson method are more commonly used. Under all methods used at AlphaCat, Talbot and Validus Re, an ultimate loss amount is established. Paid losses, case reserves and any additional case reserves are then deducted from the ultimate loss to ascertain the attritional IBNR reserves.

For all sources of IBNR, net reserves are estimated by first estimating gross IBNR reserves, then estimating reinsurance recoverables on IBNR.

Judgments and Uncertainties: Loss reserve estimates for insurance and reinsurance business are not precise in that they deal with the inherent uncertainty in the outcome of insurance and reinsurance claims made on the Company, many of which have not yet been reported to the Company. Estimating loss reserves requires management to make assumptions, both explicit and implicit, regarding future paid and reported loss development patterns, frequency and severity trends, claims settlement practices, potential changes in the legal environment and other factors. These estimates and judgments are based on numerous factors, and may be revised over time as additional experience or other data becomes available, as new or improved methodologies are developed or as current laws change.

As predominantly a broker market insurer and reinsurer, the Company must rely on loss information reported to us by brokers from clients, where such information is often incomplete or changing. The quality and type of information received varies by client and by the nature of the business, insurance or reinsurance.

In the insurance business, for risks that the Company leads, the Company receives from brokers details of potential claims, on the basis of which the Company's loss adjusters make estimates of the likely ultimate outcome of the claims. In determining these reserves, the Company takes into account a number of factors including the facts and circumstances of the individual claim, the nature of the coverage and historical information about its experience on similar types of claims. For insurance business where another company is the lead, the case reserves are established by the lead underwriter and validated centrally by the Lloyd’s market claims bureau, with a sample reviewed by the Company. The sum of the individual claim estimates for lead and follow business constitutes the case reserves.

Table of Contents

For reinsurance business, the Company typically receives from brokers details of paid losses and estimated case reserves recorded by the ceding company. In addition to this, the ceding company's estimated provision for IBNR losses is sometimes also available, although this in itself introduces additional uncertainty owing to the differing and typically unknown reserving practices of ceding companies.

There will also be a time lag between a loss occurring and it being reported, first by the original claimant to its insurer, via the insurance broker, and for reinsurance business, subsequently from the insurer to the reinsurer via the reinsurance broker.

The Company writes a mix of predominantly short-tail business, both insurance and reinsurance. The combination of low claim frequency and high claim severity that is characteristic of much of this short-tail business makes the available data more volatile and less reliable for predicting ultimate losses. For example, in property lines, there can be additional uncertainty in loss estimation related to large catastrophe events, whether natural or man-made. With wind events, such as hurricanes, the damage assessment process may take more than a year. The cost of claims is also subject to volatility due to supply shortages for construction materials and labor. In the case of earthquakes, the damage assessment process may take longer as buildings are discovered to have structural weaknesses not initially detected.

The Company also writes longer tail insurance lines of business, predominantly financial institutions ($35.8 million of gross premiums written on a claims made basis) and marine and energy liabilities ($60.3 million of gross premiums substantially written on a losses occurring basis) for the year ended December 31, 2012. These longer tail lines represent 8.9% of Talbot's gross premiums written for the year ended December 31, 2012. For marine and energy liability, the time from the occurrence of a claim to its first report to the Company can also be years. For both marine and energy liability and financial institutions, the subsequent time between reporting of a claim and its settlement can be years. In these intervening periods between occurrence, reporting and settlement, additional facts regarding individual claims and trends often will become known and current laws and case law may change, affecting the ultimate value of the claim.

Taken together, these issues add considerable uncertainty to the process of estimating ultimate losses, hence loss reserves, and this uncertainty is increased for reinsurance business compared with insurance business due to the additional parties in the chain of reporting from the original claimant to the reinsurer.

As a result of the uncertainties described above, the Company must estimate IBNR reserves, which consist of a provision for future development on known loss events, as well as a provision for claims which have occurred but which have not yet been reported to us by clients. Because of the degree of reliance that is necessarily placed on brokers and (re)insured companies for claims reporting, the associated time lag, the low frequency/high severity nature of much of the business underwritten, the rapidly emerging and changing nature of facts and circumstances surrounding large events and, for reinsurance business, the varying reserving practices among ceding companies as described above, reserve estimates are highly dependent on management's judgment and are subject to uncertainty.

The Company strives to take account of these uncertainties in the judgments and assumptions made when establishing loss reserves, but it is not possible to eliminate the uncertainties. As a result, there is a risk that the Company's actual losses may be higher or lower than the reserves booked.

For the Company's insurance business written by Talbot, where a longer reserving history exists, the Company examines the development of its own historical paid and incurred losses to identify trends, which it then incorporates into the reserving process where it deems appropriate.

For the Company's reinsurance business, especially that written by Validus Re where the Company relies more heavily on information provided by clients in order to assist it in estimating reserves, the Company performs certain processes in order to help assess the completeness and accuracy of such information as follows:

1.In addition to information received from clients on reported claims, the Company also uses information on the patterns of client loss reporting and loss settlements from previous events in order to estimate the Company's ultimate liability related to these events;

2.The Company uses reinsurance industry information in order to perform consistency checks on the data provided by ceding companies and to identify trends in loss reporting and settlement activity. Where it deems appropriate, the Company incorporates such information in establishing reinsurance reserves; and

3.For both insurance and reinsurance business, the Company supplements the loss information received from clients with loss estimates developed by market share techniques and third party catastrophe models when such information is available.

Table of Contents

Although there is normally a lag in receiving reinsurance data from cedants, the Company currently has no backlog related to the processing of assumed reinsurance information. The Company actively manages its relationships with brokers and clients and considers existing disputes with counterparties to be in the normal course of business.

As described above, the reserve for losses and loss expenses includes both a component for outstanding case reserves for claims which have been reported and a component for IBNR reserves. IBNR reserves are the difference between ultimate losses and reported losses, where reported losses are the sum of paid losses and outstanding case reserves. Ultimate losses are estimated by management using various actuarial methods, including exposure-based and loss-based methods, as well as other qualitative assessments regarding claim trends.

The Company uses a reserving methodology that establishes a point estimate for ultimate losses. The point estimate represents management’s best estimate of ultimate losses and loss expenses. The Company does not select a range as part of its loss reserving process. The extent of reliance on management judgment in the reserving process differs depending on the circumstances surrounding the estimations, including the volume and credibility of data, the perceived relevance of historical data to future conditions, the stability or level of stability in the Company’s operational processes for handling losses (including claims practices and systems) and other factors. The Company reviews its reserving assumptions and methodologies on a quarterly basis. Two of the most critical assumptions in establishing reserves are loss emergence patterns and expected loss ratios. Loss emergence patterns are critical to the reserving process as they can be one key indicator of the ultimate liability. A pattern of reported loss emergence which is different from expectations may indicate a change in the loss climate and may thus influence the estimate of future payments that should be reflected in reserves. Expected loss ratios are a primary component in the Company’s calculation of estimated ultimate losses for business at an early stage in its development.

Loss emergence patterns for the business written by Talbot are generally derived from Talbot’s own historic loss development triangulations, supplemented in some instances by Lloyd’s market data. For the business written by Validus Re, where its own historic loss development triangulations are currently more limited, greater use is made of market data including reinsurance industry data available from organizations such as statistical bureaus and consulting firms, where appropriate. Expected loss ratios are estimated in a variety of ways, largely dependent upon the data available. Wherever it deems appropriate, management incorporates the Company’s own loss experience in establishing initial expected loss ratios and reserves. This is particularly true for the business written by Talbot where a longer reserving history exists and expected losses and loss ratios consider, among other things, rate increases and changes in terms and conditions that have been observed in the market. For reinsurance business, expected losses and loss ratios are typically developed using vendor and proprietary computer models. The information used in these models is collected by underwriters and actuaries during the initial pricing of the business.

The Company has large catastrophe event ultimate loss reserve estimation procedures for the investigation, analysis, and estimation of ultimate losses resulting from large catastrophe events. The determination regarding which events follow these procedures is made by members of senior management from relevant departments within the Company. The procedures are designed to facilitate the communication of information between various relevant functions and provide an efficient approach to determining the estimated loss for the event.

In developing estimates for large catastrophe events, the Company considers various sources of information including: specific loss estimates reported by our cedants and policyholders, ceding company and overall insurance industry loss estimates reported by our brokers and by claims reporting services, proprietary and third party vendor models and internal data regarding insured or reinsured exposures related to the geographical location of the event. Use of these various sources enables management to estimate the ultimate loss for known events with a higher degree of accuracy and timeliness than if the Company relied solely on one data source. Indicated ultimate loss estimates for catastrophe events are compiled by a committee of management, and these indicated ultimate losses are incorporated into the process of selecting management’s best estimate of reserves.

As with large catastrophe events, the Company separately estimates ultimate losses for certain large claims using a number of methods, including estimation based on vendor models, analyses of specific industry occurrences and facts, as well as information from cedants and policyholders on individual contract involvements.

During 2010 and 2011, given the complexity and severity of notable loss events, an explicit reserve for potential development on 2010 and 2011 notable loss events (RDE) was included within the Company's IBNR reserving

process. As uncertainties surrounding initial estimates on notable loss events develop, it is expected that this reserve will be allocated to specific notable loss events. No RDE was established for 2012 notable losses.
The requirement for a reserve for potential development on notable loss events in a quarter is a function of (a) the number of significant events occurring in that quarter and (b) the complexity and volatility of those events.
Complexity and volatility factors considered are as follows:
•Contract complexity;
• Nature and number of perils arising from an event;

Table of Contents

• Limits and sub limits exposed;
• Quality, timing and flow of information received from each loss;
• Timing of receipt of information to the Company;
• Information regarding retrocessional covers;
• Assumptions, both explicit and implicit, regarding future paid and reported loss development patterns;
• Frequency and severity trends;
• Claims settlement practices; and
• Potential changes in the legal environment.

Each of these factors may lead to associated volatility for each notable loss event as well as consideration of the total reserve for loss events in the aggregate. Consequently, all of these factors are considered in the aggregate for the events occurring in the quarter, recognizing that it is more likely that one or some of the events may deteriorate significantly, rather than all deteriorating proportionately. The establishment of each quarter's requirement for a reserve for potential development on notable loss events takes place as part of the quarterly evaluation of the Company's overall reserve requirements. It is not directly linked in isolation to any one significant/notable loss in the quarter. The reserve for potential development on notable loss events is evaluated by our in-house actuaries as part of their normal process in setting of indicated reserves for the quarter. In ensuing quarters the senior management and the in-house actuaries revisit and re-estimate certain events previously considered in the catastrophe loss event process as well as events that have subsequently emerged in the current quarter. To the extent that there has been adverse development on a notable loss event, if there is RDE remaining from that accident year, an allocation from the respective accident year RDE will be made to the notable loss event. If there is no remaining RDE relating to the accident year of the loss, then adverse development will be recorded for the notable loss event.

Changes to the reserve for potential development on notable loss events will be considered in light of changes to previous loss estimates from notable losses in this re-estimation process.To the extent that there are continued complexity and volatility factors relating to notable loss events in the aggregate, additions to the RDE may be established for a specific accident year, as illustrated in the RDE roll forward table below.

Management's loss estimates are subject to annual corroborative review by independent external actuaries using generally accepted actuarial techniques and other analytical and qualitative methods.

The Company's reserving methodology was not changed materially in the year ended December 31, 2012 from the methodology used in the year ended December 31, 2011 for either Validus Re, AlphaCat or Talbot. Management's best estimate of the gross reserve for losses and loss expenses and loss reserves recoverable at December 31, 2012 were $3,517.6 million and $440.0 million, respectively. The following table sets forth a breakdown between gross case reserves and gross IBNR by segment at December 31, 2012.

	As at December 31, 2012		
(Dollars in thousands)	Gross Case Reserves	Gross IBNR	Total Gross Reserve for Losses and Loss Expenses
Validus Re	$1,009,434	$1,113,461	$2,122,895
AlphaCat	5,000	—	5,000
Talbot	760,149	720,158	1,480,307
Eliminations	(55,485)	(35,144)	(90,629)
Total	$1,719,098	$1,798,475	$3,517,573

Management's best estimate of the gross reserve for losses and loss expenses and loss reserves recoverable at December 31, 2011 were $2,631.1 million and $372.5 million, respectively. The following table sets forth a breakdown between gross case reserves and gross IBNR by segment at December 31, 2011.

	As at December 31, 2011		
(Dollars in thousands)	Gross Case Reserves	Gross IBNR	Total Gross Reserve for Losses and

			Loss Expenses
Validus Re	$765,299	$585,550	$1,350,849
AlphaCat	—	10,000	10,000
Talbot	703,965	673,596	1,377,561
Eliminations	(54,822)	(52,445)	(107,267)
Total	$1,414,442	$1,216,701	$2,631,143

Table of Contents

To the extent insurance and reinsurance industry data is relied upon to aid in establishing reserve estimates, there is a risk that the data may not match the Company's risk profile or that the industry's reserving practices overall differ from those of the Company and its clients. In addition, reserving can prove especially difficult should a significant loss event take place near the end of an accounting period, particularly if it involves a catastrophic event. These factors further contribute to the degree of uncertainty in the reserving process.

The uncertainties inherent in the reserving process, together with the potential for unforeseen developments, including changes in laws and the prevailing interpretation of policy terms, may result in losses and loss expenses materially different from the reserves initially established. Changes to prior year reserves will affect current period underwriting income by increasing income if the prior year ultimate losses are reduced or decreasing income if the prior year ultimate losses are increased. The Company expects volatility in results in periods when significant loss events occur because U.S. GAAP does not permit insurers or reinsurers to reserve for loss events until they have both occurred and are expected to give rise to a claim. As a result, the Company is not allowed to record contingency reserves to account for expected future losses. The Company anticipates that claims arising from future events will require the establishment of substantial reserves in future periods.

Effect if Actual Results Differ From Assumptions: Given the risks and uncertainties associated with the process for estimating reserves for losses and loss expenses, management has performed an evaluation of the potential variability in loss reserves and the impact this variability may have on reported results, financial condition and liquidity. Because of the inherent uncertainties discussed above, we have developed a reserving philosophy which attempts to incorporate prudent assumptions and estimates, and we have generally experienced favorable net development on prior year reserves in the last several years. However, there is no assurance that this will occur in future periods.

Management's best estimate of the net reserve for losses and loss expenses at December 31, 2012 is $3,077.6 million. The following tables show the effect on estimated net reserves for losses and loss expenses as of December 31, 2012 of a change in two of the most critical assumptions in establishing reserves: (1) loss emergence patterns, accelerated or decelerated by three and six months; and (2) expected loss ratios varied by plus or minus five and ten percent. Management believes that a reasonably likely scenario is represented by such a standard, as used by some professional actuaries as part of their review of an insurer's or reinsurer's reserves. Utilizing this standard as a guide, management has selected these variances to determine reasonably likely scenarios of variability in the loss emergence and loss ratio assumptions. These scenarios consider normal levels of catastrophe events. Loss reserves may vary beyond these scenarios in periods of heightened or reduced claim activity. The reserves resulting from the changes in the assumptions are not additive and should be considered separately. The following tables vary the assumptions employed therein independently. In addition, the tables below do not adjust any parameters other than the ones described above. Specifically, reinsurance collectability was not explicitly stressed as part of the calculations below.

Table of Contents

Net reserve for losses and loss expenses at December 31, 2012—Sensitivity to loss emergence patterns

Change in assumption	Reserve for losses and loss expenses (Dollars in thousands)
Six month acceleration	$2,661,432
Three month acceleration	2,855,922
No change (selected)	3,077,606
Three month deceleration	3,325,264
Six month deceleration	3,598,079

Net reserve for losses and loss expenses at December 31, 2012—Sensitivity to expected loss expenses

Change in assumption	Reserve for losses and loss expenses (Dollars in thousands)
10% favorable	$2,959,320
5% favorable	3,018,463
No change (selected)	3,077,606
5% unfavorable	3,136,749
10% unfavorable	3,195,892

The most significant variance in the above scenarios, six month deceleration in loss emergence patterns, would have the effect of increasing losses and loss expenses by $520.5 million.

Management believes that the reserve for losses and loss expenses is sufficient to cover expected claims incurred before the evaluation date on the basis of the methodologies and judgments used to support its estimates. However, there can be no assurance that actual payments will not vary significantly from total reserves. The reserve for losses and loss expenses and the methodology of estimating such reserve are regularly reviewed and updated as new information becomes known. Any resulting adjustments are reflected in income in the period in which they become known.

Premiums

Description: For insurance business, written premium estimates are determined from the business plan estimates of premiums by class, the aggregate of underwriters' estimates on a policy-by-policy basis, and projections of ultimate premiums using generally accepted actuarial methods. In particular, direct insurance premiums are recognized in accordance with the type of contract written.

The majority of our insurance premium is accepted on a direct open market or facultative basis. We receive a premium which is identified in the policy and recorded as unearned premium on the inception date of the contract. This premium will typically adjust only if the underlying insured values adjust. We actively monitor underlying insured values and record adjustment premiums in the period in which amounts are reasonably determinable.

Judgments and Uncertainties: For business written on a facultative basis, although a premium estimate is not contractually stated for the amount of business to be written under any particular facility, an initial estimate of the expected premium written is received from the coverholder via the broker. Our estimate of premium is derived by reference to one or more of the following: the historical premium volume experienced by any facility; historical premium volume of similar facilities; the estimates provided by the broker; and industry information on the underlying business. We actively monitor the development of actual reported premium against the estimates made; where actual reported premiums deviate from the estimate, we carry out an analysis to determine the cause and may, if necessary, adjust the estimated premiums. In the year ended December 31, 2012, premiums written on a facultative basis accounted for approximately $357.2 million of total gross premiums written at Talbot.

For contracts written on a losses occurring basis or claims made basis, premium income is generally earned proportionately over the expected risk period, usually 12 months. For all other contracts, comprising contracts written on a risks attaching basis, premiums are generally earned over a 24 month period due to the fact that some of the underlying exposures may attach towards the end of the contract, and such underlying exposures generally have a 12 month coverage period. The portion of the premium

Table of Contents

related to the unexpired portion of the policy at the end of any reporting period is presented on the consolidated balance sheet as unearned premiums.

(Dollars in thousands)	Year Ended December 31, 2012 (a) Gross Written Premiums	Gross Written Premiums (%)	Year Ended December 31, 2011 Gross Written Premiums	Gross Written Premiums (%)	Year Ended December 31, 2010 Gross Written Premiums	Gross Written Premiums (%)
Proportional	$333,469	15.4 %	$267,378	12.6 %	$260,149	13.1 %
Non-proportional	1,832,971	84.6 %	1,857,313	87.4 %	1,730,417	86.9 %
Total	$2,166,440	100.0 %	$2,124,691	100.0 %	$1,990,566	100.0 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

For reinsurance business where the assumed reinsurance premium is written on an excess of loss or on a pro rata basis, reinsurance contracts are generally written prior to the time the underlying direct policies are written by cedants and accordingly cedants must estimate such premiums when purchasing reinsurance coverage. For excess of loss contracts, the deposit premium is defined in the contract. The deposit premium is based on the client's estimated premiums, and this estimate is the amount recorded as written premium in the period the risk incepts. In the majority of cases, these contracts are adjustable at the end of the contract period to reflect the changes in underlying risks during the contract period. Subsequent adjustments, based on reports by the clients of actual premium, are recorded in the period in which the cedant reports are received, which would normally be reported within six months to one year subsequent to the expiration of the contract. For pro rata reinsurance contracts, an estimate of written premium is recorded in the period in which the risk incepts. The written premiums estimate is based on the pro rata cession percentage, on information provided by ceding companies and on management's judgment. Management critically evaluates the information provided by ceding companies based on experience with the cedant, broker and the underlying book of business.

Throughout the term of the policy, periodic review of the estimated premium takes place based on the latest information available, which may include actual reported premium to date, the latest premium estimates as provided by cedants and brokers, historical experience, management's professional judgment, information obtained during the underwriting renewal process, as well as an assessment of relevant economic conditions. If necessary, subsequent adjustments are recorded at the time of review.

On a quarterly basis, the Company evaluates the appropriateness of these premium estimates based on the latest information available, which may include actual reported premium to date, the latest premium estimates as provided by cedants and brokers, historical experience, management's professional judgment, information obtained during the underwriting renewal process, as well as an assessment of relevant economic conditions. Past experience may not be indicative of how future premium estimates develop. The Company believes that reasonably likely changes in assumptions made in the estimation process would not have a significant impact on gross premiums written as recorded.

Where contract terms on excess of loss contracts require the mandatory reinstatement of coverage after a client's loss, the mandatory reinstatement premiums are recorded as written and earned premiums when the loss event occurs.

Management includes an assessment of the creditworthiness of cedants in the review process above, primarily based on market knowledge, reports from rating agencies, the timeliness of cedants' payments and the status of current balances owing. Based on this assessment, management believes that as at December 31, 2012 no provision for doubtful accounts is necessary for receivables from cedants.

Reinsurance Premiums Ceded and Reinsurance Recoverables

Description: As discussed in Item 1 "Business—Underwriting Risk Management," the Company primarily uses ceded reinsurance for risk mitigation purposes. Talbot purchases reinsurance on an excess of loss and a proportional basis together with a relatively small amount of facultative reinsurance and ILWs. Validus Re purchases reinsurance on an excess of loss and a proportional basis together with ILW coverage.

Judgments and Uncertainties: For excess of loss business, the amount of premium payable is usually contractually documented at inception and management judgment is only necessary in respect of any loss-related elements of the premium, for example reinstatement or adjustment premiums, and loss-related commissions. The full premium is recorded at inception and if the contract is purchased on a "losses occurring " basis, the premium is earned on a straight line basis over the life of the contract. If the policy is purchased on a "risks attaching " basis, the premium is earned in line with the inwards gross premiums to which the risk attaching relates. After the contract has expired, a No Claims Bonus may be received for certain policies, and this is recorded as a reinsurance premium adjustment in the period in which it can be reasonably determined.

Table of Contents

Reinsurance receivable and reinsurance recoverable balances include amounts owed to us in respect of paid and unpaid ceded losses and loss expenses, respectively. The balances are presented net of a reserve for non-recoverability. As at December 31, 2012, reinsurance recoverable balances were $440.0 million and paid losses recoverable balances were $46.4 million. In establishing our reinsurance recoverable balances, significant judgment is exercised by management in determining the amount of unpaid losses and loss expenses to be ceded as well as our ability to cede losses and loss expenses under our reinsurance contracts.

Our ceded unpaid losses and loss expense consists of two elements, those for reported losses and those for losses incurred but not reported ("IBNR"). Ceded amounts for IBNR are developed as part of our loss reserving process. Consequently, the estimation of ceded unpaid losses and loss expenses is subject to similar risks and uncertainties in the estimation of gross IBNR (see "Reserve for Losses and Loss Expenses" above). As at December 31, 2012, ceded IBNR recoverable balances were $185.3 million.

Although our reinsurance receivable and reinsurance recoverable balances are derived from our determination of contractual provisions, the recoverability of such amounts may ultimately differ due to the potential for a reinsurer to become financially impaired or insolvent or for a contractual dispute over contract language or coverage. Consequently, we review our reinsurance recoverable balances on a regular basis to determine if there is a need to establish a provision for non-recoverability. In performing this review, we use judgment in assessing the credit worthiness of our reinsurers and the contractual provisions of our reinsurance agreements. As at December 31, 2012, we had a provision for non-recoverability of $6.6 million. In the event that the credit worthiness of our reinsurers were to deteriorate, actual uncollectible amounts could be significantly greater than our provision for non-recoverability.

The Company uses a default analysis to estimate uncollectible reinsurance. The primary components of the default analysis are reinsurance recoverable balances by reinsurer and default factors used to determine the portion of a reinsurer's balance deemed to be uncollectible. Default factors require considerable judgment and are determined using the current rating, or rating equivalent, of each reinsurer as well as other key considerations and assumptions.

Effect if Actual Results Differ from Assumptions: At December 31, 2012, the use of different assumptions within the model could have an effect on the provision for uncollectible reinsurance reflected in the Company's consolidated financial statements. To the extent the creditworthiness of the Company's reinsurers was to deteriorate due to an adverse event affecting the reinsurance industry, such as a large number of major catastrophes, actual uncollectible amounts could be significantly greater than the Company's provision.

Investment Valuation

Description: Consistent with U.S. GAAP, the Company recognizes fixed maturity and short-term investments at their fair value in the consolidated balance sheets. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

U.S. GAAP also established a three level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon whether the inputs to the valuation of an asset or liability are observable or unobservable in the market at the measurement date, with quoted market prices being the highest level ("Level 1") and unobservable inputs being the lowest level ("Level 3"). Generally, the degree of judgment used in measuring the fair value of financial instruments inversely correlates with the availability of observable inputs. All of the Company's fixed maturity and short-term investment fair value measurements have either quoted market prices or other observable inputs.

Judgments and Uncertainties:The Company's external investment accounting service provider receives prices from independent pricing sources to measure the fair values of its fixed maturity investments. These independent pricing sources are prioritized with respect to reliability to ensure that only the highest priority pricing inputs are used. The independent pricing sources are received via automated feeds from indices, pricing and broker-dealers services. Pricing is also obtained from other external investment managers. This information is applied consistently across all portfolios. The Company's external investment accounting service provider confirms and documents all prices received from broker-dealers on a daily basis for quality control and audit purposes.

In addition to internal controls, management relies on the effectiveness of the valuation controls in place at the Company's external investment accounting service provider (supported by a SSAE 16 Report) in conjunction with regular discussion and analysis of the investment portfolio's structure and performance. To date, management has not noted any issues or discrepancies related to investment valuation.

Other investments consist of hedge funds, a fund of hedge funds, private equity investments and a deferred compensation trust held in mutual funds. The hedge funds were valued at $538.5 million at December 31, 2012. The hedge funds consist of an investment in four Paulson & Co. managed funds and three investment funds assumed from the Flagstone Acquisition. The Paulson & Co. Inc. funds' administrator provides monthly reported Net Asset Values ("NAVs") with a one-month delay in its valuation. As a result, the funds' administrator's November 30, 2012 NAV was used as a partial basis for fair value measurement in the

Table of Contents

Company's December 31, 2012 balance sheet. The fund manager provides an estimate of the NAV at December 31, 2012 based on estimated performance. The Company adjusts fair value to the fund manager's estimated NAV that incorporates relevant valuation sources on a timely basis. As this valuation technique incorporates both observable and significant unobservable inputs, the Paulson hedge funds are classified as Level 3 assets. To determine the reasonableness of the estimated NAV, the Company assesses the variance between the fund manager's estimated NAV and the fund administrator's NAV. Material variances are recorded in the current reporting period while immaterial variances are recorded in the following reporting period. These managed hedge funds are subject to quarterly liquidity.
The Flagstone investment funds and private equity investments' monthly reported NAV is provided with a one-month or one-quarter delay in its valuation. As a result, the November 30, 2012 NAV or the September 30, 2012 NAV was used as a basis for fair value measurement in the Company's December 31, 2012 balance sheet. As this valuation technique incorporates both observable and significant unobservable inputs, the investments funds and private equity investments are classified as Level 3 assets.
The fund of hedge funds includes a side pocket valued at $4.1 million at December 31, 2012. While a redemption request has been submitted, the timing of receipt of proceeds on the side pocket is unknown. The fund's administrator provides a monthly reported NAV with a one-month delay in its valuation. As a result, the fund administrator's November 30, 2012 NAV was used as a basis for fair value measurement in the Company's December 31, 2012 balance sheet. The fund manager provides an estimate of the fund NAV at December 31, 2012 based on the estimated performance provided from the underlying third-party funds. To determine the reasonableness of the NAV, the Company compares the one-month delayed fund administrator's NAV to the fund manager's estimated NAV that incorporates relevant valuation sources on a timely basis. Material variances are recorded in the current reporting period while immaterial variances are recorded in the following reporting period. As this valuation technique incorporates both observable and significant unobservable inputs, the fund of hedge funds is classified as a Level 3 asset.
Effect if Actual Results Differ from Assumptions: Refer to Item 7A. “Quantitative and Qualitative Disclosures About Market Risk” for further discussion of interest rate risk and a sensitivity analysis of the impact of interest rate variances on the valuation of the Company’s fixed maturity and short-term investments.

Segment Reporting

Management has determined that the Company operates in three reportable segments. These segments are its significant operating subsidiaries, Validus Re, AlphaCat and Talbot. For segmental reporting purposes, the results of Flagstone’s operations since the acquisition date have been included within the Validus Re segment in the consolidated financial statements.

Results of Operations

The Company commenced operations on December 16, 2005. The Company’s fiscal year ends on December 31. Financial statements are prepared in accordance with U.S. GAAP and relevant SEC guidance.
The following table presents results of operations for the three months ended December 31, 2012 and 2011 and years ended December 31, 2012, 2011 and 2010:

Table of Contents

	Three Months Ended December 31,		Years Ended December 31,		
(Dollars in thousands)	2012 (a)	2011	2012 (a)	2011	2010
Gross premiums written	$311,847	$278,279	$2,166,440	$2,124,691	1,990,566
Reinsurance premiums ceded	(35,659)	(16,489)	(307,506)	(289,241)	(229,482)
Net premiums written	276,188	261,790	1,858,934	1,835,450	1,761,084
Change in unearned premiums	223,098	226,556	14,282	(33,307)	39
Net premiums earned	499,286	488,346	1,873,216	1,802,143	1,761,123
Losses and loss expenses	458,310	334,829	999,446	1,244,401	987,586
Policy acquisition costs	81,814	81,253	334,698	314,184	292,899
General and administrative expenses	65,095	52,253	263,652	197,497	209,290
Share compensation expenses	7,126	7,237	26,709	34,296	28,911
Total underwriting deductions	612,345	475,572	1,624,505	1,790,378	1,518,686
Underwriting (loss) income (b)	(113,059)	12,774	248,711	11,765	242,437
Net investment income	28,802	28,080	107,936	112,296	134,103
Other income	187	3,517	22,396	5,718	5,219
Finance expenses	(14,510)	(13,520)	(53,857)	(54,817)	(55,870)
Operating (loss) income before taxes and (loss) income from operating affilites (b)	(98,580)	30,851	325,186	74,962	325,889
Tax (expense) benefit	(615)	226	(2,501)	(824)	(3,126)
(Loss) income from operating affiliates	(614)	—	12,580	—	—
Net operating (loss) income (b)	(99,809)	31,077	335,265	74,138	322,763
Gain on bargain purchase, net of expenses (c)	21,485	—	17,701	—	—
Net realized (losses) gains on investments	(4,516)	5,355	18,233	28,532	32,498
Net unrealized (losses) gains on investments	(35,857)	2,159	17,585	(19,991)	45,952
(Loss) from investment affiliate	(406)	—	(964)	—	—
Foreign exchange gains (losses)	1,181	266	4,798	(22,124)	1,351
Transaction expenses (d)	—	(3,850)	—	(17,433)	—
Net (loss) income	(117,922)	35,007	392,618	43,122	402,564
Net loss (income) attributable to noncontrolling interest	27,206	(7,683)	15,820	(21,793)	—
Net (loss) income (attributable) available to Validus	$(90,716)	$27,324	$408,438	$21,329	$402,564
Selected ratios:					
Net premiums written / Gross premiums written	88.6 %	94.1 %	85.8 %	86.4 %	88.5 %
Losses and loss expenses	91.8 %	68.6 %	53.4 %	69.1 %	56.1 %
Policy acquisition costs	16.4 %	16.6 %	17.9 %	17.4 %	16.6 %
General and administrative expenses (e)	14.5 %	12.2 %	15.5 %	12.9 %	13.5 %
Expense ratio	30.9 %	28.8 %	33.4 %	30.3 %	30.1 %
Combined ratio	122.7 %	97.4 %	86.8 %	99.4 %	86.2 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

(b) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income and operating income that are not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. Reconciliations of these measures to the most comparable U.S. GAAP financial measure, are presented in the section below entitled “Underwriting Income.”

(c) The gain on bargain purchase, net of expenses, arises from the acquisition of Flagstone on November 30, 2012 and is net of transaction related expenses.

(d) The transaction expenses relate to costs incurred in connection with the Company’s proposed acquisition of Transatlantic. Transaction expenses are primarily comprised of legal, financial advisory and audit related services.

(e) The general and administrative expense ratio includes share compensation expenses.

Table of Contents

	Three Months Ended December 31,		Years Ended December 31,		
(Dollars in thousands)	2012 (a)	2011	2012 (a)	2011	2010
Validus Re					
Gross premiums written	$79,233	$55,851	$1,131,959	$1,114,493	$1,089,443
Reinsurance premiums ceded	(7,074)	(49)	(144,578)	(150,718)	(63,147)
Net premiums written	72,159	55,802	987,381	963,775	1,026,296
Change in unearned premiums	213,105	196,679	35,890	2,150	13,822
Net premiums earned	285,264	252,481	1,023,271	965,925	1,040,118
Losses and loss expenses	331,130	215,903	575,416	749,305	601,610
Policy acquisition costs	40,703	39,227	154,362	154,582	159,527
General and administrative expenses	14,716	11,716	63,048	44,663	45,613
Share compensation expenses	1,849	2,191	7,763	9,309	7,181
Total underwriting deductions	388,398	269,037	800,589	957,859	813,931
Underwriting (loss) income (b)	(103,134)	(16,556)	222,682	8,066	226,187
AlphaCat					
Gross premiums written	$(4)	$(1,323)	$21,603	$75,727	$11,796
Reinsurance premiums ceded	—	—	—	—	—
Net premiums written	(4)	(1,323)	21,603	75,727	11,796
Change in unearned premiums	5,895	27,834	(3,937)	(9,761)	(714)
Net premiums earned	5,891	26,511	17,666	65,966	11,082
Losses and loss expenses	—	10,000	—	10,000	—
Policy acquisition costs	589	3,331	1,774	7,946	1,072
General and administrative expenses	2,011	6,807	7,532	10,929	5,327
Share compensation expenses	84	33	279	107	594
Total underwriting deductions	2,684	20,171	9,585	28,982	6,993
Underwriting income (b)	3,207	6,340	8,081	36,984	4,089
Legal Entity adjustments					
Gross premiums written	$7	$—	$7	$—	$—
Reinsurance premiums ceded	—	—	—	—	—
Net premiums written	7	—	7	—	—
Change in unearned premiums	(3,833)	—	(3,833)	—	—
Net premiums earned	(3,826)	—	(3,826)	—	—
Losses and loss expenses	—	—	—	—	—
Policy acquisition costs	(365)	(1,093)	(390)	(2,394)	—
General and administrative expenses	1,673	(5,438)	5,130	(1,658)	15,927
Share compensation expenses	115	196	561	982	80
Total underwriting deductions	1,423	(6,335)	5,301	(3,070)	16,007
Underwriting (loss) income (b)	(5,249)	6,335	(9,127)	3,070	(16,007)
Talbot					
Gross premiums written	$241,100	$235,242	$1,078,636	$1,014,122	$981,073
Reinsurance premiums ceded	(37,067)	(27,931)	(228,686)	(218,174)	(258,081)
Net premiums written	204,033	207,311	849,950	795,948	722,992
Change in unearned premiums	4,098	2,043	(17,671)	(25,696)	(13,069)
Net premiums earned	208,131	209,354	832,279	770,252	709,923
Losses and loss expenses	127,180	108,926	424,030	485,096	385,976
Policy acquisition costs	41,745	41,160	183,926	157,334	143,769
General and administrative expenses	32,371	29,676	133,281	112,072	107,557
Share compensation expenses	2,442	1,934	7,789	8,582	6,923

Total underwriting deductions	203,738	181,696	749,026	763,084	644,225
Underwriting income (b)	4,393	27,658	83,253	7,168	65,698
Corporate & Eliminations					
Gross premiums written	$(8,489)	$(11,491)	$(65,765)	$(79,651)	$(91,746)
Reinsurance premiums ceded	8,482	11,491	65,758	79,651	91,746
Net premiums written	(7)	—	(7)	—	—
Change in unearned premiums	3,833	—	3,833	—	—
Net premiums earned	3,826	—	3,826	—	—
Losses and loss expenses	—	—	—	—	—
Policy acquisition costs	(858)	(1,372)	(4,974)	(3,284)	(11,469)
General and administrative expenses	14,324	9,492	54,661	31,491	34,866
Share compensation expenses	2,636	2,883	10,317	15,316	14,133
Total underwriting deductions	16,102	11,003	60,004	43,523	37,530
Underwriting (loss) (b)	(12,276)	(11,003)	(56,178)	(43,523)	(37,530)
Total underwriting (loss) income (b)	$(113,059)	$12,774	$248,711	$11,765	$242,437

Table of Contents

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

(b) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income that is not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of this measure to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled "Underwriting Income."

Three Months Ended December 31, 2012 compared to Three Months Ended December 31, 2011

Net loss attributable to Validus for the three months ended December 31, 2012 was $(90.7) million compared to net income available to Validus of $27.3 million for the three months ended December 31, 2011, a decrease of $118.0 million or 432.0%.

The primary factors driving the net loss attributable to Validus were:

- Decrease in underwriting income of $125.8 million primarily due to:
- A $123.5 million increase in loss and loss expenses;
- A $12.8 million increase in general and administrative expenses; and
- Offset by a $10.9 million increase in net premiums earned.

- Unfavorable movements in net realized and unrealized losses on investments of $9.9 million and $38.0 million, respectively.

The above items were partially offset by the following factors:

- Gain on bargain purchase, net of expenses and transaction expenses of $21.5 million; and

- Net loss attributable to noncontrolling interest which resulted in an increase to net income attributable to Validus of $34.9 million.

The change in net income available to Validus for the three months ended December 31, 2012 of $118.0 million as compared to the three months ended December 31, 2011 is described in the following table:

	Three Months Ended December 31, 2012 Increase (Decrease) Over the Three Months Ended December 31, 2011 (a)				
(Dollars in thousands)	Validus Re (a)	AlphaCat	Talbot	Corporate and Eliminations (b)	Total
Notable losses—(increase) in net loss and loss expenses (c)	$(259,639)	$—	$(47,249)	$—	$(306,888)
Less: Notable losses—increase in net reinstatement premium (c)	33,177	—	4,540	—	37,717
Other underwriting income (loss)	139,884	(3,133)	19,444	(12,857)	143,338
Underwriting (loss) income (d)	(86,578)	(3,133)	(23,265)	(12,857)	(125,833)
Net investment income	(535)	528	(1,132)	1,861	722
Other income	(2,311)	(5,076)	(1,291)	5,348	(3,330)
Finance expenses	(462)	(1,043)	75	440	(990)
Operating (loss) income before taxes and (loss) from operating affiliates	(89,886)	(8,724)	(25,613)	(5,208)	(129,431)
Tax (expense) benefit	(152)	—	(1,776)	1,087	(841)
(Loss) from operating affiliates	—	(614)	—	—	(614)
Net operating (loss) income	(90,038)	(9,338)	(27,389)	(4,121)	(130,886)
Gain on bargain purchase, net of expenses	—	—	—	21,485	21,485
Net realized (losses) on investments	(9,367)	—	(504)	—	(9,871)

Net unrealized (losses) gains on investments	(4,266)	(31,819)	(1,932)	1	(38,016)
(Loss) from investment affiliate	(406)	—	—	—	(406)
Foreign exchange gains (losses)	413	136	749	(383)	915
Transaction expenses	—	—	—	3,850	3,850
Net (loss) income	(103,664)	(41,021)	(29,076)	20,832	(152,929)
Net loss (income) attributable to noncontrolling interest	—	34,889	—	—	34,889
Net (loss) income (attributable) available to Validus	$(103,664)	$(6,132)	$(29,076)	$20,832	$(118,040)

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.
(b) The Corporate and Eliminations column includes legal entity adjustments.
(c) Notable losses for the three months ended December 31, 2012 include: Hurricane Sandy. Notable losses for the three months ended December 31, 2011 include: the Thai floods and excludes the reserve for potential development on 2011 notable loss events. The AlphaCat segment's non-consolidated

affiliates incurred loss and loss expenses of $8.4 million related to Hurricane Sandy for the three months ended December 31, 2012. These losses are not included in the table above as the entities are accounted for as investments in operating affiliates.

(d) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income (loss) that is not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of this measure to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled "Underwriting Income."

Gross Premiums Written

Gross premiums written for the three months ended December 31, 2012 were $311.8 million compared to $278.3 million for the three months ended December 31, 2011, an increase of $33.6 million or 12.1%. The property and marine lines increased by $37.4 million and $5.1 million, respectively, while the specialty lines decreased by $8.9 million. Details of gross premiums written by line of business are provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012 (a) Gross Premiums Written	Gross Premiums Written (%)	Three Months Ended December 31, 2011 Gross Premiums Written	Gross Premiums Written (%)	% Change
Property	$110,561	35.4 %	$73,200	26.3 %	51.0 %
Marine	89,394	28.7 %	84,247	30.3 %	6.1 %
Specialty	111,892	35.9 %	120,832	43.4 %	(7.4)%
Total	$311,847	100.0 %	$278,279	100.0 %	12.1 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re. Validus Re gross premiums written for the three months ended December 31, 2012 were $79.2 million compared to $55.9 million for the three months ended December 31, 2011, an increase of $23.4 million or 41.9%. Details of Validus Re gross premiums written by line of business are provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012 (a) Gross Premiums Written	Gross Premiums Written (%)	Three Months Ended December 31, 2011 Gross Premiums Written	Gross Premiums Written (%)	% Change
Property	$54,878	69.2 %	$34,053	61.0 %	61.2 %
Marine	8,621	10.9 %	9,742	17.4 %	(11.5)%
Specialty	15,734	19.9 %	12,056	21.6 %	30.5 %
Total	$79,233	100.0 %	$55,851	100.0 %	41.9 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

The increase in gross premiums written in the property lines of $20.8 million was due primarily to an increase in reinstatement premiums of $28.0 million primarily due to Hurricane Sandy and a $7.4 million increase in premiums relating to the Flagstone acquisition, slightly offset by a decrease in per risk excess of loss treaties of $5.1 million. The decrease in gross premiums written of $1.1 million in the marine lines was due primarily to a $6.8 million decrease in premium adjustments on proportional treaties, partially offset by an increase in reinstatement premiums of $4.1 million primarily on Hurricane Sandy. The increase in gross premiums written in the specialty lines of $3.7 million was due primarily to a $3.1 million increase in premiums relating to the Flagstone acquisition and a $2.5 million increase in per risk excess of loss treaties and premium adjustments on proportional treaties, slightly offset by a $2.2 million decrease in premium adjustments relating to non-proportional treaties.

Gross premiums written under the quota share, surplus treaty and excess of loss contracts with Talbot for the three months ended December 31, 2012 were $8.5 million compared to $11.5 million for the three months ended December 31, 2011, a decrease of by $3.0 million as compared to the three months ended December 31, 2011. These reinsurance transactions with Talbot are eliminated upon consolidation.

AlphaCat. AlphaCat gross premiums written for the three months ended December 31, 2012 were $0.0 million compared to $(1.3) million for the three months ended December 31, 2011, an increase of $1.3 million or 99.7%. The AlphaCat segment generally does not write premiums in the fourth quarter.

The increase in gross premiums written in the property lines of $1.3 million was due primarily to the change in accounting treatment for AlphaCat Re 2011 which occurred as at December 31, 2011, when the individual assets and liabilities and corresponding noncontrolling interest of AlphaCat Re 2011 were derecognized from the consolidated Balance Sheet of the

Table of Contents

Company. AlphaCat Re 2011 was consolidated in 2011 whereas in 2012, AlphaCat Re 2011 is accounted for as an equity method operating affiliate.

Managed gross premiums written from our non-consolidated affiliates, AlphaCat Re 2011 and AlphaCat Re 2012, for the three months ended December 31, 2012 were $0.0 million compared to $(1.4) million for the three months ended December 31, 2011, an increase of $1.3 million or 97.3%. Gross premiums written from our consolidated AlphaCat entities for the three months ended December 31, 2012 were $0.0 million compared to $0.1 million for the three months ended December 31, 2011, a decrease of $0.1 million or 106.5%.

Talbot. Talbot gross premiums written for the three months ended December 31, 2012 were $241.1 million compared to $235.2 million for the three months ended December 31, 2011, an increase of $5.9 million or 2.5%. The $241.1 million of gross premiums written translated at 2011 rates of exchange would have been $240.9 million during the three months ended December 31, 2012, giving an effective increase of $5.7 million or 2.4%. Details of Talbot gross premiums written by line of business are provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012 Gross Premiums Written	Gross Premiums Written (%)	Three Months Ended December 31, 2011 Gross Premiums Written	Gross Premiums Written (%)	% Change
Property	$62,258	25.8 %	$51,793	22.0 %	20.2 %
Marine	81,540	33.8 %	74,235	31.6 %	9.8 %
Specialty	97,302	40.4 %	109,214	46.4 %	(10.9)%
Total	$241,100	100.0 %	$235,242	100.0 %	2.5 %

The increase in gross premiums written in the property lines of $10.5 million was due primarily to a $6.4 million increase in premiums written in the direct property lines and a $4.2 million increase in the construction lines, partially offset by a $1.0 million decrease in property treaty lines. The increase in gross premiums written in the marine lines of $7.3 million was due primarily to a $5.1 million increase in premiums written in the cargo lines and a $5.1 million increase in the other treaty lines, $3.5 million of which relates to reinstatement premiums on Hurricane Sandy. These were partially offset by a $2.5 million decrease in yachts lines. The decrease in gross premiums written in the specialty lines of $11.9 million was due primarily to a $12.2 million decrease in premiums written in the direct aviation and aviation treaty lines. This decrease primarily relates to a premium reassessment of $8.2 million which has no net earned impact on the direct aviation and aviation treaty lines. In addition, there was a $2.9 million decrease in the war lines, partially offset by a $3.7 million increase in the political violence lines.

Reinsurance Premiums Ceded

Reinsurance premiums ceded for the three months ended December 31, 2012 were $35.7 million compared to $16.5 million for the three months ended December 31, 2011, an increase of $19.2 million or 116.3%. Details of reinsurance premiums ceded by line of business are provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012 (a) Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)	Three Months Ended December 31, 2011 Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)	% Change
Property	$19,644	55.1 %	$11,979	72.7 %	64.0 %
Marine	4,890	13.7 %	(1,363)	(8.3)%	458.8 %
Specialty	11,125	31.2 %	5,873	35.6 %	89.4 %
Total	$35,659	100.0 %	$16,489	100.0 %	116.3 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re. Validus Re reinsurance premiums ceded for the three months ended December 31, 2012 were $7.1 million compared to $0.0 million for the three months ended December 31, 2011, an increase of $7.0 million. Details of Validus Re reinsurance premiums ceded by line of business are provided below.

Table of Contents

(Dollars in thousands)	Three Months Ended December 31, 2012 (a) Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)	Three Months Ended December 31, 2011 Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)	% Change
Property	$4,275	60.5 %	$980	2,000.0 %	336.2 %
Marine	2,803	39.6 %	(931)	(1,900.0)%	401.1 %
Specialty	(4)	(0.1)%	—	— %	NM
Total	$7,074	100.0 %	$49	100.0 %	NM

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.
NM: Not meaningful

Reinsurance premiums ceded in the property lines increased by $3.3 million, due primarily to increases in ceded reinstatement premiums and non-proportional coverage of $2.2 million and $1.4 million, respectively. The increase in reinsurance premiums of $3.7 million ceded in the marine lines was primarily due to a $1.4 million increase in non-proportional coverage and $1.3 million of adjustments to coverage from prior periods.

AlphaCat. AlphaCat did not cede reinsurance premiums for the three months ended December 31, 2012 and 2011.

Talbot. Talbot reinsurance premiums ceded for the three months ended December 31, 2012 were $37.1 million compared to $27.9 million for the three months ended December 31, 2011, an increase of $9.1 million or 32.7%. Details of Talbot reinsurance premiums ceded by line of business are provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012 Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)	Three Months Ended December 31, 2011 Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)	% Change
Property	$21,940	59.2 %	$22,322	79.9 %	(1.7)%
Marine	2,854	7.7 %	(702)	(2.5)%	506.6 %
Specialty	12,273	33.1 %	6,311	22.6 %	94.5 %
Total	$37,067	100.0 %	$27,931	100.0 %	32.7 %

The increase in reinsurance premiums ceded in the marine lines of $3.6 million was due primarily to a $5.5 million increase in premiums ceded in the marine energy and cargo lines, $5.2 million of which relates to reinstatement premiums, partially offset by a $2.1 million decrease in other marine lines. The increase in reinsurance premiums ceded in the specialty lines of $6.0 million was due primarily to a $3.0 million increase in premiums ceded in the war, political risk and violence lines and a $2.0 million increase in financial institution lines, mainly due to higher reinstatement premiums and prior period adjustments.

Reinsurance premiums ceded under the quota share, surplus treaty and excess of loss contracts with Validus Re for the three months ended December 31, 2012 were $8.5 million compared to $11.5 million for the three months ended December 31, 2011, a decrease of $3.0 million. These reinsurance agreements with Validus Re are eliminated upon consolidation.

Net Premiums Written

Net premiums written for the three months ended December 31, 2012 were $276.2 million compared to $261.8 million for the three months ended December 31, 2011, an increase of $14.4 million or 5.5%. The ratios of net premiums written to gross premiums written for the three months ended December 31, 2012 and 2011 were 88.6% and 94.1%, respectively. Details of net premiums written by line of business are provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012 (a) Net Premiums Written	Net Premiums Written (%)	Three Months Ended December 31, 2011 Net Premiums Written	Net Premiums Written (%)	% Change
Property	$90,917	32.9 %	$61,221	23.4 %	48.5 %
Marine	84,504	30.6 %	85,610	32.7 %	(1.3)%

Specialty	100,767	36.5 %	114,959	43.9 %	(12.3	)%
Total	$276,188	100.0 %	$261,790	100.0 %	5.5	%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Table of Contents

Validus Re. Validus Re net premiums written for the three months ended December 31, 2012 were $72.2 million compared to $55.8 million for the three months ended December 31, 2011, an increase of $16.4 million or 29.3%. Details of Validus Re net premiums written by line of business are provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012 (a)		Three Months Ended December 31, 2011		
	Net Premiums Written	Net Premiums Written (%)	Net Premiums Written	Net Premiums Written (%)	% Change
Property	$50,603	70.1 %	$33,073	59.3 %	53.0 %
Marine	5,818	8.1 %	10,673	19.1 %	(45.5)%
Specialty	15,738	21.8 %	12,056	21.6 %	30.5 %
Total	$72,159	100.0 %	$55,802	100.0 %	29.3 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

The increase in Validus Re net premiums written was driven by the factors highlighted above in respect of gross premiums written and reinsurance premiums ceded. The ratios of net premiums written to gross premiums written were 91.1% and 99.9% for the three months ended December 31, 2012 and 2011, respectively.

AlphaCat. AlphaCat net premiums written for the three months ended December 31, 2012 were $0.0 million compared to $(1.3) million for the three months ended December 31, 2011, an increase of $1.3 million or 99.7%.

The increase in AlphaCat net premiums written was driven by the factors highlighted above in respect of gross premiums written. The ratios of net premiums written to gross premiums written were 100.0% for the three months ended December 31, 2012 and 2011.

Talbot. Talbot net premiums written for the three months ended December 31, 2012 were $204.0 million compared to $207.3 million for the three months ended December 31, 2011, a decrease of $3.3 million or 1.6%. Details of Talbot net premiums written by line of business are provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012		Three Months Ended December 31, 2011		
	Net Premiums Written	Net Premiums Written (%)	Net Premiums Written	Net Premiums Written (%)	% Change
Property	$40,318	19.8 %	$29,471	14.2 %	36.8 %
Marine	78,686	38.5 %	74,937	36.1 %	5.0 %
Specialty	85,029	41.7 %	102,903	49.7 %	(17.4)%
Total	$204,033	100.0 %	$207,311	100.0 %	(1.6)%

The decrease in net premiums written was driven by the factors highlighted above in respect of gross premiums written and reinsurance premiums ceded. The ratios of net premiums written to gross premiums written for the three months ended December 31, 2012 and 2011 were 84.6% and 88.1%, respectively.

Net Change in Unearned Premiums

Net change in unearned premiums for the three months ended December 31, 2012 was $223.1 million compared to $226.6 million for the three months ended December 31, 2011, a decrease of $3.5 million or 1.5%.

Table of Contents

(Dollars in thousands)	Three Months Ended December 31, 2012 (a) Net Change in Unearned Premiums	Three Months Ended December 31, 2011 Net Change in Unearned Premiums	% Change
Change in gross unearned premium	$140,243	$286,211	(51.0)%
Less change due to Flagstone acquisition	139,389	—	NM
Deconsolidation of AlphaCat Re 2011	—	(9,405)	NM
Net change in gross unearned premium	279,632	276,806	1.0%
Change in prepaid reinsurance premium	(45,195)	(50,250)	(10.1)%
Less change due to Flagstone acquisition	(11,339)	—	NM
Net change in prepaid reinsurance premiums	(56,534)	(50,250)	12.5%
Net change in unearned premium	$223,098	$226,556	(1.5)%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

NM: Not meaningful

Validus Re. Validus Re's net change in unearned premiums for the three months ended December 31, 2012 was $213.1 million compared to $196.7 million for the three months ended December 31, 2011, an increase of $16.4 million or 8.4%.

(Dollars in thousands)	Three Months Ended December 31, 2012 (a) Net Change in Unearned Premiums	Three Months Ended December 31, 2011 Net Change in Unearned Premiums	% Change
Change in gross unearned premium	$110,621	$228,747	(51.6)%
Less change due to Flagstone acquisition	139,389	—	NM
Deconsolidation of AlphaCatRe 2011	—	(9,405)	NM
Net change in gross unearned premium	250,010	219,342	14.0%
Change in prepaid reinsurance premium	(25,566)	(22,663)	(12.8)%
Less change due to Flagstone acquisition	(11,339)	—	NM
Net change in prepaid reinsurance premiums	(36,905)	(22,663)	(62.8)%
Net change in unearned premium	$213,105	$196,679	8.4%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

NM: Not meaningful

Validus Re net change in unearned premiums has increased for the three months ended December 31, 2012 due to the earnings pattern of gross premiums written and reinsurance premiums ceded.

AlphaCat. AlphaCat's net change in unearned premiums for the three months ended December 31, 2012 was $5.9 million compared to $27.8 million for the three months ended December 31, 2011, a decrease of $21.9 million or 78.8%.

(Dollars in thousands)	Three Months Ended December 31, 2012 Net Change in Unearned Premiums	Three Months Ended December 31, 2011 Net Change in Unearned Premiums	% Change

Change in gross unearned premiums	$ 5,895	$ 27,834	(78.8	)%
Net change in unearned premiums	$ 5,895	$ 27,834	(78.8	)%

AlphaCat net change in unearned premiums has decreased for the three months ended December 31, 2012 due primarily to the deconsolidation of AlphaCat Re 2011 and the earnings pattern of gross premiums written.

Table of Contents

Talbot. Talbot's net change in unearned premiums for the three months ended December 31, 2012 was $4.1 million compared to $2.0 million for the three months ended December 31, 2011, an increase of $2.1 million or 100.6%.

(Dollars in thousands)	Three Months Ended December 31, 2012 Net Change in Unearned Premiums	Three Months Ended December 31, 2011 Net Change in Unearned Premiums	% Change
Change in gross unearned premiums	$ 23,727	$ 29,630	(19.9)%
Change in prepaid reinsurance premiums	(19,629)	(27,587)	28.8 %
Net change in unearned premiums	$ 4,098	$ 2,043	100.6 %

Talbot's net change in unearned premium has increased for the three months ended December 31, 2012 due to the earnings pattern of gross premiums written and reinsurance premiums ceded.

Net Premiums Earned

Net premiums earned for the three months ended December 31, 2012 were $499.3 million compared to $488.3 million for the three months ended December 31, 2011, an increase of $10.9 million or 2.2%. Details of net premiums earned by line of business are provided below.

	Three Months Ended December 31, 2012 (a)		Three Months Ended December 31, 2011		
(Dollars in thousands)	Net Premiums Earned	Net Premiums Earned (%)	Net Premiums Earned	Net Premiums Earned (%)	% Change
Property	$250,480	50.2 %	$236,671	48.5 %	5.8 %
Marine	146,744	29.4 %	146,953	30.1 %	(0.1)%
Specialty	102,062	20.4 %	104,722	21.4 %	(2.5)%
Total	$499,286	100.0 %	$488,346	100.0 %	2.2 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re. Validus Re net premiums earned for three months ended December 31, 2012 were $285.3 million compared to $252.5 million for the three months ended December 31, 2011, an increase of $32.8 million or 13.0%. Details of Validus Re net premiums earned by line of business are provided below.

	Three Months Ended December 31, 2012 (a)		Three Months Ended December 31, 2011		
(Dollars in thousands)	Net Premiums Earned	Net Premiums Earned (%)	Net Premiums Earned	Net Premiums Earned (%)	% Change
Property	$198,002	69.4 %	$169,052	67.0 %	17.1 %
Marine	60,163	21.1 %	57,524	22.8 %	4.6 %
Specialty	27,099	9.5 %	25,905	10.2 %	4.6 %
Total	$285,264	100.0 %	$252,481	100.0 %	13.0 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

The overall increase in net premiums earned was due primarily to the increase in reinstatement premiums relating to Hurricane Sandy and an increase in net premiums earned relating to the acquisition of Flagstone. The increase in premiums earned in the property lines of $29.0 million is due primarily to the increase in earned reinstatement premiums of $25.7 million relating primarily to Hurricane Sandy and a $20.9 million increase in premiums earned relating to the acquisition of Flagstone. These items are partially offset by a $10.3 million decrease in intercompany premiums with Talbot which are eliminated upon consolidation and a $6.0 million decrease in assumed earned premium.The increase in premiums earned in the marine lines of $2.6 million is due primarily to an increase in earned reinstatement premiums of $3.1 million relating primarily to Hurricane Sandy and a $1.6 million premiums earned relating to the Flagstone acquisition, partially offset by a $3.6 million decrease in premium adjustments on proportional business. These increases are consistent with the relevant pattern of net premiums written influencing the earned premiums for the three months ended December 31, 2012 compared to the three months ended December 31, 2011.

AlphaCat. AlphaCat net premiums earned for the three months ended December 31, 2012 were $5.9 million compared to $26.5 million for the three months ended December 31, 2011, a decrease of $20.6 million or 77.8%. Details of AlphaCat net premiums earned by line of business are provided below.

Table of Contents

(Dollars in thousands)	Three Months Ended December 31, 2012 Net Premiums Earned	Net Premiums Earned (%)	Three Months Ended December 31, 2011 Net Premiums Earned	Net Premiums Earned (%)	% Change
Property	$5,891	100.0 %	$26,511	100.0 %	(77.8)%
Total	$5,891	100.0 %	$26,511	100.0 %	(77.8)%

The decrease in net premiums earned is consistent with the relevant pattern of net premiums written and the deconsolidation of AlphaCatRe 2011, influencing the earned premiums for the three months ended December 31, 2012 compared to the three months ended December 31, 2011.

Talbot. Talbot net premiums earned for the three months ended December 31, 2012 were $208.1 million compared to $209.4 million for the three months ended December 31, 2011, a decrease of $1.2 million or 0.6%. Details of Talbot net premiums earned by line of business are provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012 Net Premiums Earned	Net Premiums Earned (%)	Three Months Ended December 31, 2011 Net Premiums Earned	Net Premiums Earned (%)	% Change
Property	$46,587	22.4 %	$41,108	19.6 %	13.3 %
Marine	86,581	41.6 %	89,429	42.8 %	(3.2)%
Specialty	74,963	36.0 %	78,817	37.6 %	(4.9)%
Total	$208,131	100.0 %	$209,354	100.0 %	(0.6)%

The decrease in net premiums earned is consistent with the relevant patterns of net premiums written influencing the earned premiums for the three months ended December 31, 2012, as compared to the three months ended December 31, 2011.

Losses and Loss Expenses

Losses and loss expenses for the three months ended December 31, 2012 were $458.3 million compared to $334.8 million for the three months ended December 31, 2011, an increase of $123.5 million or 36.9%. The loss ratios, defined as losses and loss expenses divided by net premiums earned, for the three months ended December 31, 2012 and 2011 were 91.8% and 68.6%, respectively. Details of loss ratios by line of business are provided below.

	Three Months Ended December 31, 2012 (a)	Three Months Ended December 31, 2011	Percentage Point Change
Property	126.0 %	90.0 %	36.0
Marine	76.2 %	53.0 %	23.2
Specialty	30.2 %	42.0 %	(11.8)
All lines	91.8 %	68.6 %	23.2

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

For the three months ended December 31, 2012, the Company incurred $361.0 million of losses from notable loss events, which represented 72.3 percentage points of the overall loss ratio. Net of $36.4 million of reinstatement premiums, the effect of these events on net income was a decrease of $324.6 million. For the three months ended December 31, 2011, the Company incurred $54.1 million of losses from notable loss events, which represented 11.1 percentage points of the overall loss ratio, excluding the reserve for potential development on notable loss events. Including the impact of $(1.3) million of reinstatement premiums, the effect of these events on net income was a decrease of $55.5 million. The Company's loss ratio, excluding notable loss events, reserve for potential development on notable loss events and prior year loss reserve development for the three months ended December 31, 2012 and 2011 was 31.0% and 50.3%, respectively.

Table of Contents

		Three Months Ended December 31, 2012 (b) (Dollars in thousands)								
Fourth Quarter 2012 Notable Loss Events (a) (b)		Validus Re (b)			Talbot			Total		
(Dollars in thousands)	Description	Net Losses and Loss Expenses(c)	% of NPE		Net Losses and Loss Expenses(c)	% of NPE		Net Losses and Loss Expenses(c)	% of NPE	
Hurricane Sandy (d)	Windstorm	$282,603	99.1	%	$78,433	37.7	%	$361,036	72.3	%
Total		$282,603	99.1	%	$78,433	37.7	%	$361,036	72.3	%

		Three Months Ended December 31, 2011 (Dollars in thousands)								
Fourth Quarter 2011 Notable Loss Events (a)		Validus Re			Talbot			Total		
(Dollars in thousands)	Description	Net Losses and Loss Expenses(c)	% of NPE		Net Losses and Loss Expenses(c)	% of NPE		Net Losses and Loss Expenses(c)	% of NPE	
Thailand floods	Multiple flooding events	$22,964	9.1	%	$31,184	14.9	%	$54,148	11.1	%
Total		$22,964	9.1	%	$31,184	14.9	%	$54,148	11.1	%

(a) These notable loss event amounts exclude the reserve for potential development on 2011 notable loss events and are based on management’s estimates following a review of the Company’s potential exposure and discussions with certain clients and brokers. Given the magnitude and recent occurrence of these events in relation to the corresponding period end date, and other uncertainties inherent in loss estimation, meaningful uncertainty exists at the relevant reporting date regarding losses from these events and the Company’s actual ultimate net losses from these events can vary materially from these estimates.

(b) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

(c) Net of reinsurance but not of reinstatement premiums. Total reinstatement premiums were $36.4 million and $(1.3) million for the three months ended December 31, 2012 and December 31, 2011, respectively.

(d) The AlphaCat segment's non-consolidated affiliates incurred loss and loss expenses of $8.4 million related to Hurricane Sandy for the three months ended December 31, 2012. These losses are not included in the table above as the entities are accounted for as investments in operating affiliates.

Table of Contents

Details of loss ratios by line of business and period of occurrence are provided below.

	Three Months Ended December 31,		
	2012 (a)	2011	Percentage Point Change
Property—current period—excluding items below	21.0 %	46.9 %	(25.9)
Property—current period—notable losses	113.2 %	20.3 %	92.9
Property—current period—reserve for potential development on notable loss events	0.0 %	30.8 %	(30.8)
Property—change in prior accident years	(8.2)%	(8.0)%	(0.2)
Property—loss ratio	126.0 %	90.0 %	36.0
Marine—current period—excluding items below	42.8 %	53.8 %	(11.0)
Marine—current period—notable losses	47.5 %	2.9 %	44.6
Marine—current period—reserve for potential development on notable loss events	0.0 %	3.4 %	(3.4)
Marine—change in prior accident years	(14.1)%	(7.1)%	(7.0)
Marine—loss ratio	76.2 %	53.0 %	23.2
Specialty—current period—excluding items below	38.2 %	53.0 %	(14.8)
Specialty—current period—notable losses	7.7 %	1.8 %	5.9
Specialty—change in prior accident years	(15.7)%	(12.8)%	(2.9)
Specialty—loss ratio	30.2 %	42.0 %	(11.8)
All lines—current period—excluding items below	31.0 %	50.3 %	(19.3)
All lines—current period—notable losses	72.3 %	11.1 %	61.2
All lines—current period—reserve for potential development on notable loss events	0.0 %	16.0 %	(16.0)
All lines—change in prior accident years	(11.5)%	(8.8)%	(2.7)
All lines—loss ratio	91.8 %	68.6 %	23.2

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re. Validus Re losses and loss expenses for the three months ended December 31, 2012 were $331.1 million compared to $215.9 million for the three months ended December 31, 2011, an increase of $115.2 million or 53.4%. The loss ratio, defined as losses and loss expenses divided by net premiums earned, was 116.1% and 85.5% for the three months ended December 31, 2012 and 2011, respectively. For the three months ended December 31, 2012, Validus Re incurred losses of $350.9 million related to current year losses and $19.8 million of favorable loss reserve development relating to prior accident years. For three months ended December 31, 2012, favorable loss reserve development on prior accident years benefited the Validus Re loss ratio by 6.9 percentage points. For the three months ended December 31, 2011, Validus Re incurred losses of $223.0 million related to current year losses and $7.1 million of favorable loss reserve development relating to prior accident years. For the three months ended December 31, 2011, favorable loss reserve development on prior years benefited the Validus Re loss ratio by 2.8 percentage points.

For the three months ended December 31, 2012, Validus Re incurred $282.6 million of losses from notable loss events, which represented 99.1 percentage points of the overall loss ratio. Net of $34.8 million of reinstatement premiums, the effect of these events on net income was a decrease of $247.8 million. For the three months ended December 31, 2011, Validus Re incurred $23.0 million of losses from notable loss events, which represented 9.1 percentage points of the overall loss ratio, excluding the reserve for potential development on notable loss events. Net of reinstatement premiums of $1.6 million, the effect of these events on Validus Re segment income was a decrease of $21.4 million. Validus Re segment loss ratios excluding notable loss events, reserve for potential development on notable loss events and prior year loss reserve development for the three months ended December 31, 2012 and 2011 were 23.9% and 48.3%, respectively. Details of Validus Re loss ratios by line of business and period of occurrence are provided below.

Table of Contents

	Three Months Ended December 31,		
	2012 (a)	2011	Percentage Point Change
Property—current period excluding items below	18.7 %	39.3 %	(20.6)
Property—current period—notable losses	120.2 %	11.7 %	108.5
Property—current period—reserves for potential development on notable loss events	0.0 %	43.2 %	(43.2)
Property—change in prior accident years	(3.2)%	(2.8)%	(0.4)
Property—loss ratio	135.7 %	91.4 %	44.3
Marine—current period excluding items below	39.3 %	62.5 %	(23.2)
Marine—current period—notable losses	72.3 %	5.6 %	66.7
Marine—current period—reserves for potential development on notable loss events	0.0 %	8.7 %	(8.7)
Marine—change in prior accident years	(7.0)%	(0.5)%	(6.5)
Marine—loss ratio	104.6 %	76.3 %	28.3
Specialty—current period excluding items below	28.4 %	75.6 %	(47.2)
Specialty—current period—notable losses	4.2 %	0.0 %	4.2
Specialty—change in prior accident years	(34.4)%	(8.1)%	(26.3)
Specialty—loss ratio	(1.8)%	67.5 %	(69.3)
All lines—current period excluding items below	23.9 %	48.3 %	(24.4)
All lines—current period—notable losses	99.1 %	9.1 %	90.0
All lines—current period—reserves for potential development on notable loss events	0.0 %	30.9 %	(30.9)
All lines—change in prior accident years	(6.9)%	(2.8)%	(4.1)
All lines—loss ratio	116.1 %	85.5 %	30.6

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

For the three months ended December 31, 2012, Validus Re property lines losses and loss expenses included $274.9 million related to current year losses and $6.3 million of favorable loss reserve development relating to prior accident years. The favorable loss reserve development was due to a decrease in loss estimates on prior year notable loss events, as well as a reduction in loss estimates on attritional losses. For the three months ended December 31, 2011, Validus Re property lines losses and loss expenses included $159.3 million related to current year losses and $4.7 million of favorable loss reserve development relating to prior accident years.

For the three months ended December 31, 2012, Validus Re property lines incurred $237.9 million of losses from notable loss events, which represented 120.2 percentage points of the property lines loss ratio. Net of $29.5 million of reinstatement premiums, the effect of these events on net income was a decrease of $208.4 million. For the three months ended December 31, 2011, Validus Re property lines incurred $19.8 million of losses from notable loss events, which represented 11.7 percentage points of the property lines loss ratio, excluding reserve for potential development on notable loss events. Validus Re property lines loss ratios, excluding notable loss events, reserve for potential development on notable loss events and prior year loss reserve development, for the three months ended December 31, 2012 and 2011 were 18.7% and 39.3%, respectively.

For the three months ended December 31, 2012, Validus Re marine lines losses and loss expenses included $67.2 million related to current year losses and $4.2 million of favorable loss reserve development relating to prior accident years. The favorable loss reserve development was due primarily to a reduction in loss estimates on attritional losses, which was partially offset by an increase in prior year notable loss events. For the three months ended December 31, 2011, Validus Re marine lines losses and loss expenses included $44.2 million related to current year losses and $0.3 million of favorable loss reserve development relating to prior accident years.

For the three months ended December 31, 2012, Validus Re marine lines incurred $43.5 million of losses from notable loss events, which represented 72.3 percentage points of the marine lines loss ratio. Net of $5.2 million of reinstatement premiums, the effect of these events on net income was a decrease of $38.3 million. For the three months ended December 31, 2011, Validus Re marine lines incurred $3.2 million of losses from notable loss events, which represented 5.6 percentage points of the marine

lines loss ratio, excluding reserve for potential development on notable loss events. Validus Re marine lines loss ratios, excluding notable loss events, reserve for potential development on notable loss events and prior year loss reserve development, for the three months ended December 31, 2012 and 2011 were 39.3% and 62.5%, respectively.
For the three months ended December 31, 2012, Validus Re specialty lines losses and loss expenses included $8.8 million related to current year losses and $9.3 million of favorable loss reserve development relating to prior accident years. The favorable loss reserve development was due primarily to a reduction in loss estimates on attritional losses.
For the three months ended December 31, 2011, Validus Re specialty lines losses and loss expenses included $19.6 million related to current year losses and $2.1 million of favorable loss reserve development relating to prior accident years.
For the three months ended December 31, 2012 and 2011, Validus Re specialty lines incurred $1.1 million of losses from notable loss events which represented 4.2 percentage points of the specialty lines loss ratio. Validus Re specialty lines loss ratios, excluding prior year loss reserve development, for the three months ended December 31, 2012 and 2011 were 28.4% and 75.6%, respectively.
The net negative financial impact from Hurricane Sandy to Flagstone for the year ended December 31, 2012 was $39.1 million. The financial impact to Flagstone did not impact Validus' results of operations in the fourth quarter 2012 as the loss event took place prior to the date of Validus' acquisition of Flagstone which was completed on November 30, 2012.

AlphaCat. AlphaCat contributed $nil to the losses and loss expenses for the three months ended December 31, 2012 compared to $10.0 million for the three months ended December 31, 2011, a decrease of $10.0 million or 100.0%. The loss ratio defined as losses and loss expenses divided by net premiums earned, was nil% and 37.7% for the three months ended December 31, 2012 and 2011, respectively. For the three months ended December 31, 2012, AlphaCat Re 2011 and AlphaCat Re 2012 incurred Hurricane Sandy net losses of $25.0 million and $7.5 million, respectively. The AlphaCat segment's portion of incurred losses and loss expenses related to Hurricane Sandy was $8.4 million for the year ended December 31, 2012 and are included in 'income from operating affiliates'.
Talbot. Talbot losses and loss expenses for the three months ended December 31, 2012 were $127.2 million compared to $108.9 million for the three months ended December 31, 2011, an increase of $18.3 million or 16.8%. The loss ratio defined as losses and loss expenses divided by net premiums earned, was 61.1% and 52.0% for the three months ended December 31, 2012 and 2011, respectively. For the three months ended December 31, 2012, Talbot incurred losses of $164.6 million related to current year losses and $37.4 million of favorable loss reserve development relating to prior accident years. For the three months ended December 31, 2012, favorable loss reserve development on prior accident years benefited the Talbot loss ratio by 18.0 percentage points. For the three months ended December 31, 2011, Talbot incurred losses of $144.6 million related to current year losses and $35.7 million in favorable loss reserve development relating to prior accident years. For the three months ended December 31, 2011, favorable loss reserve development on prior accident years benefited the Talbot loss ratio by 17.0 percentage points.
For the three months ended December 31, 2012, Talbot incurred $78.4 million of losses from notable loss events, which represented 37.7 percentage points of the overall loss ratio. Net of $1.6 million of reinstatement premiums, the effect of these events on net income was a decrease of $76.8 million. For the three months ended December 31, 2011, Talbot incurred $31.2 million of losses from notable loss events, which represented 14.9 percentage points of the overall loss ratio. Talbot loss ratios, excluding notable loss events and prior year loss reserve development, for the three months ended December 31, 2012 and 2011 were 41.4% and 54.1%, respectively. Details of Talbot loss ratios by line of business and period of occurrence are provided below.

	Three Months Ended December 31,		
	2012	2011	Percentage Point Change
Property—current period excluding items below	33.5 %	83.8 %	(50.3)
Property—current period—notable losses	97.8 %	68.9 %	28.9
Property—change in prior accident years	(30.5)%	(34.8)%	4.3
Property—loss ratio	100.8 %	117.9 %	(17.1)
Marine—current period excluding items below	45.3 %	48.2 %	(2.9)
Marine—current period—notable losses	30.2 %	1.1 %	29.1
Marine—change in prior accident years	(19.0)%	(11.3)%	(7.7)
Marine—loss ratio	56.5 %	38.0 %	18.5
Specialty—current period excluding items below	41.8 %	45.6 %	(3.8)
Specialty—current period—notable losses	8.9 %	2.3 %	6.6
Specialty—change in prior accident years	(8.9)%	(14.3)%	5.4
Specialty—loss ratio	41.8 %	33.6 %	8.2
All lines—current period excluding items below	41.4 %	54.1 %	(12.7)
All lines—current period—notable losses	37.7 %	14.9 %	22.8
All lines—change in prior accident years	(18.0)%	(17.0)%	(1.0)
All lines—loss ratio	61.1 %	52.0 %	9.1

For the three months ended December 31, 2012, Talbot property lines losses and loss expenses included $61.2 million related to current year losses and $14.2 million of favorable loss reserve development relating to prior accident years. The prior year favorable loss reserve development was due to lower than expected claims development on attritional and large losses. For the three months ended December 31, 2011, Talbot property lines losses and loss expenses included $62.8 million related to current year losses and $14.3 million of favorable loss reserve development relating to prior accident years. The prior year favorable loss reserve development was attributable to lower than expected claims development on large losses.

For the three months ended December 31, 2012, Talbot property lines incurred $45.6 million of losses from notable loss events, which represented 97.8 percentage points of the property lines loss ratio. Net of $1.2 million of reinstatement premiums, the effect of these events on net income was a decrease of $44.3 million. For the three months ended December 31, 2011, Talbot's property lines incurred $28.3 million of losses from notable loss events, which represented 68.9 percentage points of the property lines loss ratio. Talbot property line loss ratio, excluding notable loss events and prior year loss reserve development for the three months ended December 31, 2012 and 2011 were 33.5% and 83.8%, respectively.

For the three months ended December 31, 2012, Talbot marine lines losses and loss expenses included $65.4 million related to current year losses and $16.5 million of favorable loss reserve development relating to prior accident years. The prior year favorable loss reserve development was due primarily to lower than expected claims development on attritional losses. For the three months ended December 31, 2011, Talbot marine lines losses and loss expenses included $44.1 million related to current year losses and $10.1 million of favorable loss reserve development relating to prior accident years. The prior year favorable loss reserve development was primarily due to favorable development on attritional losses.

For the three months ended December 31, 2012, Talbot marine lines incurred $26.2 million of losses from notable loss events, which represented 30.2 percentage points of the marine lines loss ratio. Net of $0.9 million of reinstatement premiums, the effect of these events on net income was a decrease of $25.2 million. For the three months ended December 31, 2011, Talbot's marine lines incurred $1.0 million of losses from notable loss events, which represented 1.1 percentage points of the marine lines loss ratio. Talbot marine lines loss ratios, excluding notable loss events and prior year loss reserve development for the three months ended December 31, 2012 and 2011 were 45.3% and 48.2%, respectively.

For the three months ended December 31, 2012, Talbot specialty lines losses and loss expenses included $38.0 million relating to current year losses and $6.7 million of favorable loss reserve development relating to prior accident years. The prior year favorable loss reserve development was attributable to lower than expected claims development on attritional losses. For the three months ended December 31, 2011, Talbot specialty lines losses and loss expenses included $37.8 million relating to current year losses and $11.3 million of favorable loss reserve development relating to prior accident years. The prior year favorable loss reserve development was primarily due to favorable development on attritional losses.

Table of Contents

For the three months ended December 31, 2012, Talbot specialty lines incurred $6.7 million of losses from notable loss events, which represented 8.9 percentage points of the specialty lines loss ratio. Net of $(0.5) million of reinstatement premiums, the effect of these events on net income was a decrease of $7.2 million. For the three months ended December 31, 2011, Talbot's specialty lines incurred $1.9 million of losses from notable loss events, which represented 2.3 percentage points of the specialty lines loss ratio. Talbot specialty lines loss ratios, excluding notable loss events and prior year loss reserve development for the three months ended December 31, 2012 and 2011 were 41.8% and 45.6%, respectively.

Reserves for Losses and Loss Expenses

At December 31, 2012 and 2011, gross and net reserves for losses and loss expenses were estimated using the methodology as outlined in the Critical Accounting Policies and Estimates as discussed above. The Company did not make any significant changes in assumptions or methodology used in its reserving process for the year ended December 31, 2012.

	As at December 31, 2012		
(Dollars in thousands)	Gross Case Reserves	Gross IBNR	Total Gross Reserve for Losses and Loss Expenses
Property	$930,553	$892,227	$1,822,780
Marine	522,907	477,948	1,000,855
Specialty	265,638	428,300	693,938
Total	$1,719,098	$1,798,475	$3,517,573

	As at December 31, 2012		
(Dollars in thousands)	Net Case Reserves	Net IBNR	Total Net Reserve for Losses and Loss Expenses
Property	$768,722	$803,182	$1,571,904
Marine	465,080	438,009	903,089
Specialty	230,584	372,029	602,613
Total	$1,464,386	$1,613,220	$3,077,606

The following table sets forth a reconciliation of gross and net reserves for losses and loss expenses by segment for the three months ended December 31, 2012:

	Three Months Ended December 31, 2012				
(Dollars in thousands)	Validus Re Segment	AlphaCat Segment	Talbot Segment	Eliminations	Total
Gross reserves at period beginning	$1,216,560	$10,000	$1,422,568	$(86,524)	$2,562,604
Losses recoverable	(38,371)	—	(365,405)	86,524	(317,252)
Net reserves at period beginning	1,178,189	10,000	1,057,163	—	2,245,352
Net reserves acquired in Flagstone acquisition	639,641	—	—	—	639,641
Incurred losses—current year	350,926	—	164,605	—	515,531
Change in prior accident years	(19,796)	—	(37,425)	—	(57,221)
Incurred losses	331,130	—	127,180	—	458,310
Foreign exchange	(1,804)	—	2,747	—	943
Paid losses	(172,907)	(5,000)	(88,733)	—	(266,640)
Net reserves at period end	1,974,249	5,000	1,098,357	—	3,077,606
Losses recoverable	148,646	—	381,950	(90,629)	439,967
Gross reserves at period end	$2,122,895	$5,000	$1,480,307	$(90,629)	$3,517,573

The amount of recorded reserves represents management’s best estimate of expected losses and loss expenses on premiums earned. For the three months ended December 31, 2012, favorable loss reserve development on prior accident years was $57.2 million of which, $19.8 million of the favorable loss reserve development related to the Validus Re segment and $37.4 million related to the Talbot segment. Favorable loss reserve development benefited the Company’s loss ratio by 11.5 percentage points for the three months ended December 31, 2012. For the three months ended December 31, 2011, favorable loss reserve development

Table of Contents

on prior accident years was $42.8 million, of which, $7.1 million related to the Validus Re segment and $35.7 million related to the Talbot segment. Favorable loss reserve development benefited the Company’s loss ratio by 8.8 percentage points for the three months ended December 31, 2011.

Management of insurance and reinsurance companies use significant judgment in the estimation of reserves for losses and loss expenses. Given the magnitude of recent loss events and other uncertainties inherent in loss estimation, meaningful uncertainty remains regarding the estimation for recent notable loss events. The Company's actual ultimate net loss may vary materially from these estimates. Ultimate losses for notable loss events are estimated through detailed review of contracts which are identified by the Company as potentially exposed to the specific notable loss event. However, there can be no assurance that the ultimate loss amount estimated for a specific contract will be accurate, or that all contracts with exposure to a specific notable loss event will be identified in a timely manner. Potential losses in excess of the estimated ultimate loss assigned to a contract on the basis of a specific review, or loss amounts from contracts not specifically included in the detailed review are reserved for in the reserve for potential development on notable loss events. The reserve for potential development on notable loss events (or “RDE”) is included as part of the Company's overall reserve requirement as defined and disclosed in the Critical Accounting Policies and Estimates section above. As at September 30, 2012, the reserve for potential development on 2010 and 2011 notable loss events was $nil and $51.3 million, respectively. During the three months ended December 31, 2012, the Company increased certain loss estimates and allocated $9.1 million of 2011 RDE to the Christchurch earthquake, the Thailand floods and the Gryphon Alpha mooring failure. As at December 31, 2012, the reserve for potential development on 2010 and 2011 notable loss events was $nil and $42.2 million, respectively. No RDE was established for 2012 notable losses.

Policy Acquisition Costs

Policy acquisition costs for the three months ended December 31, 2012 were $81.8 million compared to $81.3 million for the three months ended December 31, 2011, an increase of $0.6 million or 0.7%. Policy acquisition costs as a percent of net premiums earned for the three months ended December 31, 2012 and 2011 were 16.4% and 16.6%, respectively. The changes in policy acquisition costs are due to the factors provided below.

	Three Months Ended December 31, 2012 (a)					Three Months Ended December 31, 2011						
(Dollars in thousands)	Policy Acquisition Costs	Policy Acquisition Costs (%)		Acquisition Cost Ratio		Policy Acquisition Costs	Policy Acquisition Costs (%)		Acquisition Cost Ratio		% Change	
Property	$29,237	35.8	%	11.7	%	$26,753	32.9	%	11.3	%	9.3	%
Marine	29,429	36.0	%	20.1	%	31,603	38.9	%	21.5	%	(6.9	)%
Specialty	23,148	28.3	%	22.7	%	22,897	28.2	%	21.9	%	1.1	%
Total	$81,814	100.1	%	16.4	%	$81,253	100.0	%	16.6	%	0.7	%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re. Validus Re policy acquisition costs for the three months ended December 31, 2012 were $40.7 million compared to $39.2 million for the three months ended December 31, 2011, an increase of $1.5 million or 3.8%.

	Three Months Ended December 31, 2012 (a)					Three Months Ended December 31, 2011						
(Dollars in thousands)	Policy Acquisition Costs	Policy Acquisition Costs (%)		Acquisition Cost Ratio		Policy Acquisition Costs	Policy Acquisition Costs (%)		Acquisition Cost Ratio		% Change	
Property	$25,820	63.4	%	13.0	%	$24,734	63.0	%	14.6	%	4.4	%
Marine	10,526	25.9	%	17.5	%	11,165	28.5	%	19.4	%	(5.7	)%
Specialty	4,357	10.7	%	16.1	%	3,328	8.5	%	12.8	%	30.9	%
Total	$40,703	100.0	%	14.3	%	$39,227	100.0	%	15.5	%	3.8	%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Policy acquisition costs include brokerage, commission and excise tax, are generally driven by contract terms, are normally a set percentage of premiums and are also net of ceding commission income on retrocessions. Items such as ceded premium, earned premium adjustments and reinstatement premiums that are recognized in the period have an effect on the policy acquisition costs ratio. Validus Re policy acquisition costs as a percent of net premiums earned (the policy acquisition cost ratio) for the three months ended December 31, 2012 and 2011 were 14.3% and 15.5%, respectively. The policy acquisition cost ratio on the specialty line has increased by 3.3 percentage points due to certain large proportional contracts that have higher policy acquisition cost ratios.

Table of Contents

AlphaCat. AlphaCat policy acquisition costs for the three months ended December 31, 2012 were $0.6 million compared to $3.3 million for the three months ended December 31, 2011, a decrease of $2.7 million or 82.3%.

	Three Months Ended December 31, 2012			Three Months Ended December 31, 2011			
(Dollars in thousands)	Policy Acquisition Costs	Policy Acquisition Costs (%)	Acquisition Cost Ratio	Policy Acquisition Costs	Policy Acquisition Costs (%)	Acquisition Cost Ratio	% Change
Property	$589	100.0 %	10.0 %	$3,331	100.0 %	12.6 %	(82.3)%
Total	$589	100.0 %	10.0 %	$3,331	100.0 %	12.6 %	(82.3)%

Policy acquisition costs as a percent of net premiums earned for the three months ended December 31, 2012 and 2011 were 10.0% and 12.6%, respectively.

Talbot. Talbot policy acquisition costs for the three months ended December 31, 2012 were $41.7 million compared to $41.2 million for the three months ended December 31, 2011, an increase of $0.6 million or 1.4%.

	Three Months Ended December 31, 2012			Three Months Ended December 31, 2011			
(Dollars in thousands)	Policy Acquisition Costs	Policy Acquisition Costs (%)	Acquisition Cost Ratio	Policy Acquisition Costs	Policy Acquisition Costs (%)	Acquisition Cost Ratio	% Change
Property	$4,648	11.1 %	10.0 %	$1,053	2.5 %	2.6 %	341.4 %
Marine	18,269	43.8 %	21.1 %	20,523	49.9 %	22.9 %	(11.0)%
Specialty	18,828	45.1 %	25.1 %	19,584	47.6 %	24.8 %	(3.9)%
Total	$41,745	100.0 %	20.1 %	$41,160	100.0 %	19.7 %	1.4 %

Policy acquisition costs as a percent of net premiums earned for the three months ended December 31, 2012 and 2011 were 20.1% and 19.7%, respectively. The policy acquisition ratio on the property line increased by 7.4 percentage points primarily due to a decrease in the ceding acquisition rates on the onshore energy lines.

General and Administrative Expenses

General and administrative expenses for the three months ended December 31, 2012 were $65.1 million compared to $52.3 million for the three months ended December 31, 2011, an increase of $12.8 million or 24.6%.

	Three Months Ended December 31, 2012 (a)		Three Months Ended December 31, 2011		
(Dollars in thousands)	General and Administrative Expenses	General and Administrative Expenses (%)	General and Administrative Expenses	General and Administrative Expenses (%)	% Change
Validus Re	$14,716	22.6 %	$11,716	22.4 %	25.6 %
AlphaCat	2,011	3.1 %	6,807	13.0 %	(70.5)%
Talbot	32,371	49.7 %	29,676	56.8 %	9.1 %
Corporate & Eliminations(b)	15,997	24.6 %	4,054	7.8 %	294.6 %
Total	$65,095	100.0 %	$52,253	100.0 %	24.6 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.
(b) Corporate and Eliminations includes legal entity adjustments

General and administrative expenses of $65.1 million in the three months ended December 31, 2012 represents 13.0 percentage points of the expense ratio. Share compensation expense is discussed in the following section.

Validus Re. Validus Re general and administrative expenses for the three months ended December 31, 2012 were $14.7 million compared to $11.7 million for the three months ended December 31, 2011, an increase of $3.0 million or 25.6%. General and administrative expenses have increased primarily due to the Company consolidating the general and administrative expenses as a result of the acquisition of Flagstone. General and administrative expenses include salaries and benefits, professional fees, rent and office expenses. Validus Re general and administrative expenses as a percent of net premiums earned for the three months ended December 31, 2012 and 2011 were 5.2% and 4.6%, respectively.

AlphaCat. AlphaCat general and administrative expenses for the three months ended December 31, 2012 were $2.0 million as compared to $6.8 million for the three months ended December 31, 2011, a decrease of $4.8 million or 70.5%. General and administrative expenses have decreased primarily due to the deconsolidation of AlphaCat Re 2011 as at December 31, 2011.

Table of Contents

AlphaCat's general and administrative expenses as a percent of net premiums earned for the three months ended December 31, 2012 and 2011 were 34.1% and 25.7%, respectively. The AlphaCat segment's general and administrative ratio has been impacted by the reduction in net premiums earned as a greater proportion of the segment's revenues are generated in equity earnings from operating affiliates which is not included in the ratio calculation.

Talbot. Talbot general and administrative expenses for the three months ended December 31, 2012 were $32.4 million compared to $29.7 million for the three months ended December 31, 2011, an increase of $2.7 million or 9.1%. General and administrative expenses have increased primarily due to an increase in performance bonus expense for the three months ended December 31, 2012 as compared to the three months ended December 31, 2011. Talbot's general and administrative expenses as a percent of net premiums earned for the three months ended December 31, 2012 and 2011 were 15.6% and 14.2%, respectively.

Corporate & Eliminations. Corporate general and administrative expenses for the three months ended December 31, 2012 were $16.0 million compared to $4.1 million for the three months ended December 31, 2011, an increase of $11.9 million or 294.6%. General and administrative expenses have increased primarily due to an increase in performance bonus expense as well as a decrease in eliminations between segments. Corporate general and administrative expenses are comprised of executive and board expenses, internal and external audit expenses and other costs relating to the Company as a whole.

Share Compensation Expenses

Share compensation expenses for the three months ended December 31, 2012 were $7.1 million compared to $7.2 million for the three months ended December 31, 2011, a decrease of $0.1 million or 1.5%. This expense is non-cash and has no net effect on total shareholders' equity, as it is balanced by an increase in additional paid-in capital.

(Dollars in thousands)	Three Months Ended December 31, 2012 (a)		Three Months Ended December 31, 2011		
	Share Compensation Expenses	Share Compensation Expenses (%)	Share Compensation Expenses	Share Compensation Expenses (%)	% Change
Validus Re	$1,849	25.9 %	$2,191	30.3 %	(15.6)%
AlphaCat	84	1.2 %	33	0.5 %	154.5 %
Talbot	2,442	34.3 %	1,934	26.7 %	26.3 %
Corporate & Eliminations (b)	2,751	38.6 %	3,079	42.5 %	(10.7)%
Total	$7,126	100.0 %	$7,237	100.0 %	(1.5)%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.
(b) Corporate and Eliminations includes legal entity adjustments.

Share compensation expenses of $7.1 million in the three months ended December 31, 2012 represents 1.5 percentage points of the general and administrative expense ratio.

Validus Re. Validus Re share compensation expenses for the three months ended December 31, 2012 were $1.8 million compared to $2.2 million for the three months ended December 31, 2011, a decrease of $0.3 million or 15.6%. Share compensation expense as a percent of net premiums earned for the three months ended December 31, 2012 and 2011 were 0.6% and 0.9%, respectively.

AlphaCat. AlphaCat share compensation expense as a percent of net premiums earned for the three months ended December 31, 2012 and 2011 were 1.5% and 0.1%, respectively.

Talbot. Talbot share compensation expenses for the three months ended December 31, 2012 was $2.4 million compared to $1.9 million for the three months ended December 31, 2011, an increase of $0.5 million or 26.3%. Share compensation expense as a percent of net premiums earned for the three months ended December 31, 2012 and 2011 were 1.1% and 0.9%, respectively.

Corporate & Eliminations. Corporate share compensation expenses for the three months ended December 31, 2012 were $2.8 million compared to $3.1 million for the three months ended December 31, 2011, a decrease of $0.3 million or 10.7%.

Selected Ratios

The underwriting results of an insurance or reinsurance company are often measured by reference to its combined ratio, which is the sum of the loss ratio and the expense ratio. The net loss ratio is calculated by dividing losses and loss expenses incurred (including estimates for incurred but not reported losses) by net premiums earned. The expense ratio is calculated by dividing policy acquisition costs combined with general and administrative expenses (including share compensation expenses)

Table of Contents

by net premiums earned. The following table presents the losses and loss expense ratio, policy acquisition cost ratio, general and administrative expense ratio, expense ratio and combined ratio for the three months ended December 31, 2012 and 2011.

	Three Months Ended December 31, 2012 (a)		Three Months Ended December 31, 2011		Percentage Point Change	
Consolidated						
Losses and loss expense ratio	91.8	%	68.6	%	23.2	
Policy acquisition cost ratio	16.4	%	16.6	%	(0.2	)
General and administrative expense ratio (b)	14.5	%	12.2	%	2.3	
Expense ratio	30.9	%	28.8	%	2.1	
Combined ratio	122.7	%	97.4	%	25.3	
Validus Re						
Losses and loss expense ratio	116.1	%	85.5	%	30.6	
Policy acquisition cost ratio	14.3	%	15.5	%	(1.2	)
General and administrative expense ratio (b)	5.8	%	5.5	%	0.3	
Expense ratio	20.1	%	21.0	%	(0.9	)
Combined ratio	136.2	%	106.5	%	29.7	
AlphaCat						
Losses and loss expense ratio	0.0	%	37.7	%	(37.7	)
Policy acquisition cost ratio	10.0	%	12.6	%	(2.6	)
General and administrative expense ratio (b)	35.6	%	25.8	%	9.8	
Expense ratio	45.6	%	38.4	%	7.2	
Combined ratio	45.6	%	76.1	%	(30.5	)
Talbot						
Losses and loss expense ratio	61.1	%	52.0	%	9.1	
Policy acquisition cost ratio	20.1	%	19.7	%	0.4	
General and administrative expense ratio (b)	16.7	%	15.1	%	1.6	
Expense ratio	36.8	%	34.8	%	2.0	
Combined ratio	97.9	%	86.8	%	11.1	

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.
(b) Includes general and administrative expenses and share compensation expenses.

General and administrative expense ratios for the three months ended December 31, 2012 and 2011 were 14.5% and 12.2%, respectively. General and administrative expense ratio is the sum of general and administrative expenses and share compensation expense divided by net premiums earned.

	Three Months Ended December 31, 2012 (a)			Three Months Ended December 31, 2011		
(Dollars in thousands)	Expenses	Expenses as % of Net Earned Premiums		Expenses	Expenses as % of Net Earned Premiums	
General and administrative expenses	$65,095	13.0	%	$52,253	10.7	%
Share compensation expenses	7,126	1.5	%	7,237	1.5	%
Total	$72,221	14.5	%	$59,490	12.2	%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Underwriting (Loss) Income

Underwriting loss for the three months ended December 31, 2012 was $(113.1) million compared to income of $12.8 million for the three months ended December 31, 2011, a decrease of $125.8 million, or 985.1%.

Table of Contents

(Dollars in thousands)	Three Months Ended December 31, 2012 (a)	% of Sub-total	Three Months Ended December 31, 2011	% of Sub-total	% Change
Validus Re	$(103,134)	108.0%	$(16,556)	(94.9)%	(522.9)%
AlphaCat	3,207	(3.4)%	6,340	36.3%	(49.4)%
Talbot	4,393	(4.6)%	27,658	158.6%	(84.1)%
Sub-total	(95,534)	100.0%	17,442	100.0%	(647.7)%
Corporate & Eliminations (b)	(17,525)		(4,668)		(275.4)%
Total	$(113,059)		$12,774		(985.1)%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.
(b) Corporate and Eliminations include legal entity adjustments.

The underwriting results of an insurance or reinsurance company are also often measured by reference to its underwriting income, which is a non-GAAP financial measure. Underwriting income, as set out in the table below, is reconciled to net income (the most directly comparable GAAP financial measure) by the addition or subtraction of certain Consolidated Statement of Comprehensive Income (Loss) line items, as illustrated below.

(Dollars in thousands)	Three Months Ended December 31, 2012 (a)	Three Months Ended December 31, 2011
Underwriting (loss) income	$(113,059)	$12,774
Net investment income	28,802	28,080
Other income	187	3,517
Finance expenses	(14,510)	(13,520)
Net realized (losses) gains on investments	(4,516)	5,355
Net unrealized (losses) gains on investments	(35,857)	2,159
Gain on bargain purchase, net of expenses	21,485	—
Transaction expenses	—	(3,850)
(Loss) from investment affiliate	(406)	—
Foreign exchange gains	1,181	266
Tax (expense) benefit	(615)	226
(Loss) from operating affiliates	(614)	—
Net (loss) income	$(117,922)	$35,007

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Underwriting income indicates the performance of the Company’s core underwriting function, excluding revenues and expenses such as the reconciling items in the table above. The Company believes the reporting of underwriting income enhances the understanding of our results by highlighting the underlying profitability of the Company’s core insurance and reinsurance business. Underwriting profitability is influenced significantly by earned premium growth, adequacy of the Company’s pricing and loss frequency and severity. Underwriting profitability over time is also influenced by the Company’s underwriting discipline, which seeks to manage exposure to loss through favorable risk selection and diversification, its management of claims, its use of reinsurance and its ability to manage its expense ratio, which it accomplishes through its management of acquisition costs and other underwriting expenses. The Company believes that underwriting income provides investors with a valuable measure of profitability derived from underwriting activities.

The Company excludes the U.S. GAAP measures noted above, in particular net realized and unrealized gains and losses on investments, from its calculation of underwriting income because the amount of these gains and losses is heavily influenced by, and fluctuates in part, according to availability of investment market opportunities. The Company believes these amounts are largely independent of its underwriting business and including them distorts the analysis of trends in its operations. In addition to presenting net income determined in accordance with U.S. GAAP, the Company believes that showing underwriting income enables investors, analysts, rating agencies and other users of its financial information to more easily analyze the Company's results of operations in a manner similar to how management analyzes the Company's underlying business performance. The Company uses underwriting income as a primary measure of underwriting results in its analysis of historical financial information and when performing its budgeting and forecasting processes. Analysts, investors and rating agencies who follow the Company

Table of Contents

request this non-GAAP financial information on a regular basis. In addition, underwriting income is one of the factors considered by the compensation committee of our Board of Directors in determining the total annual incentive compensation.

Underwriting income should not be viewed as a substitute for U.S. GAAP net income as there are inherent material limitations associated with the use of underwriting income as compared to using net income, which is the most directly comparable U.S. GAAP financial measure. The most significant limitation is the ability of users of the financial information to make comparable assessments of underwriting income with other companies, particularly as underwriting income may be defined or calculated differently by other companies. Therefore, the Company provides more prominence in this filing to the use of the most comparable U.S. GAAP financial measure, net income, which includes the reconciling items in the table above. The Company compensates for these limitations by providing both clear and transparent disclosure of net income and reconciliation of underwriting income to net income.

Net Investment Income

Net investment income for the three months ended December 31, 2012 was $28.8 million compared to $28.1 million for the three months ended December 31, 2011, an increase of $0.7 million or 2.6%. Net investment income increased due to the Flagstone acquisition. Net investment income is comprised of accretion of premium or discount on fixed maturities, interest on coupon-paying bonds, short-term investments and cash and cash equivalents, partially offset by investment management fees. The components of net investment income for the three months ended December 31, 2012 and 2011 are as provided below.

(Dollars in thousands)	Three Months Ended December 31, 2012 (a)	Three Months Ended December 31, 2011	% Change
Fixed maturities and short-term investments	$26,487	$27,740	(4.5)%
Other investments	2,790	—	NM
Cash and cash equivalents	1,723	2,153	(20.0)%
Securities lending income	5	27	(81.5)%
Total gross investment income	31,005	29,920	3.6%
Investment expenses	(2,203)	(1,840)	(19.7)%
Net investment income	$28,802	$28,080	2.6%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

NM: Not meaningful

Annualized investment yield is calculated by dividing net investment income (excluding other investments) by the average balance of the assets managed by our portfolio managers (excluding other investments). Average assets is the average of the beginning, ending and intervening quarter end asset balances. Percentages for the quarter periods are annualized. The Company’s annualized effective investment yield was 1.53% and 1.84% for the three months ended December 31, 2012 and 2011 respectively, and the average duration of the portfolio at December 31, 2012 was 1.34 years (December 31, 2011—1.63 years).

The annualized effective investment yield decreased for the three months ended December 31, 2012 due to the consolidation of the Flagstone investment portfolio which included $1,060.4 million in cash and short term investments, or 72.4% of Flagstone's total investments and cash as at December 31, 2012. Excluding the effect of the consolidation of the Flagstone investment portfolio, the annualized effective investment yield would have been 1.69% for the three months ended December 31, 2012. Overall yield has decreased due to falling yields on fixed maturity investments.

Other Income

Other income for the three months ended December 31, 2012 was $0.2 million compared to $3.5 million for the three months ended December 31, 2011, a decrease of $3.3 million or 94.7%. The decrease was due primarily to a reduction in Talbot third party income and the deconsolidation of AlphaCat Re 2011 as at December 31, 2011. AlphaCat Re 2011 was a consolidated subsidiary during the three months ended December 31, 2011. The balance sheet of AlphaCat Re 2011 was deconsolidated as at December 31, 2011.

Finance Expenses

Finance expenses for the three months ended December 31, 2012 were $14.5 million compared to $13.5 million for the three months ended December 31, 2011, an increase of $1.0 million or 7.3%. Finance expenses also include the amortization of debt offering costs and discounts, and fees related to our credit facilities.

Table of Contents

	Three Months Ended December 31,			
(Dollars in thousands)	2012 (a)	2011	% Change	
2006 Junior Subordinated Deferrable Debentures	$2,235	$1,496	49.4	%
2007 Junior Subordinated Deferrable Debentures	1,850	3,029	(38.9	)%
2010 Senior Notes due 2040	5,596	5,597	0.0	%
Flagstone 2006 Junior Subordinated Deferrable Interest Notes	459	—	NM	
Flagstone 2007 Junior Subordinated Deferrable Interest Notes	327	—	NM	
Credit facilities	1,469	1,671	(12.1	)%
Bank charges	138	218	22.9	%
AlphaCat Re 2011 fees (b)	—	1,497	(100.0	)%
AlphaCat ILS Funds fees (c)	2,432	—	NM	
Talbot FAL Facility	4	12	(66.7	)%
Finance expenses	$14,510	$13,520	7.3	%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.
(b) Includes preferred share dividends and finance expenses attributable to AlphaCat Re 2011.
(c) Includes finance expenses incurred by AlphaCat Managers, Ltd. in relation to the AlphaCat ILS funds and fund-raising for AlphaCat 2013.
NM: Not Meaningful

The increase in finance expenses of $1.0 million for the three months ended December 31, 2012 was due primarily to placements fees incurred by AlphaCat for its investments in ILS Funds of $2.4 million, partially offset by a $1.5 million decrease in the preferred dividends and finance expenses attributable to AlphaCat Re 2011.

Tax (Expense) Benefit

Tax expense for the three months ended December 31, 2012 was $(0.6) million compared to a benefit of $0.2 million for the three months ended December 31, 2011, an increase in expense of $0.8 million. The increase was primarily due to higher profit commission, UK taxable profit and Canadian tax charge, partially offset by a higher bonus deduction.

The Company provides for income taxes based upon amounts reported in the financial statements and the provisions of currently enacted tax laws. The Company is registered in Bermuda and is subject to Bermuda law with respect to taxation. Under current Bermuda law, the Company is not taxed on any Bermuda income or capital gains and has received an undertaking from the Bermuda Minister of Finance that, in the event of any Bermuda income or capital gains taxes being imposed, the Company will be exempt from those taxes until March 31, 2035.

Within the segment information contained in the Financial Statements, gross premiums written allocated to the territory of coverage exposure are presented for the periods indicated. Gross premiums written allocated to the United States are written primarily through Validus Reinsurance, Ltd., a Bermuda Registered Reinsurance Company. As noted, under current Bermuda law, the Company is not taxed on any Bermuda income and therefore the premium disclosed in the segment information does not correlate to pre-tax income generated in the United States.

(Loss) Income From Operating Affiliates

Loss from operating affiliates for the three months ended December 31, 2012 was $(0.6) million, compared to $nil for the three months ended December 31, 2011, a decrease of $(0.6) million. For the three months ended December 31, 2012, loss from operating affiliates of $(0.6) million relates to equity losses relating to AlphaCat Re 2011 and AlphaCat Re 2012.

In the second quarter of 2011, AlphaCat Re 2011 was included in the consolidated results of the Company, therefore there was no comparative information for the three months ended December 31, 2011. As at December 31, 2012, the Company owned 22.3% of AlphaCat Re 2011, therefore loss from operating affiliates reflects the Company’s share of AlphaCat Re 2011’s net loss for the three months ended December 31, 2012.

AlphaCat Re 2012 was formed on May 29, 2012 therefore there was no comparative information for the three months ended December 31, 2011. As at December 31, 2012, the Company owned 37.9% of AlphaCat Re 2012, therefore loss from operating affiliates reflects the Company’s share of AlphaCat Re 2012’s net loss for the three months ended

December 31, 2012.

Table of Contents

Gain on Bargain Purchase, Net of Expenses

On November 30, 2012, the Company acquired all of the outstanding shares of Flagstone. Pursuant to the Merger Agreement, the Company acquired all of Flagstone's outstanding common shares in exchange for the Company's common shares and cash. The purchase price paid by the Company was $646.0 million for net assets acquired of $695.7 million. The Company expensed as incurred $2.0 million of transaction expenses, $20.2 million of termination expenses and $6.0 million for amortization of intangibles related to the acquisition for the three months ended December 31, 2012, resulting in a gain on bargain purchase of $21.5 million. Transaction expenses are comprised of primarily legal and corporate advisory services.

Net Realized (Losses) Gains on Investments

Net realized losses on investments for the three months ended December 31, 2012 were $(4.5) million compared to gains of $5.4 million for the three months ended December 31, 2011, a decrease of $9.9 million or 184.3%.

Net Unrealized (Losses) Gains on Investments

Net unrealized losses on fixed maturities and short term investments for the three months ended December 31, 2012 were $(3.1) million compared to gains of $1.9 million for the three months ended December 31, 2011, a decrease of $5.0 million or 263.2%.

Net unrealized losses on other investments for the three months ended December 31, 2012 were $(32.8) million compared to gains of $0.3 million for the three months ended December 31, 2011. Net unrealized losses for the three months ended December 31, 2012 were driven primarily by a $(31.3) million unrealized loss relating to the Paulson & Co. hedge fund investments held by PaCRe. The amount of net unrealized losses attributable to noncontrolling interest was $(28.2) million for the three months ended December 31, 2012, leaving a net impact to the Company of $(3.1) million.

Net unrealized gains (losses) on investments are recorded as a component of net income. The Company has adopted all authoritative guidance on U.S. GAAP fair value measurements in effect as of the balance sheet date. Consistent with these standards, certain market conditions allow for fair value measurements that incorporate unobservable inputs where active market transaction based measurements are unavailable.

Loss From Investment Affiliate

The loss from investment affiliate for the three months ended December 31, 2012 was $(0.4) million compared to $nil for the three months ended December 31, 2011, a decrease of $(0.4) million. The loss from investment affiliate relates to the loss incurred in the Company's investment in the Aquiline Financial Services Fund II L.P. for the three months ended December 31, 2012. As at December 31, 2011, the investment in the Aquiline Financial Services Fund II L.P was included in other investments.

Foreign Exchange Gains

Foreign exchange gains for the three months ended December 31, 2012 were $1.2 million compared to $0.3 million for the three months ended December 31, 2011, a favorable movement of $0.9 million or 344.0%. For the three months ended December 31, 2012, Validus Re recognized foreign exchange gains of $0.2 million and Talbot recognized foreign exchange gains of $1.2 million.

For the three months ended December 31, 2012, Validus Re segment foreign exchange gains were $0.2 million compared to foreign exchange losses of $(0.2) million for the three months ended December 31, 2011, a favorable movement of $0.4 million or 196.7%. Validus Re currently hedges foreign currency exposure by balancing assets (primarily cash and premium receivables) with liabilities (primarily case reserves and event IBNR) for certain major non-USD currencies. Consequently, Validus Re aims to have a limited exposure to foreign exchange fluctuations.

For the three months ended December 31, 2012, Talbot segment foreign exchange gains were $1.2 million compared to $0.4 million for the three months ended December 31, 2011, a favorable movement of $0.7 million or 168.7%. The favorable movement in Talbot foreign exchange was due primarily to a $0.6 million gain due to the revaluation of assets held in Euros and other currencies.

As at December 31, 2012, Talbot's balance sheet includes net unearned premiums and deferred acquisition costs denominated in foreign currencies of approximately $107.4 million and $21.5 million, respectively. These balances consisted of British pound sterling and Canadian dollars of $78.0 million and $7.9 million, respectively. Net unearned premiums and deferred acquisition costs are classified as non-monetary items and are translated at historic exchange rates. All of Talbot's other balance sheet items are classified as monetary items and are translated at period end exchange rates. Additional foreign exchange gains (losses) may be incurred on the translation of net unearned premiums and deferred acquisition costs arising from insurance and reinsurance premiums written in future periods.

Net Loss (Income) Attributable to Noncontrolling Interest

On April 2, 2012, the Company capitalized PaCRe, a new Class 4 Bermuda reinsurer formed for the purpose of writing high excess property catastrophe reinsurance. PaCRe was funded with $500.0 million of contributed capital. Validus invested $50.0 million in PaCRe's common equity and therefore owns 10.0% of PaCRe. The net loss attributable to noncontrolling interest of $27.2 million for the three months ended December 31, 2012 was calculated as 90.0% of the net loss in PaCRe for the quarter.

On May 25, 2011, the Company joined with other investors in capitalizing AlphaCat Re 2011, a new special purpose reinsurer formed for the purpose of writing collateralized reinsurance and retrocessional reinsurance. Validus Re has an equity interest in AlphaCat Re 2011 and Validus Re held a majority of AlphaCat Re 2011's outstanding voting rights up to December 23, 2011 when AlphaCat Re 2011 completed a secondary offering of its common shares to third party investors, along with a partial sale of Validus Re common shares to one of the third party investors. As a result of these transactions, the Company's outstanding voting rights decreased to 43.7%. As a result of the Company's voting interest falling below 50%, the individual assets and liabilities and corresponding noncontrolling interest of AlphaCat Re 2011 were derecognized from the consolidated balance sheet of the Company as at December 31, 2011 and the remaining investment in AlphaCat Re 2011 is treated as an equity method investment as at December 31, 2012. For the three months ended December 31, 2011, the Company recorded $(7.7) million in net income attributable to noncontrolling interest relating to AlphaCat Re 2011.

Transaction Expenses

During the three months ended December 31, 2012, the Company incurred $nil in transaction expenses compared to $3.9 million for the three months ended December 31, 2011. For the three months ended December 31, 2011, the Company incurred transaction expenses related to its proposed acquisition of Transatlantic Holdings, Inc. ("Transatlantic"). The transaction expenses related to the November 30, 2012 acquisition of Flagstone are netted against the gain on bargain purchase. Refer to the section above entitled "Gain on Bargain Purchase, Net of Expenses." Transaction expenses are primarily comprised of legal, financial advisory and audit related services.

Table of Contents

The following table presents results of operations for the three months ended December 31, 2012 and 2011 and years ended December 31, 2012, 2011 and 2010:

	Three Months Ended December 31,		Years Ended December 31,		
(Dollars in thousands)	2012 (a)	2011	2012 (a)	2011	2010
Gross premiums written	$311,847	$278,279	$2,166,440	$2,124,691	1,990,566
Reinsurance premiums ceded	(35,659)	(16,489)	(307,506)	(289,241)	(229,482)
Net premiums written	276,188	261,790	1,858,934	1,835,450	1,761,084
Change in unearned premiums	223,098	226,556	14,282	(33,307)	39
Net premiums earned	499,286	488,346	1,873,216	1,802,143	1,761,123
Losses and loss expenses	458,310	334,829	999,446	1,244,401	987,586
Policy acquisition costs	81,814	81,253	334,698	314,184	292,899
General and administrative expenses	65,095	52,253	263,652	197,497	209,290
Share compensation expenses	7,126	7,237	26,709	34,296	28,911
Total underwriting deductions	612,345	475,572	1,624,505	1,790,378	1,518,686
Underwriting (loss) income (b)	(113,059)	12,774	248,711	11,765	242,437
Net investment income	28,802	28,080	107,936	112,296	134,103
Other income	187	3,517	22,396	5,718	5,219
Finance expenses	(14,510)	(13,520)	(53,857)	(54,817)	(55,870)
Operating (loss) income before taxes and (loss) income from oprating affiliates (b)	(98,580)	30,851	325,186	74,962	325,889
Tax (expense) benefit	(615)	226	(2,501)	(824)	(3,126)
(Loss) income from operating affiliates	(614)	—	12,580	—	—
Net operating (loss) income (b)	(99,809)	31,077	335,265	74,138	322,763
Gain on bargain purchase, net of expenses (c)	21,485	—	17,701	—	—
Net realized (losses) gains on investments	(4,516)	5,355	18,233	28,532	32,498
Net unrealized (losses) gains on investments	(35,857)	2,159	17,585	(19,991)	45,952
(Loss) from investment affiliate	(406)	—	(964)	—	—
Foreign exchange gains (losses)	1,181	266	4,798	(22,124)	1,351
Transaction expenses (d)	—	(3,850)	—	(17,433)	—
Net (loss) income	(117,922)	35,007	392,618	43,122	402,564
Net loss (income) attributable to noncontrolling interest	27,206	(7,683)	15,820	(21,793)	—
Net (loss) income (attributable) available to Validus	$(90,716)	$27,324	$408,438	$21,329	$402,564
Selected ratios:					
Net premiums written / Gross premiums written	88.6%	94.1%	85.8%	86.4%	88.5%
Losses and loss expenses	91.8%	68.6%	53.4%	69.1%	56.1%
Policy acquisition costs	16.4%	16.6%	17.9%	17.4%	16.6%
General and administrative expenses (e)	14.5%	12.2%	15.5%	12.9%	13.5%
Expense ratio	30.9%	28.8%	33.4%	30.3%	30.1%
Combined ratio	122.7%	97.4%	86.8%	99.4%	86.2%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

(b) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income and operating income that are not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. Reconciliations of these measures to the most comparable U.S. GAAP financial measure, are presented in the section below entitled “Underwriting Income”

(c) The gain on bargain purchase, net of expenses, arises from the acquisition of Flagstone Reinsurance Holdings S.A. on November 30, 2012 and is net of transaction related expenses.

(d) The transaction expenses relate to costs incurred in connection with the Company’s proposed acquisition of Transatlantic. Transaction expenses are primarily comprised of legal, financial advisory and audit related services.

(e) The general and administrative expense ratio includes share compensation expenses.

Table of Contents

(Dollars in thousands)	Three Months Ended December 31, 2012 (a)	2011	Years Ended December 31, 2012 (a)	2011	2010
Validus Re					
Gross premiums written	$79,233	$55,851	$1,131,959	$1,114,493	$1,089,443
Reinsurance premiums ceded	(7,074)	(49)	(144,578)	(150,718)	(63,147)
Net premiums written	72,159	55,802	987,381	963,775	1,026,296
Change in unearned premiums	213,105	196,679	35,890	2,150	13,822
Net premiums earned	285,264	252,481	1,023,271	965,925	1,040,118
Losses and loss expenses	331,130	215,903	575,416	749,305	601,610
Policy acquisition costs	40,703	39,227	154,362	154,582	159,527
General and administrative expenses	14,716	11,716	63,048	44,663	45,613
Share compensation expenses	1,849	2,191	7,763	9,309	7,181
Total underwriting deductions	388,398	269,037	800,589	957,859	813,931
Underwriting (loss) income (b)	(103,134)	(16,556)	222,682	8,066	226,187
AlphaCat					
Gross premiums written	$(4)	$(1,323)	$21,603	$75,727	$11,796
Reinsurance premiums ceded	—	—	—	—	—
Net premiums written	(4)	(1,323)	21,603	75,727	11,796
Change in unearned premiums	5,895	27,834	(3,937)	(9,761)	(714)
Net premiums earned	5,891	26,511	17,666	65,966	11,082
Losses and loss expenses	—	10,000	—	10,000	—
Policy acquisition costs	589	3,331	1,774	7,946	1,072
General and administrative expenses	2,011	6,807	7,532	10,929	5,327
Share compensation expenses	84	33	279	107	594
Total underwriting deductions	2,684	20,171	9,585	28,982	6,993
Underwriting income (b)	3,207	6,340	8,081	36,984	4,089
Legal Entity adjustments					
Gross premiums written	$7	$—	$7	$—	$—
Reinsurance premiums ceded	—	—	—	—	—
Net premiums written	7	—	7	—	—
Change in unearned premiums	(3,833)	—	(3,833)	—	—
Net premiums earned	(3,826)	—	(3,826)	—	—
Losses and loss expenses	—	—	—	—	—
Policy acquisition costs	$(365)	$(1,093)	$(390)	$(2,394)	$—
General and administrative expenses	1,673	(5,438)	5,130	(1,658)	15,927
Share compensation expenses	115	196	561	982	80
Total underwriting deductions	1,423	(6,335)	5,301	(3,070)	16,007
Underwriting (loss) income(b)	(5,249)	6,335	(9,127)	3,070	(16,007)
Talbot					
Gross premiums written	$241,100	$235,242	$1,078,636	$1,014,122	$981,073
Reinsurance premiums ceded	(37,067)	(27,931)	(228,686)	(218,174)	(258,081)
Net premiums written	204,033	207,311	849,950	795,948	722,992
Change in unearned premiums	4,098	2,043	(17,671)	(25,696)	(13,069)
Net premiums earned	208,131	209,354	832,279	770,252	709,923
Losses and loss expenses	127,180	108,926	424,030	485,096	385,976
Policy acquisition costs	41,745	41,160	183,926	157,334	143,769
General and administrative expenses	32,371	29,676	133,281	112,072	107,557

Share compensation expenses	2,442	1,934	7,789	8,582	6,923
Total underwriting deductions	203,738	181,696	749,026	763,084	644,225
Underwriting income (b)	4,393	27,658	83,253	7,168	65,698
Corporate & Eliminations					
Gross premiums written	$(8,489)	$(11,491)	$(65,765)	$(79,651)	$(91,746)
Reinsurance premiums ceded	8,482	11,491	65,758	79,651	91,746
Net premiums written	(7)	—	(7)	—	—
Change in unearned premiums	3,833	—	3,833	—	—
Net premiums earned	3,826	—	3,826	—	—
Losses and loss expenses	—	—	—	—	—
Policy acquisition costs	(858)	(1,372)	(4,974)	(3,284)	(11,469)
General and administrative expenses	14,324	9,492	54,661	31,491	34,866
Share compensation expenses	2,636	2,883	10,317	15,316	14,133
Total underwriting deductions	16,102	11,003	60,004	43,523	37,530
Underwriting (loss) (b)	(12,276)	(11,003)	(56,178)	(43,523)	(37,530)
Total underwriting (loss) income (b)	$(113,059)	$12,774	$248,711	$11,765	$242,437

Table of Contents

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

(b) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income that is not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of this measure to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled "Underwriting Income."

Year Ended December 31, 2012 compared to Year Ended December 31, 2011

Net income available to Validus for the year ended December 31, 2012 was $408.4 million compared to $21.3 million for the year ended December 31, 2011, an increase of $387.1 million. The primary factors driving the increase in net income were:

- Increase in underwriting income of $236.9 million due primarily to:
  - A $245.0 million decrease in loss and loss expenses and a $71.1 million increase in net premiums earned;
  - Offset by the following factors:
    - A $20.5 million increase in policy acquisition costs; and
    - A $66.2 million increase in general and administrative expenses, partially offset by a $7.6 million decrease in share compensation expenses;
- Increases in other income of $16.7 million and income from operating affiliates of $12.6 million;
- Increase in net unrealized gains on investments and foreign exchange of $37.6 million and $26.9 million, respectively;
- Decrease in transaction expenses of $17.4 million ($nil in the current year) and a $17.7 million gain on bargain purchase, net of expenses; and
- Net loss attributable to controlling interest which resulted in an increase to net income attributable to Validus of $37.6 million.

The above items were partially offset by the following factors:

- Unfavorable movement in net investment income and net realized gains on investments of $4.4 million and $10.3 million, respectively.

The change in net income available to Validus for the year ended December 31, 2012 of $387.1 million as compared to the year ended December 31, 2011 is described in the following table:

Table of Contents

(Dollars in thousands)	Year Ended December 31, 2012 Decrease (increase) over the year ended December 31, 2011 Validus Re (a)	AlphaCat	Talbot	Corporate and Eliminations(b)	Total
Notable losses—decrease in net losses and loss expenses (c)	$72,055	$—	$61,240	$ —	$133,295
Less: Notable losses— increase in net reinstatement premiums (c)	6,932	—	5,898	—	12,830
Other underwriting (loss) income	135,629	(28,903)	8,947	(24,852)	90,821
Underwriting income (loss) (d)	214,616	(28,903)	76,085	(24,852)	236,946
Net investment income	(4,521)	503	(4,070)	3,728	(4,360)
Other income	(2,305)	11,763	(1,452)	8,672	16,678
Finance expenses	(1,166)	598	65	1,463	960
Operating income (loss) before taxes and income from operating affiliates	206,624	(16,039)	70,628	(10,989)	250,224
Tax (expense)	(150)	—	(1,578)	51	(1,677)
Income from operating affiliates	—	12,580	—	—	12,580
Net operating income (loss)	206,474	(3,459)	69,050	(10,938)	261,127
Gain on bargain purchase, net of expenses	—	—	—	17,701	17,701
Net realized gains on investments	(9,112)	(315)	(872)	—	(10,299)
Net unrealized gains (losses) on investments	49,731	(18,168)	6,013	—	37,576
(Loss) from investment affiliate	(964)	—	—	—	(964)
Foreign exchange gains (losses)	22,188	508	4,715	(489)	26,922
Transaction expenses	—	—	—	17,433	17,433
Net income (loss)	268,317	(21,434)	78,906	23,707	349,496
Net loss (income) attributable to noncontrolling interest	—	37,613	—	—	37,613
Net income (loss) available (attributable) to Validus	$268,317	$16,179	$78,906	$ 23,707	$387,109

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.
(b) The Corporate and Eliminations column includes legal entity adjustments.
(c) Notable losses for the year ended December 31, 2012 include: Costa Concordia, Cat 67, U.S. drought, Hurricane Isaac and Hurricane Sandy. Notable losses for the year ended December 31, 2011 include: Tohoku earthquake, Gryphon Alpha mooring failure, Christchurch earthquake, Brisbane floods, CNRL Horizon, Cat 46, Cat 48, Jupiter 1, Danish floods, Hurricane Irene and the Thai floods. Excludes the reserve for potential development on 2011 notable loss events.
(d) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income (loss) that is not calculated under standards or rules that comprise U.S. GAAP. Such measures are referred to as non-GAAP. Non-GAAP measures may be defined or calculated differently by other companies. These measures should not be viewed as a substitute for those determined in accordance with U.S. GAAP. A reconciliation of this measure to net income, the most comparable U.S. GAAP financial measure, is presented in the section below entitled "Underwriting Income".

Gross Premiums Written

Gross premiums written for the year ended December 31, 2012 were $2,166.4 million compared to $2,124.7 million for the year ended December 31, 2011, an increase of $41.7 million or 2.0%. The marine and specialty lines increased by $79.4 million and $1.3 million, respectively, while the property lines decreased by $39.0 million. Details of gross premiums written by line of business are provided below.

	Year Ended December 31, 2012 (a)	Year Ended December 31, 2011	Year Ended December 31, 2010

(Dollars in thousands)	Gross Premiums Written	Gross Premiums Written (%)		Gross Premiums Written	Gross Premiums Written (%)		Gross Premiums Written	Gross Premiums Written (%)	
Property	$1,060,297	48.9	%	$1,099,303	51.7	%	$1,037,061	52.1	%
Marine	649,421	30.0	%	569,981	26.9	%	525,307	26.4	%
Specialty	456,722	21.1	%	455,407	21.4	%	428,198	21.5	%
Total	$2,166,440	100.0	%	$2,124,691	100.0	%	$1,990,566	100.0	%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Table of Contents

Validus Re. Validus Re gross premiums written for the year ended December 31, 2012 were $1,132.0 million compared to $1,114.5 million for the year ended December 31, 2011, an increase of $17.5 million or 1.6%. Details of Validus Re gross premiums written by line of business are provided below.

(Dollars in thousands)	Year Ended December 31, 2012 (a) Gross Premiums Written	Gross Premiums Written (%)	Year Ended December 31, 2011 Gross Premiums Written	Gross Premiums Written (%)	Year Ended December 31, 2010 Gross Premiums Written	Gross Premiums Written (%)
Property	$771,617	68.2 %	$786,937	70.6 %	$778,794	71.5 %
Marine	257,469	22.7 %	232,401	20.9 %	227,135	20.8 %
Specialty	102,873	9.1 %	95,155	8.5 %	83,514	7.7 %
Total	$1,131,959	100.0 %	$1,114,493	100.0 %	$1,089,443	100.0 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

The decrease in gross premiums written in the property lines of $15.3 million was due primarily to a $25.8 million decrease in renewing premiums written on proportional and per risk excess of loss treaties relating to reduced participation on several large contracts not meeting the Company's underwriting requirements and a $12.4 million decrease in intercompany premiums written with Talbot. These were partially offset by a $9.3 million increase in new business written in the Singapore branch, a $9.1 million increase in premium adjustments and catastrophe excess of loss business and a $7.4 million increase in premiums relating to the Flagstone acquisition. The increase in gross premiums written of $25.1 million in the marine lines was due to a $24.6 million increase in reinstatement premiums primarily relating to the Costa Concordia event and a $2.8 million increase in premium adjustments on proportional business, slightly offset by a $3.8 million decrease in premiums on new business incepting during the period. The increase in gross premiums written of $7.7 million in the specialty lines was due primarily to a $6.0 million increase in premium adjustments on proportional business, a $3.1 million increase in premiums relating to the Flagstone acquisition and a $2.8 million increase in new business written in the Singapore branch. These were slightly offset by a $2.1 million decrease in premiums on new business incepting during the period and a $2.0 million decrease in intercompany premiums written with Talbot.

Gross premiums written under the quota share, surplus treaty and excess of loss contracts between Validus Re and Talbot for the year ended December 31, 2012 decreased by $14.4 million as compared to the year ended December 31, 2011. These reinsurance agreements with Talbot are eliminated upon consolidation.

AlphaCat. AlphaCat gross premiums written for the year ended December 31, 2012 were $21.6 million compared to $75.7 million for the year ended December 31, 2011 , a decrease of $54.1 million or 71.5%. Details of AlphaCat gross premiums written by line of business are provided below.

(Dollars in thousands)	Year Ended December 31, 2012 Gross Premiums Written	Gross Premiums Written (%)	Year Ended December 31, 2011 Gross Premiums Written	Gross Premiums Written (%)	Year Ended December 31, 2010 Gross Premiums Written	Gross Premiums Written (%)
Property	21,603	100.0 %	75,727	100.0 %	11,796	100.0 %
Total	21,603	100.0 %	75,727	100.0 %	11,796	100.0 %

The decrease in gross premiums written in the property lines of $54.1 million was due primarily to the deconsolidation of AlphaCat Re 2011 which occurred as at December 31, 2011, when the individual assets and liabilities and corresponding noncontrolling interest of AlphaCat Re 2011 were derecognized from the consolidated Balance Sheet of the Company. AlphaCat Re 2011 was consolidated in 2011 until December 31, 2011 whereas in 2012, AlphaCat Re 2011 is accounted for as an equity method operating affiliate. Therefore the comparative renewals are not reflected in gross premiums written in 2012, but are included in gross managed premiums, a comparable measure.

Managed gross premiums written from our non-consolidated affiliates, AlphaCat Re 2011and AlphaCat Re 2012, for the year ended December 31, 2012 were $126.5 million compared to $60.0 million for the year ended December 31, 2011, an increase of $66.5 million or 110.8%. Gross premiums written from our consolidated AlphaCat entities for the year ended December 31, 2012 were $21.6 million compared to $15.7 million for the year ended December 31, 2011, an increase of $5.9 million or 37.5% .

Gross premiums written with Talbot for the year ended December 31, 2012 increased by $0.5 million as compared to the year ended December 31, 2011. These reinsurance agreements with Talbot are eliminated upon consolidation.

Table of Contents

Talbot. Talbot gross premiums written for the year ended December 31, 2012 were $1,078.6 million compared to $1,014.1 million for the year ended December 31, 2011, an increase of $64.5 million or 6.4%. The $1,078.6 million of gross premiums written translated at 2011 rates of exchange would have been $1,081.7 million for the year ended December 31, 2012, giving an effective increase of $67.6 million or 6.7%. Details of Talbot gross premiums written by line of business are provided below.

	Year Ended December 31, 2012			Year Ended December 31, 2011			Year Ended December 31, 2010		
(Dollars in thousands)	Gross Premiums Written	Gross Premiums Written (%)		Gross Premiums Written	Gross Premiums Written (%)		Gross Premiums Written	Gross Premiums Written (%)	
Property	$324,910	30.1	%	$306,317	30.2	%	$314,769	32.1	%
Marine	396,207	36.7	%	341,821	33.7	%	315,102	32.1	%
Specialty	357,519	33.2	%	365,984	36.1	%	351,202	35.8	%
Total	$1,078,636	100.0	%	$1,014,122	100.0	%	$981,073	100.0	%

The increase in gross premiums written in the property lines of $18.6 million was due primarily to a $16.1 million increase in the direct property lines and a $9.1 million increase in the construction lines, partially offset by an $8.3 million decrease in the property treaty lines. During the nine months ended September 30, 2012, Talbot reassessed commission costs on underwriting years 2007 and prior, related to business on the marine class. This resulted in a $14.8 million increase in gross premiums written and earned premium, offset by an equal increase on policy acquisition costs for the marine class, resulting in no net impact. The increase in gross premiums written in the marine lines of $54.4 million was due primarily to a $14.8 million increase in premium adjustments, described above, a $29.9 million increase in premium adjustments in the cargo and offshore energy lines, an $8.0 million increase in premiums written in the marine energy and liability lines and a $4.9 million increase in other treaty lines mainly driven by reinstatement premiums on Hurricane Sandy. These increases were slightly offset by a $2.3 million decrease in premiums written in the hull lines. The decrease in gross premiums written in the specialty lines of $8.5 million was due primarily to a $15.1 million decrease in premiums written in direct aviation and aviation treaty lines. This decrease primarily relates to a premium reassessment of $8.2 million which has no net earned impact on the direct aviation and aviation treaty lines. In addition, there was a $1.7 million decrease in financial institutions lines, partially offset by a $9.3 million increase in political risk lines.

Reinsurance Premiums Ceded

Reinsurance premiums ceded for the year ended December 31, 2012 were $307.5 million compared to $289.2 million for the year ended December 31, 2011, an increase of $18.3 million, or 6.3%. The marine and specialty lines increased by $14.0 million and $7.2 million, respectively, while the property lines decreased by $3.0 million. Details of reinsurance premiums ceded by line of business are provided below.

	Year Ended December 31, 2012 (a)			Year Ended December 31, 2011			Year Ended December 31, 2010		
(Dollars in thousands)	Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)		Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)		Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)	
Property	$206,000	67.0	%	$208,968	72.2	%	$123,383	53.7	%
Marine	46,853	15.2	%	32,847	11.4	%	38,701	16.9	%
Specialty	54,653	17.8	%	47,426	16.4	%	67,398	29.4	%
Total	$307,506	100.0	%	$289,241	100.0	%	$229,482	100.0	%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re. Validus Re reinsurance premiums ceded for the year ended December 31, 2012 were $144.6 million compared to $150.7 million for the year ended December 31, 2011, a decrease of $6.1 million, or 4.1%. Details of Validus Re reinsurance premiums ceded by line of business are provided below.

	Year Ended December 31, 2012 (a)	Year Ended December 31, 2011	Year Ended December 31, 2010

(Dollars in thousands)	Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)		Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)		Reinsurance Premiums Ceded		Reinsurance Premiums Ceded (%)	
Property	$123,610	85.5	%	$136,369	90.5	%	$45,536		72.2	%
Marine	20,397	14.1	%	13,848	9.2	%	17,643		27.9	%
Specialty	571	0.4	%	501	0.3	%	(32	)	(0.1	)%
Total	$144,578	100.0	%	$150,718	100.0	%	$63,147		100.0	%

Table of Contents

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.
Reinsurance premiums ceded in the property lines decreased by $12.8 million, due primarily to a $7.9 million decrease in non-proportional retrocessional coverage, a $3.3 million decrease in adjustments from prior periods and a $2.1 million decrease in proportional retrocessional coverage. These were slightly offset by a $0.7 million increase in ceded reinstatement premiums. The reduction in both non-proportional and proportional retrocessional coverage is a result of comparatively higher purchases of this coverage in the three months ended March 31, 2011 prior to, and following, the notable loss events of that quarter. The increase in reinsurance premiums ceded in the marine lines of $6.5 million was due primarily to a $6.0 million increase in non-proportional coverage incepting in the year.

AlphaCat. AlphaCat did not cede reinsurance premiums during the year ended December 31, 2012 and 2011.

Talbot. Talbot reinsurance premiums ceded for the year ended December 31, 2012 were $228.7 million compared to $218.2 million for the year ended December 31, 2011, an increase of $10.5 million or 4.8%. Details of Talbot reinsurance premiums ceded by line of business are provided below.

(Dollars in thousands)	Year Ended December 31, 2012		Year Ended December 31, 2011		Year Ended December 31, 2010	
	Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)	Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)	Reinsurance Premiums Ceded	Reinsurance Premiums Ceded (%)
Property	$140,223	61.3 %	$142,277	65.2 %	$146,145	56.6 %
Marine	30,711	13.4 %	23,240	10.7 %	37,988	14.7 %
Specialty	57,752	25.3 %	52,657	24.1 %	73,948	28.7 %
Total	$228,686	100.0 %	$218,174	100.0 %	$258,081	100.0 %

The decrease in reinsurance premiums ceded in the property lines of $2.1 million was due primarily to a $4.1 million decrease in premium ceded in the onshore energy lines and a $2.3 million decrease in property treaty lines, partially offset by a $3.1 million increase in the direct property lines. The increase in reinsurance premiums ceded in the marine lines of $7.5 million was primarily due to an increase in premiums ceded in the energy lines of $5.6 million driven primarily by an increase in reinstatement premiums and prior period adjustments. The increase in reinsurance premiums ceded in the specialty lines of $5.1 million was primarily due to a $4.3 million increase in excess of loss coverage and reinstatement premiums on aviation direct lines.

Reinsurance premiums ceded under the quota share, surplus treaty and excess of loss contracts with Validus Re and AlphaCat for the year ended December 31, 2012 were $65.8 million compared to $79.7 million for the year ended December 31, 2011, a decrease of $13.9 million. These reinsurance agreements with Validus Re and AlphaCat are eliminated upon consolidation.

Net Premiums Written

Net premiums written for the year ended December 31, 2012 were $1,858.9 million compared to $1,835.5 million for the year ended December 31, 2011, an increase of $23.5 million, or 1.3%. The ratios of net premiums written to gross premiums written for the year ended December 31, 2012 and 2011 were 85.8% and 86.4%, respectively. Details of net premiums written by line of business are provided below.

(Dollars in thousands)	Year Ended December 31, 2012 (a)		Year Ended December 31, 2011		Year Ended December 31, 2010	
	Net Premiums Written	Net Premiums Written (%)	Net Premiums Written	Net Premiums Written (%)	Net Premiums Written	Net Premiums Written (%)
Property	$854,297	46.0 %	$890,335	48.5 %	$913,678	51.9 %
Marine	602,568	32.4 %	537,134	29.3 %	486,606	27.6 %
Specialty	402,069	21.6 %	407,981	22.2 %	360,800	20.5 %
Total	$1,858,934	100.0 %	$1,835,450	100.0 %	$1,761,084	100.0 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re. Validus Re net premiums written for the year ended December 31, 2012 were $987.4 million compared to $963.8 million for the year ended December 31, 2011, an increase of $23.6 million or 2.4%. Details of Validus Re net premiums written by line of business are provided below.

97

Table of Contents

(Dollars in thousands)	Year Ended December 31, 2012 (a) Net Premiums Written	Net Premiums Written (%)		Year Ended December 31, 2011 Net Premiums Written	Net Premiums Written (%)		Year Ended December 31, 2010 Net Premiums Written	Net Premiums Written (%)	
Property	$648,007	65.6	%	$650,568	67.5	%	$733,258	71.5	%
Marine	237,072	24.0	%	218,553	22.7	%	209,492	20.4	%
Specialty	102,302	10.4	%	94,654	9.8	%	83,546	8.1	%
Total	$987,381	100.0	%	$963,775	100.0	%	$1,026,296	100.0	%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

The increase in Validus Re net premiums written was driven by factors highlighted above in respect of gross premiums written and reinsurance premiums ceded. The ratios of net premiums written to gross premiums written were 87.2% and 86.5% for the year ended December 31, 2012 and 2011, respectively.

AlphaCat. AlphaCat net premiums written for the year ended December 31, 2012 were $21.6 million compared to $75.7 million for the year ended December 31, 2011, a decrease of $54.1 million or 71.5%. Details of AlphaCat net premiums written by line of business are provided below.

(Dollars in thousands)	Year Ended December 31, 2012 Net Premiums Written	Net Premiums Written (%)		Year Ended December 31, 2011 Net Premiums Written	Net Premiums Written (%)		Year Ended December 31, 2010 Net Premiums Written	Net Premiums Written (%)	
Property	$21,603	100.0	%	$75,727	100.0	%	$11,796	100.0	%
Total	$21,603	100.0	%	$75,727	100.0	%	$11,796	100.0	%

The decrease in AlphaCat net premiums written was driven by the factors highlighted above in respect of gross premiums written. The ratios of net premiums written to gross premiums written were 100.0% for the year ended December 31, 2012 and 2011.

Talbot. Talbot net premiums written for the year ended December 31, 2012 were $850.0 million compared to $795.9 million for the year ended December 31, 2011, an increase of $54.0 million or 6.8%. Details of Talbot net premiums written by line of business are provided below.

(Dollars in thousands)	Year Ended December 31, 2012 Net Premiums Written	Net Premiums Written (%)		Year Ended December 31, 2011 Net Premiums Written	Net Premiums Written (%)		Year Ended December 31, 2010 Net Premiums Written	Net Premiums Written (%)	
Property	$184,687	21.7	%	$164,040	20.6	%	$168,624	23.4	%
Marine	365,496	43.0	%	318,581	40.0	%	277,114	38.3	%
Specialty	299,767	35.3	%	313,327	39.4	%	277,254	38.3	%
Total	$849,950	100.0	%	$795,948	100.0	%	$722,992	100.0	%

The increase in Talbot net premiums written was driven by the factors highlighted above in respect of gross premiums written and reinsurance premiums ceded. The ratios of net premiums written to gross premiums written for the year ended December 31, 2012 and 2011 were 78.8% and 78.5%, respectively.

Net Change in Unearned Premiums

Net change in unearned premiums for the year ended December 31, 2012 was $14.3 million compared to $(33.3) million for the year ended December 31, 2011, an increase of $47.6 million or 142.9%.

Table of Contents

(Dollars in thousands)	Year Ended December 31, 2012 (a) Net Change in Unearned Premiums	Year Ended December 31, 2011 Net Change in Unearned Premiums	Year Ended December 31, 2010 Net Change in Unearned Premiums
Change in gross unearned premium	$(121,980)	$(43,866)	$(12,079)
Less change due to Flagstone acquisition	139,389	—	—
Deconsolidation of AlphaCat Re 2011	—	(9,405)	—
Net change in gross unearned premium	17,409	(53,271)	(12,079)
Change in prepaid reinsurance premium	8,212	19,964	12,118
Less change due to Flagstone acquisition	(11,339)	—	—
Net change in prepaid reinsurance premium	(3,127)	19,964	12,118
Net change in unearned premium	$14,282	$(33,307)	$39

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re. Validus Re net change in unearned premiums for the year ended December 31, 2012 was $35.9 million compared to $2.2 million for the year ended December 31, 2011, an increase of $33.7 million, or 1,569.3%.

(Dollars in thousands)	Year Ended December 31, 2012(a) Net Change in Unearned Premiums	Year Ended December 31, 2011 Net Change in Unearned Premiums	Year Ended December 31, 2010 Net Change in Unearned Premiums
Change in gross unearned premium	$(104,420)	$(7,771)	$16,277
Less change due to Flagstone acquisition	139,389	—	—
Deconsolidation of AlphaCat Re 2011	—	(9,405)	—
Net change in gross unearned premium	34,969	(17,176)	16,277
Change in prepaid reinsurance premium	12,260	19,326	(2,455)
Less change due to Flagstone acquisition	(11,339)	—	—
Net change in prepaid reinsurance premium	921	19,326	(2,455)
Net change in unearned premium	$35,890	$2,150	$13,822

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re net change in unearned premiums has increased for the year ended December 31, 2012 due to the earnings pattern of gross premiums written and reinsurance premiums ceded during the year ended December 31, 2012 as compared to the year ended December 31, 2011.

AlphaCat. AlphaCat net change in unearned premiums for the year ended December 31, 2012 was $(3.9) million compared to $(9.8) million for the year ended December 31, 2011, an increase of $5.8 million or 59.7%.

(Dollars in thousands)	Year Ended December 31, 2012 Net Change in Unearned Premiums	Year Ended December 31, 2011 Net Change in Unearned Premiums	Year Ended December 31, 2010 Net Change in Unearned Premiums
Change in gross unearned premium	$(3,937)	$(9,761)	$(714)
Net change in unearned premium	$(3,937)	$(9,761)	$(714)

AlphaCat net change in unearned premiums has increased for the year ended December 31, 2012 due primarily to the deconsolidation of AlphaCat Re 2011 and the earnings pattern of gross premiums written and reinsurance premiums ceded during the year ended December 31, 2012 as compared to year ended December 31, 2011.

Table of Contents

Talbot. Talbot net change in unearned premiums for the year ended December 31, 2012 was $(17.7) million compared to $(25.7) million for the year ended December 31, 2011, an increase of $8.0 million or 31.2%.

(Dollars in thousands)	Year Ended December 31, 2012 Net Change in Unearned Premiums	Year Ended December 31, 2011 Net Change in Unearned Premiums	Year Ended December 31, 2010 Net Change in Unearned Premiums
Change in gross unearned premium	$(13,623)	$(26,334)	$(27,642)
Change in prepaid reinsurance premium	(4,048)	638	14,573
Net change in unearned premium	$(17,671)	$(25,696)	$(13,069)

Talbot net change in unearned premiums has increased for the year ended December 31, 2012 due to the earnings pattern of gross premiums written and reinsurance premiums ceded during the year ended December 31, 2012 as compared to the year ended December 31, 2011.

Net Premiums Earned

Net premiums earned for the year ended December 31, 2012 were $1,873.2 million compared to $1,802.1 million for the year ended December 31, 2011, an increase of $71.1 million or 3.9%. Details of net premiums earned by line of business are provided below.

	Year Ended December 31, 2012 (a)		Year Ended December 31, 2011		Year Ended December 31, 2010	
(Dollars in thousands)	Net Premiums Earned	Net Premiums Earned (%)	Net Premiums Earned	Net Premiums Earned (%)	Net Premiums Earned	Net Premiums Earned (%)
Property	$866,365	46.3 %	$891,448	49.5 %	$923,370	52.4 %
Marine	609,012	32.5 %	517,376	28.7 %	445,426	25.3 %
Specialty	397,839	21.2 %	393,319	21.8 %	392,327	22.3 %
Total	$1,873,216	100.0 %	$1,802,143	100.0 %	$1,761,123	100.0 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

Validus Re. Validus Re net premiums earned for the year ended December 31, 2012 were $1,023.3 million compared to $965.9 million for the year ended December 31, 2011, an increase of $57.3 million or 5.9%. Details of Validus Re net premiums earned by line of business are provided below.

	Year Ended December 31, 2012 (a)		Year Ended December 31, 2011		Year Ended December 31, 2010	
(Dollars in thousands)	Net Premiums Earned	Net Premiums Earned (%)	Net Premiums Earned	Net Premiums Earned (%)	Net Premiums Earned	Net Premiums Earned (%)
Property	$673,928	65.9 %	$664,244	68.8 %	$754,583	72.5 %
Marine	254,092	24.8 %	211,344	21.9 %	176,601	17.0 %
Specialty	95,251	9.3 %	90,337	9.3 %	108,934	10.5 %
Total	$1,023,271	100.0 %	$965,925	100.0 %	$1,040,118	100.0 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

The increase in net premiums earned is consistent with the relevant pattern of net premiums written influencing the earned premiums for the year ended December 31, 2012 compared to the year ended December 31, 2011.

AlphaCat. AlphaCat net premiums earned for the year ended December 31, 2012 were $17.7 million compared to $66.0 million for the year ended December 31, 2011, a decrease of $48.3 million or 73.2%. Details of AlphaCat net premiums earned by line of business are provided below.

Table of Contents

(Dollars in thousands)	Year Ended December 31, 2012 Net Premiums Earned	Year Ended December 31, 2012 Net Premiums Earned (%)		Year Ended December 31, 2011 Net Premiums Earned	Year Ended December 31, 2011 Net Premiums Earned (%)		Year Ended December 31, 2010 Net Premiums Earned	Year Ended December 31, 2010 Net Premiums Earned (%)	
Property	$17,666	100.0	%	$65,966	100.0	%	$11,082	100.0	%
Total	$17,666	100.0	%	$65,966	100.0	%	$11,082	100.0	%

The decrease in net premiums earned is consistent with the relevant pattern of net premiums written influencing the earned premiums for the year ended December 31, 2012 compared to the year ended December 31, 2011 and the deconsolidation of AlphaCat Re 2011.

Talbot. Talbot net premiums earned for the year ended December 31, 2012 were $832.3 million compared to $770.3 million for the year ended December 31, 2011, an increase of $62.0 million or 8.1%. Details of Talbot net premiums earned by line of business are provided below.

(Dollars in thousands)	Year Ended December 31, 2012 Net Premiums Earned	Year Ended December 31, 2012 Net Premiums Earned (%)		Year Ended December 31, 2011 Net Premiums Earned	Year Ended December 31, 2011 Net Premiums Earned (%)		Year Ended December 31, 2010 Net Premiums Earned	Year Ended December 31, 2010 Net Premiums Earned (%)	
Property	$174,771	21.0	%	$161,238	21.0	%	$157,705	22.2	%
Marine	354,920	42.6	%	306,032	39.7	%	268,825	37.9	%
Specialty	302,588	36.4	%	302,982	39.3	%	283,393	39.9	%
Total	$832,279	100.0	%	$770,252	100.0	%	$709,923	100.0	%

During the nine months ended September 30, 2012, Talbot reassessed commission costs on underwriting years 2007 and prior, related to business on the marine class. This resulted in a $14.8 million increase in gross premiums written and earned premium, offset by an equal increase on policy acquisition costs for the marine class, resulting in no net impact. Increases in previously written premium income also contributed to an increase in net premiums earned of $34.1 million, driven mainly by energy, cargo, other treaty and marine energy and liability classes, offset by small decreases in other classes.

The increase in net premiums earned is consistent with the relevant patterns of net premiums written influencing the earned premiums for the year ended December 31, 2012, as compared to the year ended December 31, 2011.

Losses and Loss Expenses

Losses and loss expenses for the year ended December 31, 2012 were $999.4 million compared to $1,244.4 million for the year ended December 31, 2011, a decrease of $245.0 million or 19.7%. The loss ratios, defined as losses and loss expenses divided by net premiums earned, for the year ended December 31, 2012 and 2011 were 53.4% and 69.1%, respectively. Details of loss ratios by line of business are provided below.

	Year Ended December 31, 2012 (a)		Year Ended December 31, 2011		Year Ended December 31, 2010	
Property	54.7	%	87.1	%	60.5	%
Marine	60.1	%	61.7	%	50.3	%
Specialty	40.0	%	37.8	%	52.2	%
All lines	53.4	%	69.1	%	56.1	%

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

	Year Ended December 31, 2012 (a)	2011	2010
Property—current period—excluding items below	25.5 %	28.2 %	21.7 %
Property—current period—notable losses	37.5 %	58.7 %	45.7 %
Property—current period—reserve for potential development on notable loss events	0.0 %	8.2 %	0.9 %
Property—change in prior accident years	(8.3)%	(8.0)%	(7.8)%
Property—loss ratio	54.7 %	87.1 %	60.5 %
Marine—current period—excluding items below	44.6 %	48.4 %	44.9 %
Marine—current period—notable losses	23.9 %	20.3 %	15.5 %
Marine—current period—reserve for potential development on notable loss events	0.0 %	1.0 %	5.6 %
Marine—change in prior accident years	(8.4)%	(8.0)%	(15.7)%
Marine—loss ratio	60.1 %	61.7 %	50.3 %
Specialty—current period—excluding items below	45.4 %	47.3 %	45.7 %
Specialty—current period—notable losses (b)	7.6 %	1.5 %	10.1 %
Specialty—current period—reserve for potential development on notable loss events	0.0 %	0.0 %	0.0 %
Specialty—change in prior accident years (b)	(13.0)%	(11.0)%	(3.6)%
Specialty—loss ratio	40.0 %	37.8 %	52.2 %
All lines—current period—excluding items below	36.0 %	38.3 %	33.0 %
All lines—current period—notable losses (b)	26.7 %	35.2 %	30.1 %
All lines—current period—reserve for potential development on notable loss events	0.0 %	4.3 %	1.9 %
All lines—change in prior accident years (b)	(9.3)%	(8.7)%	(8.9)%
All lines—loss ratio	53.4 %	69.1 %	56.1 %

(a) The results of operations for Flagstone are consolidated only from the November 30, 2012 date of acquisition.

(b) The financial institution loss occurred in a prior period but developed over the notable loss threshold in the three months ended December 31, 2010. In 2010, this loss was included in the change in prior year development and excluded as a notable loss as presented above.

Validus Re. Validus Re losses and loss expenses for the year ended December 31, 2012 were $575.4 million compared to $749.3 million for the year ended December 31, 2011, a decrease of $173.9 million or 23.2%. The loss ratio, defined as losses and loss expenses divided by net premiums earned, was 56.2% and 77.6% for the year ended December 31, 2012 and 2011, respectively. For the year ended December 31, 2012, Validus Re incurred losses of $648.0 million related to current year losses and $72.6 million of favorable loss reserve development relating to prior accident years. For the year ended December 31, 2012, favorable loss reserve development on prior accident years benefited the Validus Re loss ratio by 7.1 percentage points. For the year ended December 31, 2011, Validus Re incurred losses of $817.9 million related to current year losses and $68.6 million of favorable loss reserve development relating to prior accident years. For the year ended December 31, 2011, favorable loss reserve development relating to prior accident years benefited the Validus Re loss ratio by 7.1 percentage points.

For the year ended December 31, 2012, Validus Re incurred $402.7 million of losses from notable loss events, which represented 39.4 percentage points of the loss ratio. Net of reinstatement premiums of $60.8 million, the effect of these events on Validus Re segment income was a decrease of $342.0 million. For the year ended December 31, 2011, Validus Re incurred $474.8 million of losses from notable loss events, which represented 49.2 percentage points of the loss ratio, excluding reserve for potential development on notable loss events. Net of reinstatement premiums of $53.8 million, the effect of these events on Validus Re segment income was a decrease of $420.9 million. Validus Re segment loss ratios excluding, notable loss events, reserve for potential development on notable loss events and prior year loss reserve development for the year ended December 31, 2012 and 2011 were 23.9% and 27.4%, respectively. Details of Validus Re loss ratios by line of business and period of occurrence are provided below.

	Year Ended December 31, 2012 (a)	2011 (b)	2010 (b)
Property—current period excluding items below	18.5 %	21.0 %	16.6 %
Property—current period—notable losses	41.1 %	61.1 %	46.5 %
Property—current period—reserve for potential development on notable loss events	0.0 %	11.0 %	1.1 %
Property—change in prior accident years	(6.8)%	(7.4)%	(6.6)%
Property—loss ratio	52.8 %	85.7 %	57.6 %
Marine—current period excluding items below	36.3 %	44.0 %	36.5 %
Marine—current period—notable losses	40.3 %		