OneBeacon Insurance Group, Ltd.
Form 10-Q
August 03, 2015

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

FORM 10-Q

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

For the quarterly period ended June 30, 2015

OR

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

For the transition period from to

Commission file number 1-33128

ONEBEACON INSURANCE GROUP, LTD.
(Exact name of Registrant as specified in its charter)

Bermuda (State or other jurisdiction of incorporation or organization)	98-0503315 (I.R.S. Employer Identification No.)
601 Carlson Parkway Minnetonka, Minnesota (Address of principal executive offices)	55305 (Zip Code)

Registrant's telephone number, including area code: (952) 852-2431

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 x 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes x No 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.

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

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

As of July 30, 2015, 23,509,098 Class A common shares, par value $0.01 per share, and 71,754,738 Class B common shares, par value $0.01 per share, were outstanding.

ONEBEACON INSURANCE GROUP, LTD.

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

ONEBEACON INSURANCE GROUP, LTD.
CONSOLIDATED BALANCE SHEETS
(Unaudited)

($ in millions, except per share amounts)	June 30, 2015	December 31, 2014
Assets		
Investment Securities:		
Fixed maturity investments, at fair value	$1,941.1	$1,799.8
Short-term investments, at amortized cost (which approximates fair value)	157.9	202.2
Common equity securities, at fair value	304.3	320.0
Convertible fixed maturity investments, at fair value	—	5.0
Other investments	174.9	198.8
Total investment securities	2,578.2	2,525.8
Cash	106.2	87.0
Reinsurance recoverables	168.0	173.8
Premiums receivable	292.2	241.5
Funds held under reinsurance contracts	49.3	37.1
Deferred acquisition costs	111.8	103.2
Net deferred tax asset	136.5	131.8
Investment income accrued	10.3	10.0
Accounts receivable on unsettled investment sales	1.1	7.2
Other assets	208.7	202.7
Assets held for sale	—	58.1
Total assets	$3,662.3	$3,578.2
Liabilities		
Unpaid loss and loss adjustment expense reserves	$1,350.8	$1,342.2
Unearned premiums	616.2	588.3
Funds held under insurance contracts	102.6	81.0
Debt	274.7	274.7
Accounts payable on unsettled investment purchases	20.1	0.5
Other liabilities	261.2	242.2
Total liabilities	2,625.6	2,528.9
OneBeacon's common shareholders' equity and noncontrolling interests		
OneBeacon's common shareholders' equity		
Common shares and paid-in surplus (par value $0.01; authorized, 200,000,000 shares; issued and outstanding, 95,263,836 and 95,296,387 shares)	1,023.2	1,023.7
Retained earnings	14.8	27.3
Accumulated other comprehensive loss	(4.8)	(5.2)
Total OneBeacon's common shareholders' equity	1,033.2	1,045.8
Total noncontrolling interests	3.5	3.5
Total OneBeacon's common shareholders' equity and noncontrolling interests	1,036.7	1,049.3
Total liabilities, OneBeacon's common shareholders' equity and noncontrolling interests	$3,662.3	$3,578.2

See Notes to Consolidated Financial Statements.

1

Table of Contents

ONEBEACON INSURANCE GROUP, LTD.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
($ in millions, except per share amounts)	2015	2014	2015	2014
Revenues				
Earned premiums	$319.3	$290.9	$605.9	$567.4
Net investment income	10.1	12.2	20.6	22.6
Net realized and change in unrealized investment gains	(14.0)	21.9	0.2	40.8
Net other revenues (expenses)	(1.2)	1.0	(4.3)	2.0
Total revenues	314.2	326.0	622.4	632.8
Expenses				
Loss and loss adjustment expenses	194.5	186.1	360.4	335.5
Policy acquisition expenses	56.4	49.6	107.4	96.3
Other underwriting expenses	52.9	51.7	108.8	101.1
General and administrative expenses	4.2	3.6	8.3	6.9
Interest expense	3.3	3.3	6.5	6.5
Total expenses	311.3	294.3	591.4	546.3
Pre-tax income from continuing operations	2.9	31.7	31.0	86.5
Income tax benefit (expense)	0.9	(5.9)	(2.5)	(13.0)
Net income from continuing operations	3.8	25.8	28.5	73.5
Loss from discontinued operations, net of tax	(0.2)	(0.1)	(0.3)	(0.6)
(Loss) gain from sale of discontinued operations, net of tax	0.3	(0.5)	0.3	(0.5)
Net income, including noncontrolling interests	3.9	25.2	28.5	72.4
Less: Net income attributable to noncontrolling interests	(0.5)	(0.5)	(1.0)	(0.9)
Net income attributable to OneBeacon's common shareholders	3.4	24.7	27.5	71.5
Other comprehensive income, net of tax	0.2	0.1	0.4	0.1
Comprehensive income attributable to OneBeacon's common shareholders	$3.6	$24.8	$27.9	$71.6
Earnings per share attributable to OneBeacon's common shareholders—basic and diluted				
Net income from continuing operations, per share	$0.03	$0.26	$0.29	$0.76
Loss from discontinued operations, net of tax, per share	—	—	—	(0.01)
Net income attributable to OneBeacon's common shareholders per share	$0.03	$0.26	$0.29	$0.75
Dividends declared and paid per OneBeacon's common share	$0.21	$0.21	$0.42	$0.42

See Notes to Consolidated Financial Statements.

2

Table of Contents

ONEBEACON INSURANCE GROUP, LTD.
CONSOLIDATED STATEMENTS OF COMMON SHAREHOLDERS' EQUITY
(Unaudited)

($ in millions)	OneBeacon's Common Shareholders' Equity					Total OneBeacon's common shareholders' equity and noncontrolling interests
	Common shares and paid-in surplus	Retained earnings	Accum. other comprehensive income (loss)	Total OneBeacon common shareholders' equity	Noncontrolling interests, after tax	
Balances at January 1, 2015	$ 1,023.7	$ 27.3	$ (5.2)	$ 1,045.8	$ 3.5	$ 1,049.3
Comprehensive income:						
Net income	—	27.5	—	27.5	1.0	28.5
Other comprehensive income, net of tax	—	—	0.4	0.4	—	0.4
Total comprehensive income	—	27.5	0.4	27.9	1.0	28.9
Amortization of restricted share awards	1.1	—	—	1.1	—	1.1
Issuance of common shares	—	—	—	—	0.1	0.1
Repurchase and retirement of common shares	(1.6)	—	—	(1.6)	—	(1.6)
Dividends	—	(40.0)	—	(40.0)	(1.1)	(41.1)
Balances at June 30, 2015	$ 1,023.2	$ 14.8	$ (4.8)	$ 1,033.2	$ 3.5	$ 1,036.7

($ in millions)	OneBeacon's Common Shareholders' Equity					Total OneBeacon's common shareholders' equity and noncontrolling interests
	Common shares and paid-in surplus	Retained earnings	Accum. other comprehensive income	Total OneBeacon common shareholders' equity	Noncontrolling interests, after tax	
Balances at January 1, 2014	$ 1,022.5	$ 74.4	$ 6.8	$ 1,103.7	$ 3.1	$ 1,106.8
Comprehensive income:						
Net income	—	71.5	—	71.5	0.9	72.4
Other comprehensive income, net of tax	—	—	0.1	0.1	—	0.1
Total comprehensive income	—	71.5	0.1	71.6	0.9	72.5
Amortization of restricted share awards	1.6	—	—	1.6	—	1.6
Issuance of common shares	—	—	—	—	0.2	0.2
Repurchase and retirement of common shares	(1.8)	—	—	(1.8)	—	(1.8)
Dividends	—	(40.0)	—	(40.0)	(1.0)	(41.0)
Balances at June 30, 2014	$ 1,022.3	$ 105.9	$ 6.9	$ 1,135.1	$ 3.2	$ 1,138.3

See Notes to Consolidated Financial Statements.

Table of Contents

ONEBEACON INSURANCE GROUP, LTD.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six months ended June 30,	
($ in millions)	2015	2014
Cash flows from operations:		
Net income including noncontrolling interests	$28.5	$72.4
Charges (credits) to reconcile net income to cash flows provided from operations:		
Net loss from discontinued operations	0.3	0.6
Net loss (gain) from sale of discontinued operations	(0.3)	0.5
Net realized and change in unrealized investment gains	(0.2)	(40.8)
Net adjustment to gain on sale of business	3.7	—
Deferred income tax expense (benefit)	(3.8)	12.6
Other operating items:		
Net change in loss and LAE reserves	8.6	71.1
Net change in unearned premiums	27.9	47.0
Net change in premiums receivable	(50.7)	(47.8)
Net change in reinsurance recoverables on paid and unpaid losses	5.8	(5.4)
Net change in funds held under reinsurance contracts	(12.2)	(30.0)
Net change in funds held under insurance contracts	21.6	(0.3)
Net change in other assets and liabilities	13.6	(24.4)
Net cash provided from operations—continuing operations	42.8	55.5
Net cash used for operations—discontinued operations	(0.3)	(33.9)
Net cash provided from operations	42.5	21.6
Cash flows from investing activities:		
Net maturities, purchases and sales of short-term investments	44.3	80.1
Maturities of fixed maturity investments	115.8	185.6
Sales of fixed maturity investments	450.0	850.9
Sales of common equity securities	268.1	47.6
Sales of convertible fixed maturity investments	6.1	12.2
Return of capital and distributions of other investments	22.1	3.2
Purchases of fixed maturity investments	(714.1)	(1,101.9)
Purchases of common equity securities	(248.7)	(48.7)
Purchases of convertible fixed maturity investments	(0.8)	(8.4)
Contributions for other investments	(2.5)	(3.3)
Net change in unsettled investment purchases and sales	25.8	(31.8)
Proceeds from sale of property and equipment	56.8	—
Net acquisitions of property and equipment	(1.8)	(0.7)
Net cash provided from (used for) investing activities	21.1	(15.2)
Cash flows from financing activities:		
Cash dividends paid to common shareholders	(40.0)	(40.0)
Repurchases and retirements of common stock	(1.6)	(1.8)
Payments on capital lease obligation	(2.8)	(2.6)
Net cash used for financing activities	(44.4)	(44.4)
Net increase (decrease) in cash during period	19.2	(38.0)
Cash balance at beginning of period	87.0	168.1
Cash balance at end of period	$106.2	$130.1

See Notes to Consolidated Financial Statements.

Table of Contents
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. Nature of Operations and Summary of Significant Accounting Policies
Basis of presentation
These interim consolidated financial statements include the accounts of OneBeacon Insurance Group, Ltd. (the "Company" or the "Registrant") and its subsidiaries (collectively, "OneBeacon") and have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The Company is an exempted Bermuda limited liability company with U.S.-based underwriting operating companies that are property and casualty insurance writers and a Bermuda-based reinsurance company, Split Rock Insurance, Ltd. ("Split Rock"), which primarily reinsures certain risks of affiliated entities. OneBeacon offers a wide range of specialty insurance products and services primarily through independent agencies, regional and national brokers, wholesalers and managing general agencies.
OneBeacon is 75.3% owned by White Mountains Insurance Group, Ltd. ("White Mountains"), a holding company whose businesses provide property and casualty insurance, reinsurance and certain other products. The Company's headquarters are located at 14 Wesley Street, 5th Floor, Hamilton HM 11, Bermuda. The Company's U.S. corporate headquarters are located at 601 Carlson Parkway, Minnetonka, Minnesota 55305 and its registered office is located at Clarendon House, 2 Church Street, Hamilton HM 11, Bermuda. During the three months ended June 30, 2015 OneBeacon sold its building in Canton, Massachusetts, which is presented as held for sale in the December 31, 2014 consolidated balance sheets.
On December 23, 2014, OneBeacon completed the sale of its run-off business to a subsidiary of Armour Group Holdings Limited (“Armour”). See Note 2—"Acquisitions and Dispositions" and Note 15—"Discontinued Operations." The run-off business included the results of OneBeacon's non-specialty commercial lines business and certain other run-off business, including the vast majority of asbestos and environmental reserves, as well as certain purchase accounting adjustments related to the run-off business (the “Runoff Business,” the sale of which is referred to as the “Runoff Transaction”). The Runoff Business has been presented as discontinued operations in the consolidated statements of operations for the three and six months ended June 30, 2015 and 2014 and in the consolidated statements of cash flows for the six months ended June 30, 2015 and 2014. The Runoff Business disposal group excludes investing and financing activities from amounts classified as discontinued operations. OneBeacon's investing and financing operations are conducted on an overall consolidated level and, accordingly, there are no separately identifiable investing or financing cash flows associated with the Runoff Business. The legal entities included in the sale held an agreed upon level of invested assets and capital at closing.
OneBeacon's reportable segments are Specialty Products, Specialty Industries and Investing, Financing and Corporate. The Specialty Products segment is comprised of ten active underwriting operating segments, representing an aggregation based on those that offer distinct products and tailored coverages and services to a broad customer base across the United States. During the first quarter of 2015, the Company restructured its former Professional Insurance underwriting operating segment into four separate underwriting operating segments, which are included in Specialty Products: Healthcare, Management Liability, Financial Services and Other Professional Lines.
The Specialty Industries segment is comprised of five active underwriting operating segments, representing an aggregation based on those that focus on solving the unique needs of a particular customer or industry group.
The Investing, Financing and Corporate segment includes the investing and financing activities for OneBeacon on a consolidated basis, and certain other activities conducted through the Company and its intermediate subsidiaries.
All significant intercompany transactions have been eliminated in consolidation. These interim financial statements include all adjustments considered necessary by management to fairly state the financial position, results of operations and cash flows of OneBeacon. These interim financial statements may not be indicative of financial results for the full year and should be read in conjunction with the Company’s 2014 Annual Report on Form 10-K. The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Refer to the Company’s 2014 Annual Report on Form 10-K for a complete discussion regarding OneBeacon’s significant accounting policies. Certain

amounts in the prior period financial statements have been reclassified to conform to the current presentation.
Recently Adopted Changes in Accounting Principles
Qualified Affordable Housing Projects
Effective January 1, 2015, OneBeacon adopted ASU 2014-01, Accounting for Investments in Qualified Affordable Housing Projects ("QAHP") (ASC 323). ASU 2014-01 allows investors in QAHP to make a policy election to use the proportional amortization method. Under the proportional amortization method, the investor amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the investment results, net of the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
NOTE 1. Nature of Operations and Summary of Significant Accounting Policies

related tax benefits, as a component of income tax expense. Prior to adoption, OneBeacon accounted for its QAHP investment under the equity method and recognized its share of its QAHP investment's losses in investment income. OneBeacon made the policy election to account for its QAHP investment using the proportional amortization method, applied retrospectively. Under the proportional amortization method, the cumulative loss recognized through December 31, 2014 increased by $1.2 million. As a result of the retrospective adoption, OneBeacon's common shareholders equity has been reduced by $0.6 million as of January 1, 2014. In addition, for the three and six months ended June 30, 2014, the retrospective adoption resulted in increases of $0.5 million and $0.9 million, respectively, to net investment income and net increases of $0.6 million and $1.2 million, respectively, to income tax expense. Footnote disclosures for prior year amounts have been amended to be consistent with the restated amounts described above.

Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity

In April 2014, the Financial Accounting Standard Board ("FASB") issued ASU 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity (ASC 205 and ASC 360) to reduce diversity in practice for reporting discontinued operations. ASU 2014-08 limits discontinued operations treatment to disposals that represent a strategic shift and that have a major effect on a reporting entity's operations and financial results to be reported as discontinued operations. The revised guidance also requires expanded disclosure in the financial statements for discontinued operations as well as for disposals of significant components of an entity that do not qualify for discontinued operations presentation. OneBeacon has not had any transactions that occurred since ASU 2014-08 became effective on December 15, 2014.

Pushdown Accounting

ASU 2014-17, Pushdown Accounting, a consensus of the FASB Emerging Issues Task Force (ASC 805) became effective upon its issuance on November 18, 2014. The new guidance, which is applicable prospectively, gives an acquired non-public company the option to apply pushdown accounting in its separate company financial statements in the period in which it is acquired in a change of control transaction. Once pushdown accounting has been applied, the election is irreversible. Acquired entities that chose not to apply pushdown accounting at the time of acquisition, may apply pushdown accounting in a subsequent period as a change in accounting principle under ASC 250, Accounting Changes and Error Corrections. OneBeacon has not had any acquisitions since ASU 2014-17 became effective.

Unrecognized Tax Benefits

Effective January 1, 2014, OneBeacon adopted ASU 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. The new ASU generally requires balance sheet presentation of an unrecognized tax benefit as a reduction of a deferred tax asset for a net operating loss ("NOL") carryforward or tax credit carryforward rather than as a liability. This adoption did not have any impact on the Company's financial position, results of operations, cash flows or financial statement presentation.

Recently Issued Accounting Pronouncements

Insurance Contracts

In May 2015, the FASB issued ASU 2015-09, Disclosures about Short Duration Contracts (ASC 944) which requires expanded footnote disclosures about loss and loss adjustment expense ("LAE") reserves. Under the new guidance, some disclosures currently presented outside of OneBeacon's financial statements, such as loss development tables and a reconciliation of loss development data to the loss and LAE reserves reflected on the balance sheet, will become part of the financial statement footnotes. In addition, the loss development tables required to be presented under the new ASU must be presented on a disaggregated basis by accident year rather than by reporting year as currently presented. Some of the expanded disclosures are new requirements, such as the disclosure of reserves for losses incurred but not reported ("IBNR") plus expected development on reported claims, which must be presented by accident year on a disaggregated basis. The new guidance also requires new disclosures about claim frequency data together with descriptions of the approach used to measure that data. Qualitative descriptions of methodologies and assumptions used to develop IBNR estimates must be presented together with the disaggregated amounts of IBNR to which they relate, along with a discussion of any significant changes in methodology and assumptions and the related effect upon the loss reserves. The new guidance will be effective for annual periods beginning after December 15, 2015 and interim periods within annual periods beginning after December 15, 2016 with retrospective restatement of prior periods required. OneBeacon will modify its financial statement footnote disclosures to conform to the requirements of ASU 2015-09 upon adoption, including revisions to prior year's disclosures.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
NOTE 1. Nature of Operations and Summary of Significant Accounting Policies

Fair Value Measurements
In May 2015, the FASB issued ASU 2015-07, Fair Value Measurement - Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent) (ASC 820) which eliminates the requirement to disclose the fair value hierarchy level for investments for which fair value is measured at net asset value using the practical expedient in ASC 820. OneBeacon measures the fair value of its investments in hedge funds and private equity funds using this practical expedient and has classified those measurements within Level 3 of the fair value hierarchy. The new guidance is effective for fiscal years beginning after December 15, 2015 and interim periods within those fiscal years.

Debt Issuance Costs
In April 2015, the FASB issued ASU 2015-03, Imputation of Interest (ASC 835) which requires debt issuance costs related to a recognized debt liability to be presented as a deduction from the carrying amount of the related debt, consistent with the treatment required for debt discounts. ASU 2015-03 is effective for annual and interim reporting periods beginning after December 15, 2015. OneBeacon does not expect ASU 2015-03 to impact its financial position, results of operations, cash flows, presentation and disclosures.

Amendments to Consolidation Analysis
In February 2015, the FASB issued ASU 2015-02, Amendments to the Consolidation Analysis (ASC 810) which amends the guidance for determining whether an entity is a variable interest entity ("VIE"). ASU 2015-02 eliminates the separate consolidation guidance for limited partnerships and with it, the presumption that a general partner should consolidate a limited partnership. In addition, ASU 2015-02 changes the guidance for determining if fee arrangements qualify as variable interests and the effect fee arrangements have on the determination of the primary beneficiary. ASU 2015-02 is effective for annual and interim reporting periods beginning after December 15, 2015 and must be applied retrospectively. OneBeacon does not expect ASU 2015-02 to affect the consolidation analysis for any of its existing investments.

Share-Based Compensation Awards
In June 2014, the FASB issued ASU 2014-12, Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period. The new guidance is intended to eliminate diversity in practice for employee share-based awards containing performance targets that could be achieved after the requisite service period. Some reporting entities account for performance targets that can be achieved after the requisite service period as performance conditions that affect the vesting of the award while other reporting entities treat those performance targets as non-vesting conditions that affect the grant-date fair value of the award. The updated guidance requires that a performance target that affects vesting and that can be achieved after the requisite service period be treated as a performance condition. Compensation cost should be recognized in the period it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the periods for which service has been rendered. The new guidance is effective for annual and interim reporting periods beginning after December 15, 2015. OneBeacon does not expect adoption to have a significant impact on its financial position, results of operations, cash flows, presentation or disclosures.

Revenue Recognition
In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (ASC 606), which modifies the guidance for revenue recognition. The scope of the new ASU excludes insurance contracts but is applicable to certain fee arrangements, such as investment management fees. The Company is in the process of evaluating the new guidance and has not yet determined the potential effect of adoption on its financial position, results of operations, or cash flows. ASU 2014-09 is effective for annual and interim reporting periods beginning after December 15, 2016.

NOTE 2. Acquisitions and Dispositions

Runoff Business
As described in Note 1—"Nature of Operations and Summary of Significant Accounting Policies," on December 23, 2014, OneBeacon completed the sale of its Runoff Business to Armour. As described in Note 15—"Discontinued

Operations," the Company recorded the final adjustment to the loss on sale of discontinued operations during the second quarter of 2015. Prior to the closing of the Runoff Transaction, OneBeacon Insurance Company, one of the entities that was sold upon the closing of the Runoff Transaction and which has since been renamed Bedivere Insurance Company ("Bedivere"), distributed Atlantic Specialty Insurance Company ("ASIC') to its immediate parent, as well as cash and investments such that Bedivere contained the target capital on the date of sale pursuant to the stock purchase agreement. In conjunction with the Runoff Transaction, OneBeacon provided financing in the form of surplus notes having a par value of $101.0 million, which had a fair value of $64.9 million on the date of sale. As part of the Runoff Transaction, OneBeacon and Armour entered into a limited

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
NOTE 2. Acquisitions and Dispositions

Transition Services Agreement (“TSA”), pursuant to which OneBeacon is providing certain transition services to Armour during the term of the TSA, which has an initial term of one year. See Note 15—"Discontinued Operations" for further information regarding activity reported as discontinued operations during the three and six months ended June 30, 2015 and 2014.

Essentia Insurance Company

Effective January 1, 2013, OneBeacon completed the sale of Essentia Insurance Company ("Essentia"), an indirect wholly-owned subsidiary which wrote the collector cars and boats business, to Markel Corporation and recognized a pre-tax gain on sale of $23.0 million ($15.0 million after tax) in the first quarter of 2013. During the first quarter of 2015, the Company recognized in net other revenues (expenses) a $3.7 million negative adjustment to the pre-tax gain on sale of Essentia in connection with an assessment from the Michigan Catastrophic Claims Association (MCCA) payable to Markel Corporation pursuant to the indemnification provisions in the stock purchase agreement governing the sale of Essentia.

Except as described above, during the three and six months ended June 30, 2015 and 2014, there were no significant acquisitions or dispositions.

NOTE 3. Unpaid Loss and Loss Adjustment Expense (LAE) Reserves

Loss and LAE reserve summary

The following table summarizes the loss and LAE reserve activities of OneBeacon's insurance subsidiaries for the three and six months ended June 30, 2015 and 2014:

	Three months ended June 30,		Six months ended June 30,	
($ in millions)	2015	2014	2015	2014
Gross beginning balance	$1,304.0	$1,069.8	$1,342.2	$1,054.3
Less beginning reinsurance recoverables on unpaid losses	(141.6)	(80.1)	(161.6)	(80.2)
Net beginning loss and LAE reserves	1,162.4	989.7	1,180.6	974.1
Loss and LAE incurred relating to:				
Current year losses	194.5	177.7	362.2	328.5
Prior year losses	—	8.4	(1.8)	7.0
Total incurred loss and LAE from continuing operations	194.5	186.1	360.4	335.5
Loss and LAE paid relating to:				
Current year losses	(42.7)	(41.3)	(64.8)	(59.6)
Prior year losses	(110.5)	(101.1)	(272.5)	(216.6)
Total loss and LAE payments from continuing operations	(153.2)	(142.4)	(337.3)	(276.2)
Net ending loss and LAE reserves	1,203.7	1,033.4	1,203.7	1,033.4
Plus ending reinsurance recoverables on unpaid losses	147.1	92.0	147.1	92.0
Gross ending loss and LAE reserves	$1,350.8	$1,125.4	$1,350.8	$1,125.4

Loss and LAE development

Loss and LAE development—2015

During the three months ended June 30, 2015, OneBeacon experienced no net loss and LAE reserve development on prior accident year reserves, as favorable development from several businesses, most notably Specialty Property and Surety, was offset by unfavorable development primarily due to a large claim in Entertainment and an increase in the frequency of small to medium losses in the ocean marine business within International Marine Underwriters (IMU).

During the six months ended June 30, 2015, OneBeacon experienced $1.8 million of net favorable loss and LAE reserve development on prior accident year reserves, primarily attributable to favorable development from Crop resulting from the 2014 crop year and favorable development in several other businesses, most notably Technology, Specialty Property, Government Risks, and Surety. This favorable development was mostly offset by unfavorable development in Entertainment

8

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
NOTE 3. Unpaid Loss and Loss Adjustment Expense (LAE) Reserves

driven by several large losses and small to mid-sized claims and by losses within the Company's inland marine business within IMU resulting from a few large claims and, to a lesser extent, from Tuition Reimbursement.

Loss and LAE development—2014

During the three months ended June 30, 2014, OneBeacon experienced $8.4 million of net unfavorable loss and LAE reserve development on prior accident year reserves primarily related to its Other Professional Lines and Management Liability underwriting operating segments, as well as its Entertainment, Government Risks and Accident underwriting operating segments, partially offset by favorable loss and LAE reserve development primarily in its Specialty Property underwriting operating segment. The unfavorable development was driven by a few large claims.

During the six months ended June 30, 2014, OneBeacon experienced $7.0 million of net unfavorable loss and LAE reserve development on prior accident year reserves primarily related to its Management Liability and Other Professional Lines underwriting operating segments, as well as its Entertainment, Government Risks and Accident underwriting operating segments, partially offset by favorable loss and LAE reserve development in its Specialty Property underwriting operating segment, as well as its IMU underwriting operating segment. The unfavorable development was driven by a few large claims.

See Note 15—"Discontinued Operations" for a discussion of impacts to reserves for unpaid losses and LAE related to discontinued operations.

NOTE 4. Reinsurance

In the normal course of business, OneBeacon's insurance subsidiaries seek to limit losses that may arise from catastrophes or other events by reinsuring with third-party reinsurers. OneBeacon remains liable for risks reinsured even if the reinsurer does not honor its obligations under reinsurance contracts.

Reinsurance Treaties

The Company's catastrophe reinsurance coverage is discussed in Note 4—"Reinsurance" in the Company's 2014 Annual Report on Form 10-K. Except as discussed below, there have been no material changes to the Company's reinsurance coverage from that reported in the 2014 Annual Report on Form 10-K.

Effective May 1, 2015, OneBeacon renewed its property catastrophe reinsurance program through April 30, 2016. The program provides coverage for OneBeacon's property business as well as certain acts of terrorism. Under the program, the first $20.0 million of losses resulting from any single catastrophe are retained, with 95.0% of the next $10.0 million of losses and 100.0% of the next $100.0 million of losses resulting from the catastrophe being reinsured. Any part of a catastrophe loss in excess of $130.0 million would be retained in full. In the event of a catastrophe, OneBeacon's property catastrophe reinsurance program is reinstated for the remainder of the original contract term by paying a reinstatement premium that is based on the percentage of coverage reinstated and the original property catastrophe coverage premium.

Also effective May 1, 2015, OneBeacon lowered its retention on its property-per-risk reinsurance program from $5.0 million to $3.0 million.

Additionally, effective June 1, 2015, OneBeacon lowered its retentions on certain casualty and healthcare treaties from $5.0 million to $3.0 million.

Effective January 1, 2015, OneBeacon purchased an aggregate stop loss on its multi-peril crop insurance ("MPCI") portfolio for the 2015 crop year, providing 52.0% of coverage in excess of a 98.0% loss ratio on premiums covered by the contract and a separate aggregate stop loss providing 80.0% of coverage in excess of a 100.0% loss ratio on its crop-hail portfolio. OneBeacon also purchased a new quota share reinsurance contract on 30.0% of its MPCI portfolio.

In addition to the reinsurance protections outlined above, the Company also continued to purchase dedicated reinsurance protection for certain specific lines of business.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
NOTE 4. Reinsurance

Reinsurance Recoverables
As of June 30, 2015, OneBeacon had reinsurance recoverables on paid losses of $20.9 million and reinsurance recoverables on unpaid losses of $147.1 million. As reinsurance contracts do not relieve OneBeacon of its obligations, collectibility of balances due from reinsurers is critical to OneBeacon's financial strength. The following table summarizes Standard & Poor's Financial Services, LLC ("Standard & Poor's") ratings for OneBeacon's reinsurers for its continuing insurance operations, excluding industry pools and associations, based upon reinsurance recoverable amounts on paid and unpaid losses and LAE:

($ in millions) Standard & Poor's Rating[1]:	Balance at June 30, 2015	% of total	
AA	$63.1	38	%
A	82.3	49	%
BBB, Not Rated and Other	22.6	13	%
Total reinsurance recoverables	$168.0	100	%

[1] Standard & Poor's ratings as detailed above are "AA" (Very strong), "A" (Strong) and "BBB" (Adequate).

NOTE 5. Investment Securities
OneBeacon's invested assets are comprised of securities and other investments held for general investment purposes. Refer to the Company's 2014 Annual Report on Form 10-K for a complete discussion.
OneBeacon classifies its portfolio of fixed maturity investments, common equity securities and convertible fixed maturity investments held for general investment purposes as trading securities. Trading securities are reported at fair value as of the balance sheet date as determined by quoted market prices when available. Realized and change in unrealized investment gains on trading securities are reported in total revenues as net realized and unrealized investment gains in revenues on a pre-tax basis.
Short-term investments consist of money market funds, certificates of deposit and other securities which, at the time of purchase, mature or become available for use within one year. Short-term investments are carried at amortized cost, which approximates fair value.
Other investments primarily include surplus notes, private equity funds and hedge funds. OneBeacon measures its investments in private equity funds and hedge funds at fair value with changes therein reported in total revenues as net realized and change in unrealized investment gains. Surplus notes provided in conjunction with the financing of the Runoff Transaction are measured at their estimated fair value based on discounted expected cash flows, with changes in fair value reported in total revenues as net realized and change in unrealized investment gains. Other investments also include an investment in a community reinvestment vehicle which is accounted for at fair value, with changes in fair value reported in total revenues as net realized and change in unrealized investment gains and a tax advantaged federal affordable housing development fund which is accounted for under the proportional amortization method.
Prospector Partners, LLC (“Prospector”), was the primary manager of OneBeacon's publicly-traded common equity securities and convertible fixed maturity securities portfolio. The Prospector-managed separate accounts were liquidated during the second quarter of 2015, and the Prospector-managed hedge fund was redeemed, with the intention to convert the majority of the proceeds to passive equity vehicles. As the separate accounts were liquidated, OneBeacon reinvested the majority of the proceeds into exchange traded funds ("ETFs") that seek to provide investment results that, before expenses, generally correspond to the performance of the S&P 500, Russell 1000, and Russell 1000 Value indices.

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
NOTE 5. Investment Securities

OneBeacon's net investment income is comprised primarily of interest income associated with fixed maturity investments and dividend income from its equity investments.
Net investment income for the three and six months ended June 30, 2015 and 2014 consisted of the following:

	Three months ended June 30,		Six months ended June 30,	
($ in millions)	2015	2014	2015	2014
Fixed maturity investments	$10.3	$10.6	$20.5	$20.9
Common equity securities	1.5	2.0	3.1	3.7
Convertible fixed maturity investments	—	0.1	—	0.1
Other investments	(0.1)	1.1	—	1.2
Gross investment income	11.7	13.8	23.6	25.9
Less investment expenses	(1.6)	(1.6)	(3.0)	(3.3)
Net investment income, pre-tax	$10.1	$12.2	$20.6	$22.6

The composition of net realized investment gains consisted of the following:

	Three months ended June 30,		Six months ended June 30,	
($ in millions)	2015	2014	2015	2014
Fixed maturity investments	$1.2	$1.6	$1.9	$2.4
Common equity securities	24.6	6.5	34.4	11.9
Convertible fixed maturity investments	0.3	1.2	0.3	2.3
Other investments	9.1	—	8.1	—
Net realized investment gains, pre-tax	$35.2	$9.3	$44.7	$16.6

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
NOTE 5. Investment Securities

The net changes in fair value for the three and six months ended June 30, 2015 and 2014 are as follows:

($ in millions)	Three months ended June 30, 2015			Six months ended June 30, 2015		
	Changes in net unrealized investment gains	Changes in net foreign currency gains (losses)	Total net changes in fair value reflected in revenues	Changes in net unrealized investment gains	Changes in net foreign currency gains (losses)	Total net changes in fair value reflected in revenues
Fixed maturity investments	$(9.1)	$—	$(9.1)	$(2.5)	$—	$(2.5)
Short-term investments	—	—	—	—	—	—
Common equity securities	(26.5)	0.3	(26.2)	(30.9)	0.2	(30.7)
Convertible fixed maturity investments	(0.3)	—	(0.3)	0.1	—	0.1
Other investments	(13.6)	—	(13.6)	(11.4)	—	(11.4)
Net change, pre-tax	$(49.5)	$0.3	$(49.2)	$(44.7)	$0.2	$(44.5)

($ in millions)	Three months ended June 30, 2014			Six months ended June 30, 2014		
	Changes in net unrealized investment gains	Changes in net foreign currency gains (losses)	Total net changes in fair value reflected in revenues	Changes in net unrealized investment gains	Changes in net foreign currency gains (losses)	Total net changes in fair value reflected in revenues
Fixed maturity investments	$7.3	$—	$7.3	$12.0	$—	$12.0
Common equity securities	6.6	—	6.6	9.7	—	9.7
Convertible fixed maturity investments	(3.0)	—	(3.0)	(2.3)	—	(2.3)
Other investments	1.7	—	1.7	4.8	—	4.8
Net change, pre-tax	$12.6	$—	$12.6	$24.2	$—	$24.2

The components of OneBeacon's ending net unrealized investment gains and losses, excluding the impact of net unrealized foreign currency translation gains and losses, on its investment portfolio as of June 30, 2015 and December 31, 2014 were as follows:

($ in millions)	June 30, 2015	December 31, 2014
Investment securities:		
Gross unrealized investment gains	$62.3	$104.7
Gross unrealized investment losses	(11.2)	(8.9)
Total net unrealized investment gains, pre-tax	51.1	95.8
Income taxes	(18.7)	(26.9)
Total net unrealized investment gains, after tax	$32.4	$68.9

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
NOTE 5. Investment Securities

The cost or amortized cost, gross unrealized pre-tax investment gains and losses, net foreign currency losses and carrying values of OneBeacon's fixed maturity investments as of June 30, 2015 and December 31, 2014 were as follows:

	June 30, 2015				
($ in millions)	Cost or amortized cost	Gross unrealized gains	Gross unrealized losses	Net unrealized foreign currency gains (losses)	Carrying value
U.S. Government and agency obligations	$43.8	$0.1	$—	$—	$43.9
Debt securities issued by industrial corporations	813.2	8.7	(0.6)	—	821.3
Municipal obligations	66.8	0.7	(0.5)	—	67.0
Asset-backed securities	922.5	2.7	(1.9)	—	923.3
Foreign government obligations	1.0	0.2	—	—	1.2
Preferred stocks	78.3	6.1	—		