

VALIDUS HOLDINGS LTD

Form 10-Q

November 06, 2009

Table of Contents

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

**FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended September 30, 2009  
Commission file number 001-33606**

**VALIDUS HOLDINGS, LTD.**  
(Exact name of registrant as specified in its charter)

**BERMUDA**  
(State or other jurisdiction of  
incorporation or organization)

**98-0501001**  
(I.R.S. Employer  
Identification No.)

**19 Par-La-Ville Road, Hamilton, Bermuda HM 11**  
(Address of principal executive offices and zip code)

**(441) 278-9000**

(Registrant's telephone number, including area code)

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  No**

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  No**

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  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a 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  No**

As of November 6, 2009, there were 131,134,398 outstanding Common Shares, \$0.175 par value per share, of the registrant.

**INDEX**

|   | <b>Page</b> |
|---|-------------|
| <b><u>PART I. FINANCIAL INFORMATION</u></b>   |             |
| <b><u>Item 1. Financial Statements:</u></b>   |             |
| <u>Consolidated Balance Sheets as at September 30, 2009 (Unaudited) and December 31, 2008</u>   | 3           |
| <u>Consolidated Statements of Operations and Comprehensive Income for the Three and Nine months ended September 30, 2009 and 2008 (Unaudited)</u> | 4           |
| <u>Consolidated Statements of Shareholders' Equity for the Nine months ended September 30, 2009 and 2008 (Unaudited)</u>                          | 5           |
| <u>Consolidated Statements of Cash Flows for the Nine months ended September 30, 2009 and 2008 (Unaudited)</u>                                    | 6           |
| <u>Notes to Consolidated Financial Statements (Unaudited)</u>   | 7           |
| <u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>  | 41          |
| <u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>   | 96          |
| <u>Item 4. Controls and Procedures</u>  | 98          |
| <b><u>PART II. OTHER INFORMATION</u></b>  |             |
| <u>Item 1. Legal Proceedings</u>  | 99          |
| <u>Item 1A. Risk Factors</u>  | 99          |
| <u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>  | 99          |
| <u>Item 3. Defaults Upon Senior Securities</u>  | 99          |
| <u>Item 4. Submission of Matters to a Vote of Security Holders</u>  | 99          |
| <u>Item 5. Other Information</u>  | 100         |
| <u>Item 6. Exhibits</u>   | 100         |
| <u>Signatures</u>   | 101         |
| EXHIBIT 10.1 AMENDMENT TO STANDBY LETTER OF CREDIT FACILITY   |             |
| EXHIBIT 10.2 SECOND AMENDMENT TO EACH OF THE THREE-YEAR AND FIVE YEAR UNSECURED LETTER OF CREDIT FACILITY AGREEMENTS                              |             |

EX-31.1

EX-31.2

EX-32

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**Table of Contents**

**PART I. FINANCIAL INFORMATION**

**ITEM I. FINANCIAL STATEMENTS**

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**Table of Contents****Validus Holdings, Ltd.**

Consolidated Balance Sheets

**As at September 30, 2009 (Unaudited) and December 31, 2008**

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

|   | <b>September<br/>30,<br/>2009<br/>(Unaudited)</b> | <b>December<br/>31,<br/>2008</b> |
|---|---|----------------------------------|
| <b>Assets</b>   |   |                                  |
| Fixed maturities, at fair value<br>(amortized cost: 2009 - \$4,566,801; 2008 - \$2,553,018)   | \$ 4,590,143                                      | \$ 2,454,501                     |
| Short-term investments, at fair value<br>(amortized cost: 2009 - \$595,557; 2008 - \$379,537) | 594,581   | 377,036                          |
| Other investments, at fair value<br>(amortized cost: 2009 - \$126,301)                        | 129,012   |                                  |
| Cash and cash equivalents   | 393,788   | 449,848                          |
| <b>Total investments and cash</b>   | <b>5,707,524</b>                                  | <b>3,281,385</b>                 |
| Premiums receivable   | 723,029   | 408,259                          |
| Deferred acquisition costs  | 139,157   | 108,156                          |
| Prepaid reinsurance premiums  | 101,711   | 22,459                           |
| Securities lending collateral   | 100,053   | 98,954                           |
| Loss reserves recoverable   | 172,101   | 208,796                          |
| Paid losses recoverable   | 10,064  | 1,388                            |
| Net receivable for investments sold   |   | 490                              |
| Income taxes recoverable  | 3,027   | 1,365                            |
| Intangibles assets  | 124,096   | 127,217                          |
| Goodwill  | 20,393  | 20,393                           |
| Accrued investment income   | 43,190  | 20,433                           |
| Other assets  | 32,726  | 23,185                           |
| <b>Total assets</b>   | <b>\$ 7,177,071</b>                               | <b>\$ 4,322,480</b>              |
| <b>Liabilities</b>  |   |                                  |
| Reserve for losses and loss expenses  | \$ 1,624,743                                      | \$ 1,305,303                     |
| Unearned premiums   | 955,049   | 539,450                          |
| Reinsurance balances payable  | 40,879  | 33,042                           |
| Securities lending payable  | 101,040   | 105,688                          |
| Deferred income taxes   | 26,110  | 21,779                           |
| Net payable for investments purchased   | 39,224  |                                  |
| Accounts payable and accrued expenses   | 119,534   | 74,184                           |
| Debentures payable  | 304,300   | 304,300                          |
| <b>Total liabilities</b>  | <b>3,210,879</b>                                  | <b>2,383,746</b>                 |

**Shareholders equity**

|  |                     |                     |
|--|---------------------|---------------------|
| Common shares, 571,428,571 authorized, par value \$0.175       |                     |                     |
| Issued and outstanding (2009 - 131,107,196; 2008 - 75,624,697) | 22,944              | 13,235              |
| Additional paid-in-capital                                     | 2,748,121           | 1,412,635           |
| Accumulated other comprehensive (loss)                         | (4,976)             | (7,858)             |
| Retained earnings  | 1,200,103           | 520,722             |
| <b>Total shareholders equity</b>                               | <b>3,966,192</b>    | <b>1,938,734</b>    |
| <br>   |                     |                     |
| <b>Total liabilities and shareholders equity</b>               | <b>\$ 7,177,071</b> | <b>\$ 4,322,480</b> |

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

**Table of Contents****Validus Holdings, Ltd.**

Consolidated Statements of Operations and Comprehensive Income (Loss)

**For the three and nine months ended September 30, 2009 and 2008 (Unaudited)**

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

|  | <b>Three months ended</b> |                     | <b>Nine months ended</b> |                    |
|--|---------------------------|---------------------|--------------------------|--------------------|
|  | <b>September</b>          | <b>September</b>    | <b>September</b>         | <b>September</b>   |
|  | <b>30,</b>                | <b>30,</b>          | <b>30,</b>               | <b>30,</b>         |
|  | <b>2009</b>               | <b>2008</b>         | <b>2009</b>              | <b>2008</b>        |
|  | <b>(Unaudited)</b>        | <b>(Unaudited)</b>  | <b>(Unaudited)</b>       | <b>(Unaudited)</b> |
| <b>Revenues</b>                              |                           |                     |                          |                    |
| Gross premiums written                       | \$ 331,028                | \$ 269,236          | \$ 1,365,951             | \$ 1,170,749       |
| Reinsurance premiums ceded                   | (67,687)                  | (35,139)            | (202,489)                | (121,438)          |
| Net premiums written                         | 263,341                   | 234,097             | 1,163,462                | 1,049,311          |
| Change in unearned premiums                  | 111,376                   | 105,229             | (141,786)                | (108,823)          |
| Net premiums earned                          | 374,717                   | 339,326             | 1,021,676                | 940,488            |
| Gain on bargain purchase, net of expenses    | 302,950                   |                     | 287,099                  |                    |
| Net investment income                        | 29,532                    | 36,379              | 83,267                   | 108,857            |
| Realized gain on repurchase of debentures    |                           |                     |                          | 8,752              |
| Net realized gains (losses) on investments   | 5,429                     | (13,667)            | (20,642)                 | (8,348)            |
| Net unrealized gains (losses) on investments | 50,437                    | (14,649)            | 109,839                  | (72,608)           |
| Other income                                 | 1,101                     | 1,269               | 2,875                    | 3,666              |
| Foreign exchange (losses)                    | (5,244)                   | (44,933)            | (1,012)                  | (35,843)           |
| <b>Total revenues</b>                        | <b>758,922</b>            | <b>303,725</b>      | <b>1,483,102</b>         | <b>944,964</b>     |
| <b>Expenses</b>                              |                           |                     |                          |                    |
| Losses and loss expenses                     | 134,152                   | 318,464             | 390,736                  | 580,578            |
| Policy acquisition costs                     | 64,236                    | 60,425              | 190,125                  | 173,545            |
| General and administrative expenses          | 46,036                    | 30,120              | 125,315                  | 101,139            |
| Share compensation expenses                  | 5,862                     | 6,012               | 18,848                   | 19,818             |
| Finance expenses                             | 11,257                    | 14,517              | 29,732                   | 48,796             |
| <b>Total expenses</b>                        | <b>261,543</b>            | <b>429,538</b>      | <b>754,756</b>           | <b>923,876</b>     |
| <b>Net income (loss) before taxes</b>        | <b>497,379</b>            | <b>(125,813)</b>    | <b>728,346</b>           | <b>21,088</b>      |
| Income tax benefit (expenses)                | 1,799                     | (487)               | 3,301                    | (4,992)            |
| <b>Net income (loss)</b>                     | <b>\$ 499,178</b>         | <b>\$ (126,300)</b> | <b>\$ 731,647</b>        | <b>\$ 16,096</b>   |
| <b>Comprehensive income</b>                  |                           |                     |                          |                    |
| Foreign currency translation adjustments     | (915)                     | (1,556)             | 2,882                    | (1,479)            |



|   |            |              |            |            |
|---|------------|--------------|------------|------------|
| <b>Comprehensive income (loss)</b>  | \$ 498,263 | \$ (127,856) | \$ 734,529 | \$ 14,617  |
| <b>Earnings per share</b>   |            |              |            |            |
| Weighted average number of common shares and common share equivalents outstanding |            |              |            |            |
| Basic   | 92,492,373 | 74,864,724   | 81,458,329 | 74,435,840 |
| Diluted   | 95,834,809 | 74,864,724   | 84,626,505 | 77,922,718 |
| <b>Basic earnings (loss) per share</b>  | \$ 5.38    | \$ (1.71)    | \$ 8.92    | \$ 0.15    |
| <b>Diluted earnings (loss) per share</b>  | \$ 5.21    | \$ (1.71)    | \$ 8.65    | \$ 0.14    |
| <b>Cash dividends declared per share</b>  | \$ 0.20    | \$ 0.20      | \$ 0.60    | \$ 0.60    |

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

4

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**Table of Contents****Validus Holdings, Ltd.**

Consolidated Statements of Shareholders' Equity

**For the nine months ended September 30, 2009 and 2008 (Unaudited)**

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

|   | <b>September 30,<br/>2009<br/>(Unaudited)</b> | <b>September 30,<br/>2008<br/>(Unaudited)</b> |
|---|---|---|
| <b>Common shares</b>                          |   |   |
| Balance Beginning of period                   | \$ 13,235                                     | \$ 12,985                                     |
| Issue of common shares                        | 9,709   | 119   |
| Balance End of period                         | \$ 22,944                                     | \$ 13,104                                     |
| <b>Additional paid-in capital</b>             |   |   |
| Balance Beginning of period                   | \$ 1,412,635                                  | \$ 1,384,604                                  |
| Issue of common shares, net of expenses       | 1,311,207                                     | (518)   |
| Share compensation expenses                   | 24,279  | 19,818  |
| Balance End of period                         | \$ 2,748,121                                  | \$ 1,403,904                                  |
| <b>Accumulated other comprehensive (loss)</b> |   |   |
| Balance Beginning of period                   | \$ (7,858)                                    | \$ (49)                                       |
| Currency translation adjustments              | 2,882   | (1,479)                                       |
| Balance End of period                         | \$ (4,976)                                    | \$ (1,528)                                    |
| <b>Retained earnings</b>                      |   |   |
| Balance Beginning of period                   | \$ 520,722                                    | \$ 537,260                                    |
| Dividends                                     | (52,266)                                      | (52,225)                                      |
| Net Income                                    | 731,647                                       | 16,096  |
| Balance End of period                         | \$ 1,200,103                                  | \$ 501,131                                    |
| <b>Total shareholders' equity</b>             | <b>\$ 3,966,192</b>                           | <b>\$ 1,916,611</b>                           |

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

**Table of Contents****Validus Holdings, Ltd.**

Consolidated Statements of Cash Flows

**For the nine months ended September 30, 2009 and 2008 (Unaudited)**

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

|   | <b>September<br/>30,<br/>2009<br/>(Unaudited)</b> | <b>September<br/>30,<br/>2008<br/>(Unaudited)</b> |
|---|---|---|
| <b>Cash flows provided by (used in) operating activities</b>                            |   |   |
| Net income  | \$ 731,647  | \$ 16,096   |
| Adjustments to reconcile net income to cash provided by (used in) operating activities: |   |   |
| Share compensation expenses   | 24,279  | 19,818  |
| Realized gain on repurchase of debentures   |   | (8,752)   |
| Bargain purchase gain   | (352,349)   |   |
| Net realized losses on investments  | 20,642  | 8,348   |
| Net unrealized (gains) losses on investments  | (109,838)   | 72,608  |
| Amortization of intangible assets   | 24,792  | 3,121   |
| Foreign exchange (gains) losses on cash and cash equivalents included in net income     | (10,487)  | 19,768  |
| Amortization of premium on fixed maturities   | 8,969   | 2,226   |
| Change in:  |   |   |
| Premiums receivable   | (134,007)   | (134,822)   |
| Deferred acquisition costs  | (8,914)   | (26,635)  |
| Prepaid reinsurance premiums  | (75,617)  | (28,149)  |
| Loss reserves recoverable   | 42,634  | (41,145)  |
| Paid losses recoverable   | (8,621)   | 4,279   |
| Income taxes recoverable  | (1,486)   | 2,436   |
| Accrued investment income   | 66  | (4,466)   |
| Other assets  | (557)   | 3,861   |
| Reserve for losses and loss expenses  | (8,900)   | 369,962   |
| Unearned premiums   | 210,099   | 147,461   |
| Reinsurance balances payable  | 3,903   | 17,779  |
| Deferred income taxes   | 4,731   | 6,083   |
| Accounts payable and accrued expenses   | (12,602)  | (52,500)  |
| <b>Net cash provided by operating activities</b>  | <b>348,384</b>                                    | <b>397,377</b>                                    |
| <b>Cash flows provided by (used in) investing activities</b>                            |   |   |
| Proceeds on sales of investments  | 2,247,581   | 1,770,892   |
| Proceeds on maturities of investments   | 466,065   | 264,103   |
| Purchases of fixed maturities   | (2,792,562)                                       | (2,355,159)                                       |
| Sales (purchases) of short-term investments, net  | 91,354  | (74,290)  |
| Purchases of other investments  | (2,047)   |   |
| Decrease in securities lending collateral   | 4,649   | 2,597   |
| Purchase of subsidiary, net of cash acquired  | (376,878)   |   |

|  |            |           |
|--|------------|-----------|
| <b>Net cash (used in) investing activities</b>                       | (361,838)  | (391,857) |
| <b>Cash flows provided by (used in) financing activities</b>         |            |           |
| Repurchase of debentures   |            | (36,948)  |
| Issue of common shares, net of expenses                              | (1,774)    | (398)     |
| Dividends paid   | (50,938)   | (50,570)  |
| (Decrease) in securities lending payable                             | (4,649)    | (2,597)   |
| <b>Net cash (used in) financing activities</b>                       | (57,361)   | (90,513)  |
| Effect of foreign currency rate changes on cash and cash equivalents | 14,755     | (24,338)  |
| Net (decrease) in cash   | (56,060)   | (109,331) |
| Cash and cash equivalents beginning of period                        | 449,848    | 444,698   |
| <b>Cash and cash equivalents end of period</b>                       | \$ 393,788 | 335,367   |
| <b>Taxes paid (recovered) during the period</b>                      | \$ 1,395   | (2,467)   |
| <b>Interest paid during the period</b>                               | \$ 20,016  | 20,802    |

The accompanying notes are an integral part of these consolidated financial statements (unaudited).

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

**1. Basis of preparation and consolidation**

These unaudited consolidated financial statements include Validus Holdings, Ltd. and its wholly owned subsidiaries (together, the Company) and have been prepared in accordance with U.S. Generally Accepted Accounting Principles (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In addition, the year-end balance sheet data was derived from audited financial statements but does not include all disclosures required by U.S. GAAP. This Quarterly Report should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2008, as filed with the U.S. Securities and Exchange Commission (the SEC).

In the opinion of management, these unaudited consolidated financial statements reflect all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the Company's financial position and results of operations as at the end of and for the periods presented. Certain amounts in prior periods have been reclassified to conform to current period presentation. All significant intercompany accounts and transactions have been eliminated. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. The major estimates reflected in the Company's consolidated financial statements include the reserve for losses and loss expenses, premium estimates for business written on a line slip or proportional basis, the valuation of goodwill and intangible assets, reinsurance recoverable balances including the provision for unrecoverable reinsurance recoverable balances and investment valuation. Actual results could differ from those estimates. The results of operations for any interim period are not necessarily indicative of the results for a full year.

**2. Significant accounting policies**

In addition to the policies set forth below, the significant accounting policies described in Part II, Item 8 of the Company's Annual Report on Form 10-K for the year ended December 31, 2008 should be read and considered.

**a) Business combinations**

On September 4, 2009, the Company acquired all of the outstanding shares of IPC Holdings, Ltd. (IPC). The transaction was accounted for as an acquisition method business combination. Accordingly, the purchase price was allocated to assets and liabilities based on their estimated fair value at the acquisition date. The consideration for the net assets acquired was concluded upon prior to the assessment of the fair value of the net assets at the acquisition date. Therefore, the excess of the value of the net assets acquired over the purchase price was recorded as gain on bargain purchase and is shown as a separate component of revenues in the Company's Consolidated Statements of Operations and Comprehensive Income (Loss) for the three and nine months ended September 30, 2009. Significant judgment is required to arrive at an estimate of fair value and changes to assumptions used could lead to a materially different result. Certain amounts in IPC's financial statements have been reclassified to conform to the Company's accounting policies.

**b) Other investments**

Other investments consist of an investment in a fund of hedge funds and a deferred compensation trust. All investment transactions are recorded on a first-in-first-out basis and realized gains and losses on the sale of

**Table of Contents****Validus Holdings, Ltd.**

## Notes to Consolidated Financial Statements (Unaudited)

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

investments are determined on the basis of amortized cost. Other investments are carried at fair value with interest and dividend income, income distributions and realized and unrealized gains and losses included in net investment income. The fair value of other investments is generally established on the basis of the net valuation criteria established by the managers of the investments. These net valuations are determined based upon the valuation criteria established by the governing documents of such investments. In addition, due to a lag in reporting, some of the Company's fund managers, fund administrators, or both, are unable to provide final fund valuations as of the Company's current reporting date. In these circumstances, the Company estimates the fair value of these funds by starting with the prior month's fund valuation, adjusting these valuations for capital calls, redemptions or distributions and the impact of changes in foreign currency exchange rates, and then estimating the return for the current period. In circumstances in which the Company estimates the return for the current period, it uses all credible information available. This principally includes preliminary estimates reported by its fund managers, obtaining the valuation of underlying portfolio investments where such underlying investments are publicly traded and therefore have a readily observable price, using information that is available to the Company with respect to the underlying investments, reviewing various indices for similar investments or asset classes, as well as estimating returns based on the results of similar types of investments for which the Company has reported results, or other valuation methods, as necessary. Actual final fund valuations may differ, perhaps materially so, from the Company's estimates and these differences are recorded in the period they become known as a change in estimate.

**3. Recent accounting pronouncements**

In December 2007, the Financial Accounting Standards Board ( FASB ) issued authoritative guidance on *Business Combinations* and *Consolidation* which are effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. In April 2009, the FASB issued further authoritative guidance on business combinations that amended previous guidance on the initial recognition and measurement, subsequent measurement and accounting, and disclosure of assets acquired and liabilities assumed in a business combination that arise from contingencies. Significant changes arising from this update, which impact current and future acquisitions include the determination of the purchase price and treatment of transaction expenses, restructuring charges and negative goodwill as follows;

**Purchase Price** The purchase price is determined as of the acquisition date, which is the date that the acquirer obtains control. Under previous guidance, the date the business combination was announced was used as the effective date in determining the purchase price;

**Transaction Expenses** All costs associated with purchase transactions must be expensed as incurred. Under previous guidance, all such costs could be capitalized and included as part of transaction purchase price, adding to the amount of goodwill recognized;

**Restructuring Costs** Expected restructuring costs are not recorded at the closing date, but rather after the transaction. The only costs to be included as a liability at the closing date are those for which an acquirer is obligated at the time of the closing. Under previous guidance, restructuring costs that were planned to occur after the closing of the transaction were recognized and recorded at the closing date as a liability;

**Negative Goodwill/Bargain Purchases** Where total fair value of net assets acquired exceeds consideration paid (creating negative goodwill ), the acquirer will record a gain as a result of the bargain purchase, to be recognized through the income statement at the close of the transaction. Under previous guidance, negative goodwill was recognized as a pro rata reduction of the assets assumed to allow the net assets acquired to equal the consideration paid; and

**Table of Contents****Validus Holdings, Ltd.**

## Notes to Consolidated Financial Statements (Unaudited)

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

**Noncontrolling Interests** In a partial or step acquisition where control is obtained, 100% of goodwill and identifiable net assets are recognized at fair value and the noncontrolling (sometimes called minority interest) interest is also recorded at fair value. Under previous guidance, in a partial acquisition only the controlling interest's share of goodwill was recognized, the controlling interest's share of identifiable net assets was recognized at fair value and the noncontrolling interest's share of identifiable net assets was recognized at carrying value. A noncontrolling interest is now recognized in the equity section, presented separately from the controlling interest's equity. Under previous guidance, noncontrolling interest in general was recorded in the mezzanine section.

As a result of the adoption of this update the Company has expensed as incurred the transaction costs related to the definitive Amalgamation Agreement dated July 9, 2009 among IPC, Validus Holdings, Ltd and Validus, Ltd (the Amalgamation Agreement) with IPC, as described in Note 4. The adoption of this update on business combinations and consolidation materially impacts the consolidated financial statement recognition and measurement of current and future acquisitions.

In June 2008, the FASB issued authoritative guidance on the *Balance Sheet* presentation of instruments granted in Share-based Payment transactions. This update addresses whether instruments granted in share-based payment transactions may be participating securities prior to vesting and, therefore, need to be included in the earnings allocation in computing basic earnings per share (EPS) pursuant to the two-class method. This update is effective for financial statements issued for fiscal years beginning after December 15, 2008. The adoption of this update has not had a material impact on the Company's consolidated financial statements.

In January 2009, the FASB issued authoritative guidance on *Investments Other* and the beneficial interests in securitized financial assets that amends certain recognition aspects of other-than-temporary impairments (OTTI). This update is effective prospectively for interim and annual periods ending after December 15, 2008. Retrospective application of this update to a prior interim or annual period is prohibited. As the Company's investment portfolio is classified as trading, the adoption of this guidance has not had a material impact on the Company's consolidated financial statements.

In April 2009, the FASB issued authoritative guidance on *Fair Value Measurements and Disclosures* and the recognition and presentation of other-than-temporary impairments (OTTI). The fair value measurement update includes guidance on; (1) estimating the fair value of an asset or liability (financial and nonfinancial) when the volume and level of activity for the asset or liability have significantly decreased; and (2) identifying transactions that are not orderly. The primary change to the OTTI model for debt securities is the change in focus from an entity's intent and ability to hold a security until recovery. Instead, an OTTI is triggered if; (1) an entity has the intent to sell the security; (2) it is more likely than not that it will be required to sell the security before recovery; or (3) it does not expect to recover the entire amortized cost basis of the security. Both updates are effective for interim and annual periods ending after June 15, 2009. The adoption of these updates has not had a material impact on the Company's consolidated financial statements.

In April 2009, the FASB issued authoritative guidance on interim disclosures about fair value of *Financial Instruments*. This update expands the fair value disclosures required for specified financial instruments for interim periods of publicly traded entities. This update also requires entities to disclose the method(s) and significant assumptions used to estimate the fair value of financial instruments in financial statements on an interim basis and to highlight any changes of the methods and significant assumptions from prior periods. This update is effective for interim and annual periods ending after June 15, 2009. As this update only expands certain disclosures requirements it has not had a material impact on the Company's consolidated financial statements.

**Table of Contents****Validus Holdings, Ltd.**

## Notes to Consolidated Financial Statements (Unaudited)

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

In May 2009, the FASB issued authoritative guidance on management's assessment of *Subsequent Events*. This update clarifies that management must evaluate, as of each reporting period, events or transactions that occur after the balance sheet date through the date that the financial statements are issued or are available to be issued. This update is effective prospectively for interim and annual periods ending after June 15, 2009. The adoption of this update has not had a material impact on management's existing processes for assessing subsequent events, and consequently the Company's consolidated financial statements.

In June 2009, the FASB issued authoritative guidance on accounting for *Transfers and Servicing* of financial assets which amends previous derecognition guidance. This update addresses practices that have developed that are not consistent with the original intent and key requirements and concerns that derecognized financial assets and related obligations should continue to be reported in the transferors' financial statements. This update is effective for financial asset transfers in the interim and annual periods beginning after November 15, 2009. Early adoption is prohibited. The adoption of this update is not expected to have a material impact on the Company's consolidated financial statements.

In June 2009, the FASB issued authoritative guidance which amends the *Consolidation* guidance that applies to Variable Interest Entities (VIEs). This update amends the guidance for the identification of VIEs and their primary beneficiaries and the financial statement disclosures required. This update is effective for interim and annual periods beginning after November 15, 2009. Early adoption is prohibited. The adoption of this update is not expected to have a material impact on the Company's consolidated financial statements.

In June 2009, the FASB issued authoritative guidance which prescribes the use of the FASB Accounting Standards Codification (the Codification) as the authoritative source of U.S. *Generally Accepted Accounting Principles* (GAAP). All of its content carries the same level of authority, effectively superseding previous guidance to include only two levels of U.S. GAAP: authoritative and nonauthoritative. This update is effective for interim and annual periods ending after September 15, 2009. The adoption of this update has not had a material impact on the Company's consolidated financial statements.

In August 2009, the FASB updated guidance on *Fair Value Measurements and Disclosures* of liabilities. This update clarifies that the quoted price for the identical liability, when traded as an asset in an active market, is also a Level 1 measurement for that liability when no adjustment to the quoted price is required. In the absence of a Level 1 measurement, an entity must use one or more prescribed valuation techniques to estimate fair value. This update is effective for the first interim or annual reporting period beginning after August 28, 2009. The adoption of this update will not have a material impact on the Company's consolidated financial statements and affected disclosures only.

In August 2009, the FASB proposed updated guidance on improving *Fair Value Measurements and Disclosures*. The proposed updated would clarify existing requirements regarding disclosures of inputs and valuation techniques and levels of disaggregation. In addition, the proposed updated would require new disclosures on (1) sensitivity disclosures regarding the effect of changing Level 3 inputs if the change in the fair value measurement would change significantly, (2) significant transfers in and out of Levels 1 and 2 and the reasons that such transfers were made, and (3) additional disclosure in the reconciliation of Level 3 activity, including information on a gross basis for purchases, sales, issuances, and settlements. An effective date has not been established. As this update only expands certain disclosure requirements it is not expected to have a material impact on the Company's consolidated financial statements.

In September 2009, the FASB updated guidance on accounting for uncertainty in *Income Taxes* and disclosure amendments for nonpublic entities. This update provides guidance on (1) what constitutes a tax position for a pass-through or not-for-profit entity, (2) determining when an income tax is attributed to the reporting entity or its



**Table of Contents****Validus Holdings, Ltd.**

## Notes to Consolidated Financial Statements (Unaudited)

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

owners, and (3) application of accounting for uncertainty in income taxes to a group of related entities composed of both taxable and nontaxable entities. The guidance is effective for interim and annual periods ending after September 15, 2009. The adoption of this update has not had a material impact on the Company's consolidated financial statements.

In September 2009, the FASB updated guidance on *Fair Value Measurements and Disclosures* of certain alternative investments. This guidance offers investors a practical expedient for measuring the fair value of investments in certain entities that calculate net asset value per share. This guidance is effective for interim and annual reporting periods ending after December 15, 2009. Early adoption is permitted. This update was not adopted for the Company's interim period ended September 30, 2009. The adoption of this update is not expected to have a material impact on the Company's consolidated financial statements.

**4. Business combination**

On September 4, 2009, the Company acquired all of the outstanding shares of IPC (the *IPC Acquisition*). Pursuant to an Amalgamation Agreement, the Company acquired all of IPC's outstanding common shares in exchange for 0.9727 Company common shares and \$7.50 cash per IPC common share. IPC's operations are focused on short-tail lines of reinsurance. 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 other short-tail reinsurance on a worldwide basis. The acquisition of IPC was undertaken to gain a strategic advantage in the current reinsurance market and increase the Company's capital base.

The aggregate purchase price paid by the Company was \$1,746,224 for adjusted tangible net assets acquired of \$2,076,902. The global financial crisis and related market illiquidity have led to several publicly traded companies trading at substantial discounts. This was the primary factor responsible for a purchase price less than the book value of IPC's net assets, and the recognition of a bargain purchase gain on acquisition.

The estimates of fair values for tangible assets acquired and liabilities assumed are determined by management based on various market and income analyses and recent asset appraisals. Significant judgment is required to arrive at these estimates of fair value and changes to assumptions used could lead to materially different results.

An adjustment of \$50,000 was made to IPC's net assets acquired in respect of the termination fee (the *Max Termination Fee*) paid under the Agreement and Plan of Amalgamation among Max Capital Group Ltd. (*Max*), IPC and IPC Limited (the *Max Amalgamation Agreement*). This Max Termination Fee was advanced to IPC by Validus on July 9, 2009, but was repayable in certain circumstances.

In addition, the Company at closing recorded a \$21,671 intangible asset for the acquired IPC customer relationships. This intangible asset relates to the acquired broker distribution network and is fair valued using a variation of the income approach. Under this approach, the Company estimated the present value of expected future cash flows to an assumed hypothetical market participant resulting from the existing IPC customer relationships, considering attrition, and discounting at a weighted average cost of capital. The composition of purchase price and fair value of net assets acquired is summarized as follows:

**Total allocable purchase price**

|   |            |
|---|------------|
| IPC shares outstanding at September 4, 2009 | 56,110,096 |
| Exchange ratio                              | 0.9727     |
| Validus common shares issued                | 54,578,268 |

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

|   |              |                   |
|---|--------------|-------------------|
| <b>Total allocable purchase price</b>   |              |                   |
| Validus closing share price on September 4, 2009  | \$ 24.10     |                   |
| Total value of Validus shares to be issued  |              | \$ 1,315,337      |
| Total cash consideration paid at \$7.50 per IPC share   |              | 420,826           |
| Share compensation awards issued to IPC employees pursuant to the Amalgamation Agreement and earned prior to the Amalgamation |              | 10,061            |
| <b>Total allocable purchase price</b>   |              | <b>1,746,224</b>  |
| <b>Tangible Assets Acquired</b>   |              |                   |
| Cash and investments  | \$ 2,463,374 |                   |
| Receivables (a)   | 202,278      |                   |
| <b>Tangible Assets Acquired</b>   |              | <b>2,665,652</b>  |
| <b>Liabilities Acquired</b>   |              |                   |
| Net loss reserves and paid losses recoverable   | \$ 304,957   |                   |
| Unearned premiums, net of expenses  | 180,370      |                   |
| Other liabilities   | 53,423       |                   |
| <b>Liabilities acquired</b>   |              | <b>538,750</b>    |
| <b>Net tangible assets acquired, at fair value</b>  |              | <b>2,126,902</b>  |
| Max Termination Fee   |              | (50,000)          |
| <b>Net tangible assets acquired, at fair value, adjusted</b>  |              | <b>2,076,902</b>  |
| <b>Bargain purchase gain before establishment of intangible assets</b>  |              | <b>330,678</b>    |
| Intangible asset customer relationships   |              | 21,671            |
| <b>Bargain purchase gain on acquisition of IPC</b>  |              | <b>\$ 352,349</b> |

(a) The fair value of receivables approximates the gross contractual amounts receivable.

The Company also incurred transaction and termination expenses related to the acquisition. Transaction expenses are primarily comprised of legal, corporate advisory, and audit related services. Termination expenses are primarily comprised of severance costs and accelerated share compensation costs in connection with certain IPC employment contracts that have been terminated. Finally, the customer relationships intangible asset has been fully amortized as it not expected to significantly contribute to the Company's future cash flows beyond the balance sheet date. The gain on

bargain purchase, net of expenses has been presented as a separate line item in the Company's Consolidated Statements of Operations and Comprehensive Income (Loss), and is composed of the following:

|   | <b>September 30, 2009</b>         |                              |
|---|-----------------------------------|------------------------------|
|   | <b>Three<br/>months<br/>ended</b> | <b>Nine months<br/>ended</b> |
| Bargain purchase gain on acquisition of IPC               | \$ 352,349                        | \$ 352,349                   |
| Transaction expenses                                      | (13,597)                          | (29,448)                     |
| Termination expenses                                      | (14,131)                          | (14,131)                     |
| Amortization of intangible asset - customer relationships | (21,671)                          | (21,671)                     |
| Gain on bargain purchase, net of expenses                 | \$ 302,950                        | \$ 287,099                   |

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

The following selected unaudited information has been provided to present a summary of the results of IPC since the acquisition date, that have been included within the Validus Re segment in the consolidated financial statements.

|                      | <b>From Acquisition Date<br/>to<br/>September 30, 2009</b> |        |
|----------------------|--|--------|
| Net premiums written | \$   | (658)  |
| Total revenue        |  | 57,434 |
| Total expenses       |  | 13,550 |
| Net income           | \$   | 43,884 |

**Supplemental Pro Forma Information**

Operating results of IPC have been included in the consolidated financial statements from the September 4, 2009 acquisition date. The following selected unaudited pro forma information has been provided to present a summary of the combined results of the Company and IPC, assuming the transaction had been effected on January 1, 2008. The unaudited pro forma data is for informational purposes only and does not necessarily represent results that would have occurred if the transaction had taken place on the basis assumed above.

|                            | <b>Three months ended</b>     |                               |
|----------------------------|-------------------------------|-------------------------------|
|                            | <b>September<br/>30, 2009</b> | <b>September 30,<br/>2008</b> |
| Net premiums written       | \$ 288,605                    | \$ 293,647                    |
| Total revenue              | 609,620                       | 327,033                       |
| Total expenses             | 274,365                       | 545,898                       |
| Net income                 | 335,255                       | (218,865)                     |
| Basic earnings per share   | \$ 3.61                       | \$ (2.95)                     |
| Diluted earnings per share | \$ 3.50                       | \$ (2.95)                     |

|                            | <b>Nine months ended</b>      |                               |
|----------------------------|-------------------------------|-------------------------------|
|                            | <b>September<br/>30, 2009</b> | <b>September 30,<br/>2008</b> |
| Net premiums written       | \$ 1,544,270                  | \$ 1,407,062                  |
| Total revenue              | 1,620,181                     | 1,122,443                     |
| Total expenses             | 841,921                       | 1,074,763                     |
| Net income                 | 778,260                       | 47,680                        |
| Basic earnings per share   | \$ 9.49                       | \$ 0.57                       |
| Diluted earnings per share | \$ 9.20                       | \$ 0.54                       |

**5. Investments**

During the first quarter of 2007, the Company adopted authoritative guidance on fair value measurements and disclosures and financial instruments. Prior to January 1, 2007, the Company's investments in fixed maturities were

classified as available-for-sale and carried at fair value, with related net unrealized gains or losses excluded from earnings and included in shareholders' equity as a component of accumulated other comprehensive income. The Company believes that accounting for its investment portfolio as trading more closely reflects its investment guidelines. Beginning on January 1, 2007, the Company's investments in fixed maturities were classified as trading and carried at fair value, with related net unrealized gains or losses included in earnings. The Company has adopted all authoritative guidance in effect as of the balance sheet date regarding certain market conditions that allow for fair value measurements that incorporate unobservable inputs where active market transaction based measurements are unavailable.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

**(a) Classification within the fair value hierarchy**

Under U.S. GAAP, a company must determine the appropriate level in the fair value hierarchy for each fair value measurement. The fair value hierarchy prioritizes the inputs, which refer broadly to assumptions market participants would use in pricing an asset or liability, into three levels. It gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The level in the fair value hierarchy within which a fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices within Level 1 that are observable for the asset or liability, either directly or indirectly. A significant adjustment to a Level 2 input could result in the Level 2 measurement becoming a Level 3 measurement. Level 3 inputs are unobservable inputs for the asset or liability.

Level 1 primarily consists of financial instruments whose value is based on quoted market prices or alternative indices but for which the Company typically obtained independent external valuation information including U.S. and U.K. Treasuries, overnight repos and commercial paper. Level 2 includes financial instruments that are valued through independent external sources using models or other valuation methodologies. These models are primarily industry-standard models that consider various assumptions, including time value, yield curve, prepayment speeds, default rates, loss severity, current market and contractual prices for the underlying financial instruments, as well as other relevant economic measures. Sustainably all of these assumptions are observable in the marketplace, can be derived from observable data or are supported by observable levels at which transactions are executed in the marketplace. The Company performs internal procedures on the valuations received from independent external sources. Financial instruments in this category include U.S. Treasuries, sovereign debt, corporate debt and U.S. agency and non-agency mortgage and asset-backed securities. Level 3 includes financial instruments that are valued using market approach and income approach valuation techniques. These models incorporate both observable and unobservable inputs. Financial instruments in this category include certain residential mortgage-backed securities.

Other investments consist of an investment in a fund of hedge funds and a deferred compensation trust. The fund investment manager provides monthly reported net asset values ( NAV ) with a one-month delay in its valuation. As a result, the fund investment manager's August 31, 2009 NAV was used as a partial basis for fair value measurement in the Company's September 30, 2009 balance sheet. The fund investment manager's NAV relies on an estimate of the performance of the fund based on the month end positions from the underlying third-party funds. The Company combines the fund investment manager's primarily market approach NAV with relevant valuation sources obtained on a timelier basis. As this combined approach valuation technique incorporates both observable and significant unobservable inputs, the fund of hedge funds is classified as a Level 3 asset. The foundation for the income approach is the amount and timing of future cash flows. To determine the reasonableness of the combined approach NAV, the Company assesses the variance between the combined approach NAV and the one-month delayed fund investment manager's NAV. These variances are recorded in the following reporting period.

On August 28, 2009, the Company sold short equity index futures contracts with the goal of hedging until closing of the IPC acquisition and liquidation of IPC's mutual fund equity portfolio exposure. The contracts were closed when the equity positions were fully redeemed on September 9, 2009. The Company experienced a \$3.3 million realized investment loss as a result of the futures contracts.

At September 30, 2009, the Company's investments were allocated between Levels 1, 2 and 3 as follows:

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

|   | <b>Level 1</b>    | <b>Level 2</b>      | <b>Level 3</b>    | <b>Total</b>        |
|---|-------------------|---------------------|-------------------|---------------------|
| U.S. Government and Government Agency             | \$                | \$ 1,182,985        | \$                | \$ 1,182,985        |
| Non-U.S. Government and Government Agency         |                   | 464,940             |                   | 464,940             |
| States, municipalities, political subdivision     |                   | 8,642               |                   | 8,642               |
| Agency residential mortgage-backed securities     |                   | 645,849             |                   | 645,849             |
| Non-Agency residential mortgage-backed securities |                   | 66,400              | 96,527            | 162,927             |
| U.S. corporate                                    |                   | 1,170,782           |                   | 1,170,782           |
| Non-U.S. corporate                                |                   | 827,048             |                   | 827,048             |
| Catastrophe bonds                                 |                   | 21,368              |                   | 21,368              |
| Asset-backed securities                           |                   | 52,381              |                   | 52,381              |
| Commercial mortgage-backed securities             |                   | 53,221              |                   | 53,221              |
| Total fixed maturities                            |                   | 4,493,616           | 96,527            | 4,590,143           |
| Total short-term investments                      | 592,325           | 2,256               |                   | 594,581             |
| Total other investments                           |                   | 11,614              | 117,398           | 129,012             |
| <b>Total</b>                                      | <b>\$ 592,325</b> | <b>\$ 4,507,486</b> | <b>\$ 213,925</b> | <b>\$ 5,313,736</b> |

At December 31, 2008, the Company's investments were allocated between Levels 1, 2 and 3 as follows:

|   | <b>Level 1</b>    | <b>Level 2</b>      | <b>Level 3</b>    | <b>Total</b>        |
|---|-------------------|---------------------|-------------------|---------------------|
| U.S. Government and Government Agency             | \$                | \$ 768,344          | \$                | \$ 768,344          |
| Non-U.S. Government and Government Agency         |                   | 96,073              |                   | 96,073              |
| States, municipalities, political subdivision     |                   | 15,516              |                   | 15,516              |
| Agency residential mortgage-backed securities     |                   | 433,736             |                   | 433,736             |
| Non-Agency residential mortgage-backed securities |                   | 119,813             | 111,318           | 231,131             |
| U.S. corporate                                    |                   | 443,847             |                   | 443,847             |
| Non-U.S. corporate                                |                   | 125,700             |                   | 125,700             |
| Catastrophe bonds                                 |                   | 10,872              |                   | 10,872              |
| Asset-backed securities                           |                   | 137,023             |                   | 137,023             |
| Commercial mortgage-backed securities             |                   | 192,259             |                   | 192,259             |
| Total fixed maturities                            |                   | 2,343,183           | 111,318           | 2,454,501           |
| Total short-term investments                      | 365,357           | 11,679              |                   | 377,036             |
| Total   | <b>\$ 365,357</b> | <b>\$ 2,354,862</b> | <b>\$ 111,318</b> | <b>\$ 2,831,537</b> |

At September 30, 2009, Level 3 investments totaled \$213,925, representing 4.0% of total investments measured at fair value on a recurring basis. At December 31, 2008, Level 3 investments totaled \$111,318, representing 3.9% of total investments measured at fair value on a recurring basis.

The following table presents a reconciliation of the beginning and ending balances for all investments measured at fair value on a recurring basis using Level 3 inputs as at September 30, 2009 and December 31, 2008:

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

|   | <b>Nine months<br/>ended<br/>September 30,<br/>2009</b> | <b>Year ended<br/>December 31,<br/>2008</b> |
|---|---|---|
| Level 3 investments    Beginning of period  | \$ 111,318  | \$  |
| Payments and purchases                      | 115,351   |   |
| Sales and maturities                        | (822)   | (59)  |
| Realized losses                             | (1,284)   |   |
| Unrealized losses                           | 1,133   | (14,603)                                    |
| Amortization                                | (11,771)  | (4,048)                                     |
| Transfers in                                |   | 130,028                                     |
| <b>Level 3 investments    End of period</b> | <b>\$ 213,925</b>                                       | <b>\$ 111,318</b>                           |

**(b) Net investment income**

Net investment income was derived from the following sources:

|   | <b>Three months ended</b>         |                                   | <b>Nine months ended</b>          |                                   |
|---|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
|   | <b>September<br/>30,<br/>2009</b> | <b>September<br/>30,<br/>2008</b> | <b>September<br/>30,<br/>2009</b> | <b>September<br/>30,<br/>2008</b> |
| Fixed maturities and short-term investments | \$ 29,427                         | \$ 32,443                         | \$ 82,341                         | \$ 98,654                         |
| Cash and cash equivalents                   | 742                               | 4,308                             | 2,623                             | 11,524                            |
| Securities lending income                   | 171                               | 261                               | 683                               | 1,150                             |
| Gross investment income                     | 30,340                            | 37,012                            | 85,647                            | 111,328                           |
| Investment expenses                         | (808)                             | (633)                             | (2,380)                           | (2,471)                           |
| Net investment income                       | \$ 29,532                         | \$ 36,379                         | \$ 83,267                         | \$ 108,857                        |

**(c) Fixed maturity and short-term investments**

The following represents an analysis of net realized gains (losses) and the change in unrealized gains (losses) on investments:

|  | <b>Three months ended</b>         |                                   | <b>Nine months ended</b>          |                                   |
|--|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|
|  | <b>September<br/>30,<br/>2009</b> | <b>September<br/>30,<br/>2008</b> | <b>September<br/>30,<br/>2009</b> | <b>September<br/>30,<br/>2008</b> |
| Fixed maturities, short-term and other<br>investments and cash equivalents |                                   |                                   |                                   |                                   |
| Gross realized gains   | \$ 9,795                          | \$ 3,653                          | \$ 23,175                         | \$ 14,965                         |
| Gross realized losses  | (4,366)                           | (17,320)                          | (43,817)                          | (23,313)                          |
| Net realized gains (losses) on investments                                 | 5,429                             | (13,667)                          | (20,642)                          | (8,348)                           |



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|   |           |             |           |             |
|---|-----------|-------------|-----------|-------------|
| Change in unrealized gains (losses) on securities lending                                       | 1,441     | (2,422)     | 5,747     | (3,316)     |
| Change in unrealized gains (losses) on investments  | 48,996    | (12,227)    | 104,092   | (69,292)    |
| <b>Total net realized gains (losses) and change in unrealized gains (losses) on investments</b> | \$ 55,866 | \$ (28,316) | \$ 89,197 | \$ (80,956) |

The amortized cost, gross unrealized gains and losses and estimated fair value of investments at September 30, 2009 were as follows:

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

|   | <b>Amortized<br/>Cost</b> | <b>Gross<br/>unrealized<br/>gains</b> | <b>Gross<br/>unrealized<br/>losses</b> | <b>Estimated<br/>fair<br/>value</b> |
|---|---------------------------|---------------------------------------|--|-------------------------------------|
| U.S. Government and Government Agency             | \$ 1,165,337              | \$ 17,707                             | \$ (59)                                | \$ 1,182,985                        |
| Non-U.S. Government and Government Agency         | 467,741                   | 7,365                                 | (10,166)                               | 464,940                             |
| States, municipalities, political subdivision     | 8,500                     | 142                                   |  | 8,642                               |
| Agency residential mortgage-backed securities     | 629,725                   | 16,431                                | (307)                                  | 645,849                             |
| Non-Agency residential mortgage-backed securities | 198,597                   | 817                                   | (36,487)                               | 162,927                             |
| U.S. corporate                                    | 1,146,483                 | 25,432                                | (1,133)                                | 1,170,782                           |
| Non-U.S. corporate                                | 825,255                   | 8,731                                 | (6,938)                                | 827,048                             |
| Catastrophe bonds                                 | 20,757                    | 731                                   | (120)                                  | 21,368                              |
| Asset-backed securities                           | 52,196                    | 723                                   | (538)                                  | 52,381                              |
| Commercial mortgage-backed securities             | 52,210                    | 1,015                                 | (4)                                    | 53,221                              |
| Total fixed maturities                            | 4,566,801                 | 79,094                                | (55,752)                               | 4,590,143                           |
| Total short-term investments                      | 595,557                   | 38                                    | (1,014)                                | 594,581                             |
| Total other investments                           | 126,301                   | 2,711                                 |  | 129,012                             |
| <b>Total</b>                                      | <b>\$ 5,288,659</b>       | <b>\$ 81,843</b>                      | <b>\$ (56,766)</b>                     | <b>\$ 5,313,736</b>                 |

The amortized cost, gross unrealized gains and losses and estimated fair value of investments at December 31, 2008 were as follows:

|   | <b>Amortized<br/>Cost</b> | <b>Gross<br/>unrealized<br/>gains</b> | <b>Gross<br/>unrealized<br/>losses</b> | <b>Estimated<br/>fair<br/>value</b> |
|---|---------------------------|---------------------------------------|--|-------------------------------------|
| U.S. Government and Government Agency             | \$ 732,155                | \$ 36,189                             | \$                                     | \$ 768,344                          |
| Non-U.S. Government and Government Agency         | 115,389                   | 4,403                                 | (23,719)                               | 96,073                              |
| States, municipalities, political subdivision     | 14,954                    | 562                                   |  | 15,516                              |
| Agency residential mortgage-backed securities     | 425,533                   | 8,358                                 | (155)                                  | 433,736                             |
| Non-Agency residential mortgage-backed securities | 299,346                   | 6                                     | (68,221)                               | 231,131                             |
| U.S. corporate                                    | 454,810                   | 2,126                                 | (13,089)                               | 443,847                             |

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|                                       |                     |                  |                     |                     |
|---------------------------------------|---------------------|------------------|---------------------|---------------------|
| Non-U.S. corporate                    | 140,807             | 1,696            | (16,803)            | 125,700             |
| Catastrophe bonds                     | 11,012              | 2                | (142)               | 10,872              |
| Asset-backed securities               | 141,209             |                  | (4,186)             | 137,023             |
| Commercial mortgage-backed securities | 217,803             |                  | (25,544)            | 192,259             |
| Total fixed maturities                | 2,553,018           | 53,342           | (151,859)           | 2,454,501           |
| Total short-term investments          | 379,537             | 55               | (2,556)             | 377,036             |
| <b>Total</b>                          | <b>\$ 2,932,555</b> | <b>\$ 53,397</b> | <b>\$ (154,415)</b> | <b>\$ 2,831,537</b> |

The following table sets forth certain information regarding the investment ratings of the Company's fixed maturities portfolio as at September 30, 2009 and December 31, 2008. Investment ratings are the lower of Moody's or Standard & Poor's rating for each investment security, presented in Standard & Poor's equivalent rating. For investments where Moody's and Standard & Poor's ratings are not available, Fitch ratings are used and presented in Standard & Poor's equivalent rating.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

|                               | <b>September 30, 2009</b>           |                       | <b>December 31, 2008</b>            |                       |
|-------------------------------|-------------------------------------|-----------------------|-------------------------------------|-----------------------|
|                               | <b>Estimated<br/>fair<br/>value</b> | <b>% of<br/>total</b> | <b>Estimated<br/>fair<br/>value</b> | <b>% of<br/>total</b> |
| AAA                           | \$ 2,831,934                        | 61.7%                 | \$ 1,941,349                        | 79.1%                 |
| AA                            | 578,547                             | 12.6%                 | 146,923                             | 6.0%                  |
| A                             | 978,886                             | 21.3%                 | 338,966                             | 13.8%                 |
| BBB                           | 71,914                              | 1.6%                  | 12,427                              | 0.5%                  |
| Investment grade              | 4,461,281                           | 97.2%                 | 2,439,665                           | 99.4%                 |
| BB                            | 33,907                              | 0.7%                  | 7,416                               | 0.3%                  |
| B                             | 42,358                              | 1.0%                  | 7,420                               | 0.3%                  |
| CCC                           | 51,045                              | 1.1%                  |                                     | 0.0%                  |
| NR                            | 1,552                               | 0.0%                  |                                     | 0.0%                  |
| Non-Investment grade          | 128,862                             | 2.8%                  | 14,836                              | 0.6%                  |
| <b>Total fixed maturities</b> | <b>\$ 4,590,143</b>                 | <b>100.0%</b>         | <b>\$ 2,454,501</b>                 | <b>100.0%</b>         |

The amortized cost and estimated fair value amounts for fixed maturity securities held at September 30, 2009 and December 31, 2008 are shown by contractual maturity. Actual maturity may differ from contractual maturity because certain borrowers may have the right to call or prepay certain obligations with or without call or prepayment penalties.

|   | <b>September 30, 2009</b> |                                     | <b>December 31, 2008</b>  |                                     |
|---|---------------------------|-------------------------------------|---------------------------|-------------------------------------|
|   | <b>Amortized<br/>cost</b> | <b>Estimated<br/>fair<br/>value</b> | <b>Amortized<br/>cost</b> | <b>Estimated<br/>fair<br/>value</b> |
| Due in one year or less                     | \$ 322,574                | \$ 323,395                          | \$ 277,137                | \$ 279,727                          |
| Due after one year through five years       | 2,896,645                 | 2,932,941                           | 1,143,494                 | 1,134,275                           |
| Due after five years through ten years      | 412,464                   | 416,835                             | 17,451                    | 17,493                              |
| Due after ten years                         | 2,391                     | 2,595                               | 31,045                    | 28,858                              |
|   | 3,634,074                 | 3,675,766                           | 1,469,127                 | 1,460,353                           |
| Asset-backed and mortgage-backed securities | 932,727                   | 914,377                             | 1,083,891                 | 994,148                             |
| <b>Total</b>                                | <b>\$ 4,566,801</b>       | <b>\$ 4,590,143</b>                 | <b>\$ 2,553,018</b>       | <b>\$ 2,454,501</b>                 |

The Company has a five year, \$500,000 secured letter of credit facility provided by a syndicate of commercial banks. At September 30, 2009, approximately \$269,231 (December 31, 2008: \$199,186) of letters of credit were issued and outstanding under this facility for which \$365,238 of investments were pledged as collateral (December 31, 2008: \$258,573). In 2007, the Company entered into a \$100,000 standby letter of credit facility which provides Funds at Lloyd's. At September 30, 2009, \$100,000 (December 31, 2008: \$100,000) of letters of credit were issued and

outstanding under this facility for which \$129,041 of investments were pledged as collateral (December 31, 2008: \$144,149). In addition, \$1,297,788 of investments were held in trust at September 30, 2009, (December 31, 2008: \$1,100,235). Of those, \$1,188,295 were held in trust for the benefit of Talbot's cedants and policyholders, and to facilitate the accreditation as an alien insurer/reinsurer by certain regulators (December 31, 2008: \$1,032,267).

The Company assumed two letters of credit facilities as part of the IPC Acquisition. A \$250,000 Credit Agreement between IPC Holdings, Ltd., IPCRe Limited, the Lenders party thereto and Wachovia Bank, National Association (the IPC Syndicated Facility ) and a \$350,000 Letters of Credit Master Agreement between Citibank N.A. and IPCRe Limited (the IPC Bi-Lateral Facility ). At September 30, 2009, the IPC Syndicated Facility had \$38,602 letters of credit issued and outstanding for which

**Table of Contents****Validus Holdings, Ltd.**

## Notes to Consolidated Financial Statements (Unaudited)

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

\$39,760 investments were pledged as collateral. At September 30, 2009, the IPC Bi-Lateral Facility had \$91,071 letters of credit issued and outstanding for which \$321,760 of investments were held in an associated collateral account.

**(d) Securities lending**

The Company participates in a securities lending program whereby certain securities from its portfolio are loaned to third parties for short periods of time through a lending agent. The Company retains all economic interest in the securities it lends and receives a fee from the borrower for the temporary use of the securities. Collateral in the form of cash, government securities and letters of credit is required at a rate of 102% of the market value of the loaned securities and is held by a third party. As at September 30, 2009, the Company had \$98,840 (December 31, 2008: \$103,266) in securities on loan. During the nine months ended September 30, 2009, the Company recorded a \$5,747 unrealized gain on this collateral on its Statements of Operations (September 30, 2008: unrealized loss \$3,316).

Securities lending collateral reinvested is primarily comprised of corporate floating rate securities with an average reset period of 23.4 days (December 31, 2008: 26.7 days). As at September 30, 2009, the securities lending collateral reinvested by the Company in connection with its securities lending program was allocated between Levels 1, 2 and 3 as follows:

|   | <b>Level 1</b>  | <b>Level 2</b>   | <b>Level 3</b> | <b>Total</b>      |
|---|-----------------|------------------|----------------|-------------------|
| Corporate                                   | \$              | \$ 14,140        | \$             | \$ 14,140         |
| Agency                                      |                 | 14,879           |                | 14,879            |
| Asset-backed securities                     |                 | 11,382           |                | 11,382            |
| Cash equivalents and short-term investments | 4,981           | 54,671           |                | 59,652            |
| <b>Total</b>                                | <b>\$ 4,981</b> | <b>\$ 95,072</b> | <b>\$</b>      | <b>\$ 100,053</b> |

As at December 31, 2008, the securities lending collateral reinvested lending by the Company in connection with its securities program was allocated between Levels 1, 2 and 3 as follows:

|   | <b>Level 1</b>  | <b>Level 2</b>   | <b>Level 3</b> | <b>Total</b>     |
|---|-----------------|------------------|----------------|------------------|
| Corporate                                   | \$              | \$ 57,574        | \$             | \$ 57,574        |
| Asset-backed securities                     |                 | 18,228           |                | 18,228           |
| Cash equivalents and short-term investments | 7,390           | 15,762           |                | 23,152           |
| <b>Total</b>                                | <b>\$ 7,390</b> | <b>\$ 91,564</b> | <b>\$</b>      | <b>\$ 98,954</b> |

The following table sets forth certain information regarding the investment ratings of the Company's securities lending collateral reinvested as at September 30, 2009 and December 31, 2008. Investment ratings are the lower of Moody's or Standard & Poor's rating for each investment security, presented in Standard & Poor's equivalent rating. For investments where Moody's and Standard & Poor's ratings are not available, Fitch ratings are used and presented in Standard & Poor's equivalent rating.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

|              | September 30, 2009         |               | December 31, 2008          |               |
|--------------|----------------------------|---------------|----------------------------|---------------|
|              | Estimated<br>fair<br>value | % of<br>total | Estimated<br>fair<br>value | % of<br>total |
| AAA          | \$ 85,919                  | 85.8%         | \$ 45,137                  | 45.7%         |
| AA           | 8,985                      | 9.0%          | 37,608                     | 37.9%         |
| A            |                            | 0.0%          | 8,729                      | 8.8%          |
| NR           | 168                        | 0.2%          | 90                         | 0.1%          |
|              | 95,072                     | 95.0%         | 91,564                     | 92.5%         |
| NR- Cash (1) | 4,981                      | 5.0%          | 7,390                      | 7.5%          |
| <b>Total</b> | <b>\$ 100,053</b>          | <b>100.0%</b> | <b>\$ 98,954</b>           | <b>100.0%</b> |

(1) This amount relates to cash and is therefore not a rated security.

The amortized cost and estimated fair value amounts for securities lending collateral reinvested held at September 30, 2009 and December 31, 2008 are shown by contractual maturity below. Actual maturity may differ from contractual maturity because certain borrowers may have the right to call or prepay certain obligations with or without call or prepayment penalties.

|                                       | September 30, 2009 |                            | December 31, 2008 |                            |
|---------------------------------------|--------------------|----------------------------|-------------------|----------------------------|
|                                       | Amortized<br>cost  | Estimated<br>fair<br>value | Amortized<br>cost | Estimated<br>fair<br>value |
| Due in one year or less               | \$ 74,587          | \$ 74,530                  | \$ 24,390         | \$ 23,152                  |
| Due after one year through five years | 26,453             | 25,523                     | 81,298            | 75,802                     |
| <b>Total</b>                          | <b>\$ 101,040</b>  | <b>\$ 100,053</b>          | <b>\$ 105,688</b> | <b>\$ 98,954</b>           |

**6. Reinsurance**

The Company enters into reinsurance and retrocession agreements in order to mitigate its accumulation of loss, reduce its liability on individual risks, enable it to underwrite policies with higher limits, and increase its aggregate capacity. The cession of insurance and reinsurance does not legally discharge the Company from its primary liability for the full amount of the policies, and the Company is required to pay the loss and bear collection risk if the reinsurer fails to meet its obligations under the reinsurance or retrocession agreement. Amounts recoverable from reinsurers are estimated in a manner consistent with the underlying liabilities.

**a) Credit risk**

The Company evaluates the financial condition of its reinsurers and monitors concentration of credit risk arising from its exposure to individual reinsurers. The reinsurance program is generally placed with reinsurers whose rating, at the time of placement, was A- or better rated by Standard & Poor's or the equivalent with other rating agencies. Exposure to a single reinsurer is also controlled with restrictions dependent on rating. At September 30, 2009, 99.3% of reinsurance recoverables (which includes loss reserves recoverable and recoverables on paid losses) were from reinsurers rated A- or better and included \$62,631 of IBNR recoverable (December 31, 2008: \$71,580). Reinsurance recoverables by reinsurer are as follows:

|   | <b>September 30, 2009</b> |                       | <b>December 31, 2008</b> |                       |
|---|---------------------------|-----------------------|--------------------------|-----------------------|
|   | <b>Reinsurance</b>        |                       | <b>Reinsurance</b>       |                       |
|   | <b>recoverable</b>        | <b>% of<br/>Total</b> | <b>recoverable</b>       | <b>% of<br/>Total</b> |
| Top 10 reinsurers                       | \$ 167,265                | 91.8%                 | 198,403                  | 94.4%                 |
| Other reinsurers balances > \$1 million | 6,105                     | 3.4%                  | 8,987                    | 4.3%                  |
| Other reinsurers balances < \$1 million | 8,795                     | 4.8%                  | 2,794                    | 1.3%                  |
| <b>Total</b>                            | <b>\$ 182,165</b>         | <b>100.0%</b>         | <b>210,184</b>           | <b>100.0%</b>         |



**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

| Top 10 Reinsurers               | Rating | September 30, 2009      |               |
|---------------------------------|--------|-------------------------|---------------|
|                                 |        | Reinsurance recoverable | % of Total    |
| Fully collateralized reinsurers | NR     | \$ 55,601               | 33.1%         |
| Hannover Re                     | AA-    | 28,711                  | 17.2%         |
| Lloyd's Syndicates              | A      | 25,977                  | 15.5%         |
| Allianz                         | AA     | 14,035                  | 8.4%          |
| Munich Re                       | AA-    | 11,742                  | 7.0%          |
| Swiss Re                        | A+     | 11,003                  | 6.6%          |
| Aspen                           | A      | 7,282                   | 4.4%          |
| Transatlantic Re                | A+     | 5,781                   | 3.5%          |
| Platinum                        | A      | 3,941                   | 2.4%          |
| Brit                            | A      | 3,192                   | 1.9%          |
| <b>Total</b>                    |        | <b>\$ 167,265</b>       | <b>100.0%</b> |

At September 30, 2009 and December 31, 2008, the provision for uncollectible reinsurance relating to losses recoverable was \$3,221 and \$3,228, respectively. To estimate the provision for uncollectible reinsurance recoverable, the reinsurance recoverable must first be allocated to applicable reinsurers. This determination is based on a process rather than an estimate, although an element of judgment must be applied. As part of this process, ceded IBNR is allocated by reinsurer. Of the \$182,165 reinsurance recoverable at September 30, 2009, \$55,601 was fully collateralized (December 31, 2008: \$83,511).

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.

**(b) Collateralized quota share retrocession treaties**

On December 22, 2007, Validus Re entered into a collateralized retrocessional reinsurance agreement with an unaffiliated third party whereby the Company cedes certain business underwritten in the marine offshore energy lines. For the three months ended September 30, 2009 and 2008 Validus Re ceded \$392 and \$3,994 of premiums written through this agreement, respectively. The earned portions of premiums ceded for the three months ended September 30, 2009 and 2008 were \$392 and \$7,744, respectively. For the nine months ended September 30, 2009 and 2008 Validus Re ceded \$1,491 and \$18,554 of premiums written through this agreement, respectively. The earned portions of premiums ceded for the nine months ended September 30, 2009 and 2008 were \$1,671 and \$14,230, respectively.

**7. Share capital****a) Authorized and issued**

The Company's authorized share capital is 571,428,571 voting and non-voting shares with a par value of \$0.175 each. The holders of common voting shares are entitled to receive dividends and are allocated one vote per share, provided that, if the controlled shares of any shareholder or group of related shareholders constitute more than 9.09 percent of the outstanding common shares of the Company, their voting power will be reduced to 9.09 percent.



**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

On September 4, 2009, the Company acquired all of the outstanding shares of IPC from a group of institutional and other investors. Pursuant to the Amalgamation Agreement, the Company acquired all of IPC's outstanding common shares in exchange for the Company's common shares and cash. The Company issued 54,556,762 common shares (excluding 21,506 restricted share awards) valued at \$24.10 per share as partial consideration for the IPC Acquisition.

The following table is a summary of the common shares issued and outstanding:

|   | <b>Common shares</b> |
|---|----------------------|
| Common shares outstanding, December 31, 2008  | 75,624,697           |
| IPC Acquisition issuance                      | 54,556,762           |
| Restricted share awards vested                | 376,354              |
| Restricted share units vested                 | 51,423               |
| Employee seller shares vested                 | 248,085              |
| Options exercised                             | 12,033               |
| Warrants exercised                            | 237,842              |
| Common shares outstanding, September 30, 2009 | 131,107,196          |
|   | <b>Common shares</b> |
| Common shares outstanding, December 31, 2007  | 74,199,836           |
| Restricted share awards vested                | 777,953              |
| Employee seller shares vested                 | 515,103              |
| Options exercised                             | 112,825              |
| Warrants exercised                            | 18,980               |
| Common shares outstanding, December 31, 2008  | 75,624,697           |

**b) Warrants**

During the three months ended September 30, 2009, nil warrants were exercised. During the nine months ended September 30, 2009, 728,010 warrants were exercised which resulted in the net share issuance of 237,842 common shares. During the three months ended September 30, 2008, nil warrants were exercised. During the nine months ended September 30, 2008, 31,580 warrants were exercised which resulted in the net share issuance of 18,980 common shares.

**c) Deferred share units**

Under the terms of the Company's Director Stock Compensation Plan, non-management directors may elect to receive their director fees in deferred share units rather than cash. The number of share units distributed in case of election under the plan is equal to the amount of the annual retainer fee otherwise payable to the director on such payment date divided by 100% of the fair market value of a share on such payment date. Additional deferred share units are issued in lieu of dividends that accrue on these deferred share units. The total outstanding deferred share units at September 30, 2009 were 4,543 (December 31, 2008: 4,430).

**d) Dividends**

On November 4, 2009, the Company announced a quarterly cash dividend of \$0.20 (2008: \$0.20) per common share and \$0.20 per common share equivalent for which each outstanding warrant is then exercisable, payable on December 31, 2009 to holders of record on December 15, 2009.



**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

**8. Stock plans****a) Long-term incentive plan**

The Company's Long Term Incentive Plan ( LTIP ) provides for grants to employees of any option, stock appreciation right ( SAR ), restricted share, restricted share unit, performance share, performance unit, dividend equivalent or other share-based award. The total number of shares reserved for issuance under the LTIP is 13,126,896 shares. The LTIP is administered by the Compensation Committee of the Board of Directors. No SARs or performance shares have been granted to date. Grant prices are established at the estimated fair market value of the Company's common shares at the date of grant.

In accordance with the terms of the Amalgamation Agreement, the IPC 2007 Stock Incentive Plan, was assumed by Validus on the acquisition date and this resulted in the issuance of 21,603 restricted share awards, 218,804 restricted share units, 199,315 performance share units and 650,557 non-qualified options.

**b) LTIP options**

Options granted under the LTIP may be exercised for voting common shares upon vesting. Options have a life of 10 years and vest either ratably or at the end of the required service period from the date of grant. All options granted in 2009 were as a result of the Amalgamation Agreement. Grant prices are established at the estimated fair value of the Company's common shares at the date of grant using the Black-Scholes option-pricing model. The following weighted average assumptions were used for all grants to date:

| Year                 | Weighted average risk free interest rate | Weighted average dividend yield | Expected life (years) | Expected volatility |
|----------------------|--|---------------------------------|-----------------------|---------------------|
| 2007 and prior years | 4.5%                                     | 0.0%                            | 7                     | 30.0%               |
| 2008                 | 3.5%                                     | 3.2%                            | 7                     | 30.0%               |
| 2009                 | 3.9%                                     | 3.7%                            | 2                     | 34.6%               |

Expected volatility is based on stock price volatility of comparable publicly-traded companies. The Company uses the simplified method consistent with U.S. GAAP authoritative guidance on stock compensation expenses to estimate expected lives for options granted during the period as historical exercise data is not available and the options met the requirement as set out in the bulletin.

Share compensation expenses of \$1,063 were recorded for the three months ended September 30, 2009 (2008: \$1,080). Share compensation expenses of \$3,037 were recorded for the nine months ended September 30, 2009 (2008: \$3,171). The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period. Activity with respect to the options for the nine months ended September 30, 2009 was as follows:

|  | Options   | Weighted average grant date fair value | Weighted average grant date exercise price |
|--|-----------|--|--|
| Options outstanding, December 31, 2008 | 2,799,938 | \$ 7.57                                | \$ 18.23                                   |
| Options granted                        | 650,557   | 3.42                                   | 27.27                                      |
| Options exercised                      | (12,033)  | 6.32                                   | 21.11                                      |
| Options forfeited                      | (7,646)   | 10.30                                  | 20.39                                      |

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|   |           |    |      |    |       |
|---|-----------|----|------|----|-------|
| Options outstanding, September 30, 2009   | 3,430,816 | \$ | 6.80 | \$ | 19.93 |
| Options exercisable at September 30, 2009 | 1,520,416 | \$ | 7.56 | \$ | 17.89 |

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

Activity with respect to options for the year ended December 31, 2008 was as follows:

|  | <b>Options</b> |    | <b>Weighted<br/>average<br/>grant date fair<br/>value</b> |    | <b>Weighted<br/>average<br/>grant date<br/>exercise<br/>price</b> |
|--|----------------|----|---|----|---|
| Options outstanding, December 31, 2007   | 2,761,176      | \$ | 7.61  | \$ | 17.82   |
| Options granted                          | 164,166        |    | 6.73  |    | 24.73   |
| Options exercised                        | (112,825)      |    | 7.38  |    | 17.57   |
| Options forfeited                        | (12,579)       |    | 8.56  |    | 18.69   |
| Options outstanding, December 31, 2008   | 2,799,938      | \$ | 7.57  | \$ | 18.23   |
| Options exercisable at December 31, 2008 | 1,396,353      | \$ | 7.46  | \$ | 17.63   |

At September 30, 2009, there were \$5,794 (December 31, 2008: \$9,139) of total unrecognized share compensation expenses that are expected to be recognized over a weighted-average period of 1.5 years (December 31, 2008: 2.2 years).

**c) LTIP restricted shares**

Restricted shares granted under the LTIP vest either ratably or at the end of the required service period and contain certain restrictions for the vesting period, relating to, among other things, forfeiture in the event of termination of employment and transferability. Share compensation expenses of \$3,621 were recorded for the three months ended September 30, 2009 (2008: \$3,767). Share compensation expenses of \$12,008 were recorded for the nine months ended September 30, 2009 (2008: \$10,334). The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period. Activity with respect to unvested restricted shares for the nine months ended September 30, 2009 was as follows:

|   | <b>Restricted<br/>shares</b> |    | <b>Weighted<br/>average<br/>grant<br/>date fair<br/>value</b> |
|---|------------------------------|----|---|
| Restricted shares outstanding, December 31, 2008  | 2,307,402                    | \$ | 22.73   |
| Restricted shares granted                         | 736,030                      |    | 24.62   |
| Restricted shares vested                          | (459,910)                    |    | 22.32   |
| Restricted shares forfeited                       | (4,517)                      |    | 21.19   |
| Restricted shares outstanding, September 30, 2009 | 2,579,005                    | \$ | 23.34   |

Activity with respect to unvested restricted shares for the period ended December 31, 2008 was as follows:

**Weighted**

|  | <b>Restricted<br/>shares</b> | <b>average<br/>grant<br/>date fair<br/>value</b> |
|--|------------------------------|--|
| Restricted shares outstanding, December 31, 2007 | 2,158,220                    | \$ 20.44   |
| Restricted shares granted                        | 1,007,083                    | 24.09  |
| Restricted shares vested                         | (822,370)                    | 18.55  |
| Restricted shares forfeited                      | (35,531)                     | 21.87  |
| Restricted shares outstanding, December 31, 2008 | 2,307,402                    | \$ 22.73   |



**Table of Contents****Validus Holdings, Ltd.**

## Notes to Consolidated Financial Statements (Unaudited)

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

At September 30, 2009, there were \$40,978 (December 31, 2008: \$35,915) of total unrecognized share compensation expenses that are expected to be recognized over a weighted-average period of 2.9 years (December 31, 2008: 3.2 years).

**d) Employee seller shares**

Pursuant to the Share Sale Agreement for the purchase of Talbot, the Company issued 1,209,741 restricted shares to Talbot employees (the employee seller shares). Upon consummation of the acquisition, the employee seller shares were validly issued, fully-paid and non-assessable and entitled to vote and participate in distributions and dividends in accordance with the Company's By-laws. However, the employee seller shares are subject to a restricted period during which they are subject to forfeiture (as implemented by repurchase by the Company for a nominal amount). Forfeiture of employee seller shares will generally occur in the event that any such Talbot employee's employment terminates, with certain exceptions, prior to the end of the restricted period. The restricted period will end for 25% of the employee seller shares on each anniversary of the closing date of July 2, 2007 for all Talbot employees other than Talbot's Chairman, such that after four years forfeiture will be completely extinguished.

Share compensation expenses of \$1,285 were recorded for the three months ended September 30, 2009 (2008: \$1,153). Share compensation expenses of \$3,874 were recorded for the nine months ended September 30, 2009 (2008: \$6,286). The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period. Activity with respect to unvested employee seller shares for the nine months ended September 30, 2009 was as follows:

|  | <b>Employee<br/>seller<br/>shares</b> | <b>Weighted<br/>average<br/>grant date fair<br/>value</b> |
|--|---------------------------------------|---|
| Employee seller shares outstanding, December 31, 2008  | 663,375                               | \$ 22.01  |
| Employee seller shares granted                         |                                       |   |
| Employee seller shares vested                          | (248,085)                             | 22.01   |
| Employee seller shares forfeited                       | (3,799)                               | 22.01   |
| Employee seller shares outstanding, September 30, 2009 | 411,491                               | \$ 22.01  |

Activity with respect to unvested employee seller shares for the year ended December 31, 2008 was as follows:

|   | <b>Employee<br/>seller<br/>shares</b> | <b>Weighted<br/>average<br/>grant date fair<br/>value</b> |
|---|---------------------------------------|---|
| Employee seller shares outstanding, December 31, 2007 | 1,209,741                             | \$ 22.01  |
| Employee seller shares granted                        |                                       |   |
| Employee seller shares vested                         | (515,103)                             | 22.01   |
| Employee seller shares forfeited                      | (31,263)                              | 22.01   |
| Employee seller shares outstanding, December 31, 2008 | 663,375                               | \$ 22.01  |

At September 30, 2009, there were \$8,146 (December 31, 2008: \$12,157) of total unrecognized share compensation expenses that are expected to be recognized over a weighted-average period of 1.8 years (December 31, 2008: 2.5 years).

***e) Restricted share units***

Restricted share units under the LTIP vest either ratably or at the end of the required service period and contain certain restrictions for the vesting period, relating to, among other things, forfeiture in the event of termination of employment and transferability. Share compensation expenses of \$2,802 were recorded for the three months ended September 30, 2009 (2008: \$12). Share compensation expenses of \$2,838 were recorded for the nine months ended

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

September 30, 2009 (2008: \$27) related to restricted share units. The expenses represent the proportionate accrual of the fair value of each grant based on the remaining vesting period. Activity with respect to unvested restricted share units for the nine months ended September 30, 2009 was as follows:

|  | <b>Restricted share<br/>units</b> |    | <b>Weighted<br/>average<br/>grant date fair<br/>value</b> |
|--|-----------------------------------|----|---|
| Restricted share units outstanding, December 31, 2008  | 11,853                            | \$ | 25.28   |
| Restricted share units granted                         | 228,136                           |    | 24.76   |
| Restricted share units vested                          | (51,753)                          |    | 24.76   |
| Restricted share units forfeited                       |                                   |    |   |
| Restricted share units outstanding, September 30, 2009 | 188,236                           | \$ | 24.79   |

Activity with respect to unvested restricted share units for the year ended December 31, 2008 was as follows:

|   | <b>Restricted share<br/>units</b> |    | <b>Weighted<br/>average<br/>grant date fair<br/>value</b> |
|---|-----------------------------------|----|---|
| Restricted share units outstanding, December 31, 2007 |                                   | \$ |   |
| Restricted share units granted                        | 11,853                            |    | 25.28   |
| Restricted share units vested                         |                                   |    |   |
| Restricted share units forfeited                      |                                   |    |   |
| Restricted share units outstanding, December 31, 2008 | 11,853                            | \$ | 25.28   |

At September 30, 2009, there were \$687 (December 31, 2008: \$223) of total unrecognized share compensation expenses that are expected to be recognized over a weighted-average period of 3.2 years (December 31, 2008: 4.6 years). Additional restricted share units are issued in lieu of accrued dividends from unvested restricted share units. As at September 30, 2009, unvested restricted share units issued in lieu of dividends were 708 (December 31, 2008: 315).

**f) Performance share units**

In accordance with the terms of the Amalgamation Agreement, the IPC 2007 Stock Incentive Plan, the plan under which the IPC Performance Share Units were granted, was assumed by Validus.

The PSUs contain both a market and performance based component. The market component is defined as the relative total shareholder return as compared to the BSX Bermuda Insurance Index. The performance component relates to the annual return on equity on an operating basis based on opening shareholders' equity. At inception of the three year cycle for the PSU awards, IPC estimated the fair value of the market and the performance based components of the PSUs granted under the IPC 2007 Stock incentive plan together with a forfeiture rate and recorded the compensation expense in its consolidated statements of income over the course of such period. The fair value estimate in respect of the market based component was set and earns over the requisite attribution period and is not adjusted unless the total shareholder return as compared to the BSX Bermuda Insurance Index falls below the 35th

percentile minimum. The estimate in respect of the performance component was reassessed at the end of each quarter as IPC's financial results evolved and IPC reflected any adjustments in the consolidated statements of income in the period in which they are determined. The PSUs contain a lock-in provision at the end of each year within the three year cycle.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

Share compensation expenses of \$2,522 were recorded for the three and nine months ended September 30, 2009 related to performance share units. Activity with respect to unvested performance share units for the nine months ended September 30, 2009 was as follows:

|   | <b>Performance<br/>share<br/>units</b> | <b>Weighted<br/>average<br/>grant date fair<br/>value</b> |
|---|--|---|
| Performance share units outstanding, December 31, 2008  |  | \$  |
| Performance share units granted                         | 199,315                                | 24.76   |
| Performance share units vested                          |  |   |
| Performance share units forfeited                       |  |   |
| Performance share units outstanding, September 30, 2009 | 199,315                                | \$ 24.76  |

At September 30, 2009, there were \$77 of total unrecognized share compensation expenses that are expected to be recognized over a weighted-average period of 2.0 years.

**g) Share compensation expenses**

Total share compensation expenses include 5,431 of IPC-related termination expenses which have been included to the gain on bargain purchase, net of expenses in the Statements of Operations. The breakdown of share compensation expenses was as follows:

|                             | <b>Three months ended</b>     |                               | <b>Nine months ended</b>          |                               |
|-----------------------------|-------------------------------|-------------------------------|-----------------------------------|-------------------------------|
|                             | <b>September<br/>30, 2009</b> | <b>September 30,<br/>2008</b> | <b>September<br/>30,<br/>2009</b> | <b>September 30,<br/>2008</b> |
| LTIP options                | \$ 1,063                      | \$ 1,080                      | \$ 3,037                          | \$ 3,171                      |
| LTIP restricted shares      | 3,621                         | 3,767                         | 12,008                            | 10,334                        |
| Employee seller shares      | 1,285                         | 1,153                         | 3,874                             | 6,286                         |
| LTIP restricted share units | 2,802                         | 12                            | 2,838                             | 27                            |
| Performance share units     | 2,522                         |                               | 2,522                             |                               |
| <b>Total</b>                | <b>\$ 11,293</b>              | <b>\$ 6,012</b>               | <b>\$ 24,279</b>                  | <b>\$ 19,818</b>              |

**9. Debt and financing arrangements****a) Financing structure and finance expenses**

The financing structure at September 30, 2009 was:

|  | <b>Commitment</b> | <b>Outstanding<br/>(1)</b> | <b>Drawn</b> |
|--|-------------------|----------------------------|--------------|
| 9.069% Junior Subordinated Deferrable Debentures | \$ 150,000        | \$ 150,000                 | \$ 150,000   |
| 8.480% Junior Subordinated Deferrable Debentures | 200,000           | 154,300                    | 154,300      |
| \$200,000 unsecured letter of credit facility    | 200,000           |                            |              |
| \$500,000 secured letter of credit facility      | 500,000           | 269,231                    |              |

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|                                     |              |            |            |
|-------------------------------------|--------------|------------|------------|
| \$250,000 IPC Syndicated facility   | 250,000      | 38,602     |            |
| \$350,000 IPC Bi-Lateral facility   | 350,000      | 91,071     |            |
| Talbot FAL facility (2)             | 100,000      | 100,000    |            |
| Talbot third party FAL facility (2) | 121,515      | 121,515    |            |
| <b>Total</b>                        | \$ 1,871,515 | \$ 924,719 | \$ 304,300 |

27

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**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

The financing structure at December 31, 2008 was:

|  | <b>Commitment</b>   | <b>Outstanding<br/>(1)</b> | <b>Drawn</b>      |
|--|---------------------|----------------------------|-------------------|
| 9.069% Junior Subordinated Deferrable Debentures | \$ 150,000          | \$ 150,000                 | \$ 150,000        |
| 8.480% Junior Subordinated Deferrable Debentures | 200,000             | 154,300                    | 154,300           |
| \$200,000 unsecured letter of credit facility    | 200,000             |                            |                   |
| \$500,000 secured letter of credit facility      | 500,000             | 199,186                    |                   |
| Talbot FAL facility (2)                          | 100,000             | 100,000                    |                   |
| Talbot third party FAL facility (2)              | 144,015             | 144,015                    |                   |
| <b>Total</b>                                     | <b>\$ 1,294,015</b> | <b>\$ 747,501</b>          | <b>\$ 304,300</b> |

(1) Indicates utilization of commitment amount, not drawn borrowings.

(2) Talbot operates in Lloyd s through a corporate member, Talbot 2002 Underwriting Capital Ltd ( T02 ), which is the sole participant in Syndicate 1183. Lloyd s sets T02 s required capital annually based on syndicate 1183 s business plan, rating environment, reserving environment together with

input arising from Lloyd's discussions with, inter alia, regulatory and rating agencies. Such capital, called Funds at Lloyd's ( FAL ), comprises: cash, investments and undrawn letters of credit provided by various banks.

Finance expenses consist of interest on our junior subordinated deferrable debentures, the amortization of debt offering costs, fees relating to our credit facilities and the costs of FAL as follows:

|  | Three months ended |                    | Nine months ended  |                    |
|--|--------------------|--------------------|--------------------|--------------------|
|  | September 30, 2009 | September 30, 2008 | September 30, 2009 | September 30, 2008 |
| 9.069% Junior Subordinated Deferrable Debentures | \$ 3,588           | \$ 3,588           | \$ 10,765          | \$ 10,765          |
| 8.480% Junior Subordinated Deferrable Debentures | 3,348              | 3,509              | 10,044             | 11,517             |
| Credit facilities                                | 395                | 218                | 1,235              | 692                |
| Talbot letter of credit facilities               | 62                 | 44                 | 167                | 169                |
| Talbot other interest                            |                    | (194)              |                    | (81)               |
| Talbot third party FAL facility                  | 3,864              | 7,352              | 7,521              | 25,734             |
| <b>Total</b>                                     | <b>\$ 11,257</b>   | <b>\$ 14,517</b>   | <b>\$ 29,732</b>   | <b>\$ 48,796</b>   |

***(b) Junior subordinated deferrable debentures***

On June 15, 2006, the Company participated in a private placement of \$150,000 of junior subordinated deferrable interest debentures due 2036 (the 9.069% Junior Subordinated Deferrable Debentures ). The 9.069%



**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

Junior Subordinated Deferrable Debentures mature on June 15, 2036, are redeemable at the Company's option at par beginning June 15, 2011, and require quarterly interest payments by the Company to the holders of the 9.069% Junior Subordinated Deferrable Debentures. Interest will be payable at 9.069% per annum through June 15, 2011, and thereafter at a floating rate of three-month LIBOR plus 355 basis points, reset quarterly. The proceeds of \$150,000 from the sale of the 9.069% Junior Subordinated Deferrable Debentures, after the deduction of commissions paid to the placement agents in the transaction and other expenses, are being used by the Company to fund Validus Re segment operations and for general working capital purposes. Debt issuance costs of \$3,750 were deferred as an asset and are amortized to income over the five year optional redemption period.

On June 21, 2007, the Company participated in a private placement of \$200,000 of junior subordinated deferrable interest debentures due 2037 (the 8.480% Junior Subordinated Deferrable Debentures). The 8.480% Junior Subordinated Deferrable Debentures mature on June 15, 2037, are redeemable at the Company's option at par beginning June 15, 2012, and require quarterly interest payments by the Company to the holders of the 8.480% Junior Subordinated Deferrable Debentures. Interest will be payable at 8.480% per annum through June 15, 2012, and thereafter at a floating rate of three-month LIBOR plus 295 basis points, reset quarterly. The proceeds of \$200,000 from the sale of the 8.480% Junior Subordinated Deferrable Debentures, after the deduction of commissions paid to the placement agents in the transaction and other expenses, were used by the Company to fund the purchase of Talbot Holdings Ltd. Debt issuance costs of \$2,000 were deferred as an asset and are amortized to income over the five year optional redemption period.

On April 29, 2008, the Company repurchased from an unaffiliated financial institution \$45,700 principal amount of its 8.480% Junior Subordinated Deferrable Debentures due 2037 at an aggregate price of \$36,560, plus accrued and unpaid interest of \$474. The repurchase resulted in the recognition of a realized gain of \$8,752 for the year ended December 31, 2008.

Future expected payments of interest and principal on the Junior Subordinated Deferrable Debentures assuming that the Company exercises its call option at the earliest opportunity are as follows:

|                                      |                   |
|--------------------------------------|-------------------|
| 2009                                 | \$ 6,672          |
| 2010                                 | 26,688            |
| 2011                                 | 169,887           |
| 2012                                 | 160,842           |
| 2013 and thereafter                  |                   |
| <b>Total minimum future payments</b> | <b>\$ 364,089</b> |

**(c) Credit facilities**

On March 12, 2007, the Company entered into a \$200,000 three-year unsecured facility, as subsequently amended on October 25, 2007 and September 4, 2009, which provides for letter of credit availability for Validus Re and our other subsidiaries and revolving credit availability for the Company (the Three Year Facility) (the full \$200,000 of which is available for letters of credit and/or revolving loans), and a \$500,000 five-year secured letter of credit facility, as subsequently amended on October 25, 2007 and September 4, 2009, which provides for letter of credit availability for Validus Re and our other subsidiaries (the Five Year Facility and together with the Three Year Facility, the Credit Facilities). The Credit Facilities were provided by a syndicate of commercial banks arranged by J.P. Morgan Securities Inc. and Deutsche Bank Securities Inc.

As amended, the Credit Facilities contain covenants that include, among other things, (i) the requirement that the Company initially maintain a minimum level of consolidated net worth of at least 70% of consolidated net worth as

calculated using the pro forma balance sheet included in the definitive proxy statement relating to the IPC Acquisition and, commencing with the end of the fiscal quarter ending September 30, 2009 to be increased quarterly by an amount equal to 50% of our consolidated net income (if positive) for such quarter plus 50% of any net proceeds received from any issuance of common shares during such quarter, (ii) the requirement that the Company

**Table of Contents****Validus Holdings, Ltd.**

## Notes to Consolidated Financial Statements (Unaudited)

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

maintain at all times a consolidated total debt to consolidated total capitalization ratio not greater than 0.35:1.00, and (iii) the requirement that Validus Re and any other material insurance subsidiaries maintain a financial strength rating by A.M. Best of not less than B++ (Fair). For purposes of covenant compliance (i) net worth is calculated with investments carried at amortized cost and (ii) consolidated total debt does not include the Company's junior subordinated deferrable debentures. The credit facilities also contain restrictions on our ability to pay dividends and other payments in respect of equity interests at any time that we are otherwise in default with respect to certain provisions under the credit facilities, make investments, incur debt at our subsidiaries, incur liens, sell assets and merge or consolidate with others.

As of September 30, 2009 and throughout the reporting periods presented, the Company was in compliance with all covenants and restrictions under the Credit Facilities.

As of September 30, 2009, we had \$269,231 in outstanding letters of credit under our five-year secured letter of credit facility (December 31, 2008: \$199,186) and no amounts were outstanding under our three-year unsecured facility (December 31, 2008: \$nil).

On October 25, 2007, the Company entered into the First Amendment to the Credit Facilities to provide for, among other things, additional capacity to incur up to \$100,000 under a new Funds at Lloyd's Letter of Credit Facility (as described below) to support underwriting capacity provided to Talbot 2002 Underwriting Ltd through Syndicate 1183 at Lloyd's of London for the 2008 and 2009 underwriting years of account. The amendment also modifies certain provisions in the Credit Facilities in order to permit dividend payments on existing and future preferred and hybrid securities notwithstanding certain events of default.

On September 4, 2009 the Company entered into the Second Amendment to the Credit Facilities to provide for, among other things, the IPC Acquisition.

On November 28, 2007, Talbot entered into a \$100,000 standby Letter of Credit facility (the Talbot FAL Facility) to provide Funds at Lloyd's; this facility is guaranteed by the Company and is secured against the assets of Validus Re. The Talbot FAL Facility was provided by a syndicate of commercial banks arranged by Lloyds TSB Bank plc and ING Bank N.V., London Branch. On July 23, 2009 the Company entered into the First Amendment to the Talbot FAL Facility to provide for, among other things, the IPC Acquisition. As amended, the Talbot FAL Facility contains affirmative covenants that include, among other things, (i) the requirement that we initially maintain a minimum level of consolidated net worth of at least 70% of consolidated net worth as calculated using the pro forma balance sheet included in the definitive proxy statement relating to the IPC Acquisition, and commencing with the end of the fiscal quarter ending September 30, 2009 to be increased quarterly by an amount equal to 50% of our consolidated net income (if positive) for such quarter plus 50% of any net proceeds received from any issuance of common shares during such quarter, and (ii) the requirement that we maintain at all times a consolidated total debt to consolidated total capitalization ratio not greater than 0.35:1.00.

The Talbot FAL Facility also contains restrictions on our ability to make investments, incur debt at our subsidiaries, incur liens, sell assets and merge or consolidate with others. Other than in respect of existing and future preferred and hybrid securities, the payment of dividends and other payments in respect of equity interests are not permitted at any time that we are in default with respect to certain provisions under the credit facilities. As of September 30, 2009 the Company had \$100,000 in outstanding letters of credit under this facility and was in compliance with all covenants and restrictions.

IPC obtains letters of credit through the IPC Syndicated Facility and the IPC Bi-Lateral Facility. In July, 2009, certain terms of these facilities were amended including suspending IPCRe's ability to increase existing letters of credit or to issue new letters of credit. With respect of the IPC Syndicated Facility, IPCRe provides the banks security by depositing cash in the amount of 103% of the aggregate letters of credit outstanding. Effective September 30, 2009, there were outstanding letters of credit of \$129,673 of which \$38,602 were issued from the IPC Syndicated Facility

with \$91,071 issued from the IPC Bi-Lateral Facility.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

**(d) Funds at Lloyd's**

Talbot's underwriting at Lloyd's is supported by Funds at Lloyd's (FAL) comprising: cash, investments and undrawn letters of credit provided by various banks on behalf of various companies and persons under reinsurance and other agreements. The FAL are provided in exchange for payment calculated principally by reference to the syndicate's results, as appropriate, when they are declared. The amounts of cash, investments and letters of credit at September 30, 2009 supporting the 2009 underwriting year amount to \$346,750 all of which is provided by the Company. A third party FAL facility comprising \$121,515 which supports the 2007 and prior underwriting years has now been withdrawn from Lloyd's and placed in escrow, however, the funds remain available to pay losses on that year.

**10. Commitments and contingencies****a) Concentrations of credit risk**

The Company's investments are managed following prudent standards of diversification. The Company attempts to limit its credit exposure by purchasing high quality fixed income investments to maintain an average portfolio credit quality of AA- or higher with mortgage and commercial mortgage-backed issues having an aggregate weighted average credit quality of triple-A. In addition, the Company limits its exposure to any single issuer to 3% or less, excluding treasury and agency securities. The minimum credit rating of any security purchased is A-/A3 and where investments are downgraded, the Company permits a holding of up to 2% in aggregate market value, or 10% with written pre-authorization. At September 30, 2009, 3.8% of the portfolio had a split rating below A-/A3 and the Company did not have an aggregate exposure to any single issuer of more than 1.8% of our investment portfolio, other than with respect to government and agency securities.

**b) Funds at Lloyd's**

Talbot operates in Lloyd's through a corporate member, Talbot 2002 Underwriting Capital Ltd (T02), which is the sole participant in Syndicate 1183. Lloyd's sets T02's required capital annually based on syndicate 1183's business plan, rating environment, reserving environment together with input arising from Lloyd's discussions with, inter alia, regulatory and rating agencies. The amounts of cash, investments and letters of credit at September 30, 2009 amounted to \$346,750 (December 31, 2008: \$351,394).

The FAL are provided for each year of account as follows:

|                     | <b>2009</b>         | <b>2008</b>         |
|---------------------|---------------------|---------------------|
|                     | <b>Underwriting</b> | <b>Underwriting</b> |
|                     | <b>year</b>         | <b>year</b>         |
| Talbot FAL facility | \$ 100,000          | \$ 100,000          |
| Group funds         | 246,750             | 216,483             |
| <b>Total</b>        | <b>\$ 346,750</b>   | <b>\$ 316,483</b>   |

The amounts which the Company provides as FAL are not available for distribution to the Company for the payment of dividends. Talbot's corporate member may also be required to maintain funds under the control of Lloyd's in excess of its capital requirement and such funds also may not be available for distribution to the Company for the payment of dividends.

The amounts provided under the Talbot FAL facility would become a liability of the group in the event of the syndicate declaring a loss at a level which would call on this arrangement.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

**c) Lloyd's central fund**

Whenever a member of Lloyd's is unable to pay its debts to policyholders, such debts may be payable by the Lloyd's central fund. If Lloyd's determines that the central fund needs to be increased, it has the power to assess premium levies on current Lloyd's members up to 3% of a member's underwriting capacity in any one year. The Company does not believe that any assessment is likely in the foreseeable future and has not provided any allowance for such an assessment. However, based on the Company's 2009 estimated premium income at Lloyd's of £400,000 the September 30, 2009 exchange rate of £1 equals \$1.60 and assuming the maximum 3% assessment the Company would be assessed approximately \$19,200.

**11. Related party transactions**

The transactions listed below are classified as related party transactions as each counterparty has either a direct or indirect shareholding in the Company.

- a) The Company entered into an agreement on December 8, 2005 with BlackRock Financial Management, Inc. (BlackRock) under which BlackRock was appointed as an investment manager of part of Company's investment portfolio. Merrill Lynch is a shareholder of BlackRock. Merrill Lynch entities, which are now wholly-owned subsidiaries of Bank of America Corp, own 6,134,530 non-voting shares in the Company, hold warrants to purchase 1,067,187 shares and have an employee on the Company's Board of Directors who does not receive compensation from the Company. Merrill Lynch's warrants are convertible to non-voting shares. Under the terms of the investment manager agreement with Blackrock, the Company incurred expenses of \$576 during the three months ended September 30, 2009 (2008: \$401) and \$1,554 during the nine months ended September 30, 2009 (2008: \$1,624), of which \$1,219 was included in accounts payable and accrued expenses at September 30, 2009 (December 31, 2008: \$584).
- b) The Company entered into an agreement on December 8, 2005 with Goldman Sachs Asset Management and its affiliates (GSAM) under which GSAM was appointed as an investment manager of part of the Company's investment portfolio. Goldman Sachs entities, own 14,057,137 non-voting shares in the Company, hold warrants to purchase 1,604,410 non-voting shares, and have an employee on the Company's Board of Directors who does not receive compensation from the Company. The Company incurred expenses of \$373 during the three months ended September 30, 2009 (2008: \$291) and \$1,099 during the nine months ended September 30, 2009 (2008: \$1,038), of which \$317 was included in accounts payable and accrued expenses at September 30, 2009 (December 31, 2008: \$641).
- c) Vestar Capital entities, which own 8,571,427 shares in the Company, hold warrants to purchase 972,810 shares, are shareholders of PARIS RE Holdings Limited (Paris Re), and have an employee on the Company's Board of Directors who does not receive compensation from the Company. Pursuant to reinsurance agreements with Paris Re, the Company recognized gross premiums written of \$nil during the three months ended September 30, 2009 (2008: \$nil) and \$6,634 during the nine months ended September 30, 2009 (2008: \$5,885), of which \$7,147 was included in premiums receivable at September 30, 2009 (December 31, 2008: \$4,412). The earned premium adjustments of \$1,710 (2008: \$(194)) and \$5,101 (2008: \$2,389) were recorded for the three and nine months ended September 30, 2009, respectively.
- d) Aquiline Capital Partners, LLC and its related companies (Aquiline), which own 6,886,342 shares in the Company, hold warrants to purchase 3,193,865 shares, and have three employees on the Board of Directors who do not receive compensation from the Company, are shareholders of Group Ark Insurance Holdings Ltd. (Group Ark). Pursuant to reinsurance agreements with Group Ark, the Company recognized \$nil (2008: \$nil) of gross premiums written and \$158 (2008: \$433) of reinsurance premiums ceded during the three months ended September 30, 2009 and recognized \$nil (2008: \$nil) of gross premiums written and \$953 (2008: \$1,531) of reinsurance premiums ceded during the nine months ended September 30, 2009, of which \$319 was included in reinsurance balances payable at September 30,

2009 (December 31, 2008: \$60).

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

e) Certain members of the Company's management and staff have provided guarantees to 1384 Capital Ltd, a company formed to indirectly facilitate the provision of Funds at Lloyd's (FAL). The Company paid \$118 of finance expenses to such management and staff in respect of such provision of FAL for the three months ended September 30, 2009 (2008: \$227) and \$261 for the nine months ended September 30, 2009 (2008: \$806), all of which was included in accounts payable and accrued expenses at September 30, 2009 (December 31, 2008: \$803). An amount of \$9 was included in general and administrative expenses in respect of the reimbursement of expenses relating to such FAL provision for the three months ended September 30, 2009 (2008: \$nil). An amount of \$25 was included in general and administrative expenses in respect of the reimbursement of expenses relating to such FAL provision for the nine months ended September 30, 2009 (2008: \$2).

**12. Earnings per share**

The following table sets forth the computation of basic and diluted earnings per share for the three and nine months ended September 30, 2009 and 2008:

|  | <b>Three months ended</b> |                  | <b>Nine months ended</b> |                  |
|--|---------------------------|------------------|--------------------------|------------------|
|  | <b>September</b>          | <b>September</b> | <b>September</b>         | <b>September</b> |
|  | <b>30,</b>                | <b>30,</b>       | <b>30,</b>               | <b>30,</b>       |
|  | <b>2009</b>               | <b>2008</b>      | <b>2009</b>              | <b>2008</b>      |
| <b>Basic earnings (loss) per share</b>                             |                           |                  |                          |                  |
| Income (loss)  | \$ 499,178                | \$ (126,300)     | \$ 731,647               | \$ 16,096        |
| less: Dividends and distributions declared on outstanding warrants | (1,591)                   | (1,739)          | (4,917)                  | (5,217)          |
| Income (loss) available to common shareholders                     | \$ 497,587                | \$ (128,039)     | \$ 726,730               | \$ 10,879        |
| Weighted average number of common shares outstanding               | 92,492,373                | 74,864,724       | 81,458,329               | 74,435,840       |
| <b>Basic earnings (loss) per share</b>                             | <b>\$ 5.38</b>            | <b>\$ (1.71)</b> | <b>\$ 8.92</b>           | <b>\$ 0.15</b>   |
| <b>Diluted earnings (loss) per share</b>                           |                           |                  |                          |                  |
| Income (loss)  | \$ 499,178                | \$ (126,300)     | \$ 731,647               | \$ 16,096        |
| less: Dividends and distributions declared on outstanding warrants |                           | (1,739)          |                          | (5,217)          |
| Income (loss) available to common shareholders                     | \$ 499,178                | \$ (128,039)     | \$ 731,647               | \$ 10,879        |
| Weighted average number of common shares outstanding               | 92,492,373                | 74,864,724       | 81,458,329               | 74,435,840       |
| Share equivalents:   |                           |                  |                          |                  |



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|  |                |                  |                |                |
|--|----------------|------------------|----------------|----------------|
| Warrants   | 2,146,172      |                  | 2,086,546      | 2,065,282      |
| Stock options  | 466,525        |                  | 378,144        | 182,268        |
| Unvested restricted shares                                   | 729,739        |                  | 703,486        | 1,239,328      |
| Weighted average number of diluted common shares outstanding | 95,834,809     | 74,864,724       | 84,626,505     | 77,922,718     |
| <b>Diluted earnings (loss) per share</b>                     | <b>\$ 5.21</b> | <b>\$ (1.71)</b> | <b>\$ 8.65</b> | <b>\$ 0.14</b> |

Share equivalents that would result in the issuance of common shares of 175,994 and nil were outstanding for the three months ended September 30, 2009 and 2008, respectively, but were not included in the computation of diluted earnings per share because the effect would be antidilutive. Share equivalents that would result in the issuance of common shares of 178,473 and 94,925 were outstanding for the nine months ended September 30, 2009 and 2008, respectively, but were not included in the computation of diluted earnings per share because the effect would be antidilutive.

**Table of Contents**

**Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

**13. Subsequent Event**

No material subsequent events were noted from the balance sheet date through to November 6, 2009.

**14. Segment information**

The Company conducts its operations worldwide through two wholly-owned subsidiaries, Validus Reinsurance, Ltd. and Talbot Holdings Ltd. from which two operating segments have been determined under U.S. GAAP segment reporting. The Company's operating segments are strategic business units that offer different products and services. They are managed and have capital allocated separately because each business requires different strategies.

**Validus Re**

The Validus Re segment is focused on short-tail lines of reinsurance. The primary lines in which the segment conducts business are property, marine and specialty which includes agriculture, aerospace, nuclear, terrorism, life and accident & health and workers' compensation catastrophe.

**Talbot**

The Talbot segment focuses on a wide range of marine and energy, war, political violence, commercial property, financial institutions, contingency, bloodstock & livestock, accident & health classes of business on an insurance or facultative reinsurance basis. Principally property, aerospace and marine classes of business on a treaty reinsurance basis.

**Corporate and other reconciling items**

The Company has a Corporate function, which includes the activities of the parent company, and which carries out functions for the group. Corporate also denotes the activities of certain key executives such as the Chief Executive Officer and Chief Financial Officer. The only revenue earned by Corporate is a minor amount of interest income that is incidental to the activities of the enterprise. For internal reporting purposes, Corporate is reflected separately as a business unit, however Corporate is not considered an operating segment under these circumstances and U.S. GAAP segment reporting. Other reconciling items include, but are not limited to, the elimination of intersegment revenues and expenses and unusual items that are not allocated to segments.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

The following tables summarize the underwriting results of our operating segments and corporate segment:

| <b>Three months ended September 30, 2009</b> | <b>Validus Re</b> | <b>Talbot</b>    | <b>Corporate<br/>&amp;<br/>Eliminations</b> | <b>Total</b>      |
|--|-------------------|------------------|---|-------------------|
| Gross premiums written                       | \$ 124,704        | \$ 227,325       | \$ (21,001)                                 | \$ 331,028        |
| Reinsurance premiums ceded                   | (38,435)          | (50,253)         | 21,001                                      | (67,687)          |
| Net premiums written                         | 86,269            | 177,072          |   | 263,341           |
| Change in unearned premiums                  | 113,499           | (2,123)          |   | 111,376           |
| Net premiums earned                          | 199,768           | 174,949          |   | 374,717           |
| Losses and loss expenses                     | 45,987            | 88,165           |   | 134,152           |
| Policy acquisition costs                     | 32,648            | 33,106           | (1,518)                                     | 64,236            |
| General and administrative expenses          | 17,987            | 23,424           | 4,625                                       | 46,036            |
| Share compensation expenses                  | 1,766             | 1,371            | 2,725                                       | 5,862             |
| <b>Underwriting income (loss)</b>            | <b>\$ 101,380</b> | <b>\$ 28,883</b> | <b>\$ (5,832)</b>                           | <b>\$ 124,431</b> |
| Net investment income (loss)                 | 23,420            | 7,629            | (1,517)                                     | 29,532            |
| Net realized gains on investments            | 5,397             | 32               |   | 5,429             |
| Net unrealized gains on investments          | 40,893            | 9,544            |   | 50,437            |
| Other income                                 | 1,847             | 772              | (1,518)                                     | 1,101             |
| Finance expenses                             | (393)             | (3,926)          | (6,938)                                     | (11,257)          |
| Foreign exchange gains (losses)              | 739               | (5,983)          |   | (5,244)           |
| Gain on bargain purchase, net of expenses    |                   |                  | 302,950                                     | 302,950           |
| <b>Net income before taxes</b>               | <b>173,283</b>    | <b>36,951</b>    | <b>287,145</b>                              | <b>497,379</b>    |
| Income tax (expense) benefit                 | (41)              | 1,840            |   | 1,799             |
| <b>Net income</b>                            | <b>\$ 173,242</b> | <b>\$ 38,791</b> | <b>\$ 287,145</b>                           | <b>\$ 499,178</b> |
| <b>Selected ratios (1)</b>                   |                   |                  |   |                   |
| Losses and loss expenses                     | 23.0%             | 50.4%            |   | 35.8%             |
| Policy acquisition costs                     | 16.3%             | 18.9%            |   | 17.1%             |
| General and administrative expenses          | 9.9%              | 14.2%            |   | 13.8%             |
| Expense ratio                                | 26.2%             | 33.1%            |   | 30.9%             |
| <b>Combined ratio</b>                        | <b>49.2%</b>      | <b>83.5%</b>     |   | <b>66.7%</b>      |

|                     |                     |                     |                  |                     |
|---------------------|---------------------|---------------------|------------------|---------------------|
| <b>Total assets</b> | <b>\$ 5,087,544</b> | <b>\$ 2,049,647</b> | <b>\$ 39,880</b> | <b>\$ 7,177,071</b> |
|---------------------|---------------------|---------------------|------------------|---------------------|

(1) Ratios are based on net premiums earned. The general and administrative expense ratio includes share compensation expenses.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

| <b>Three months ended September 30, 2008</b> | <b>Validus Re</b>  | <b>Talbot</b>      | <b>Corporate<br/>&amp;<br/>Eliminations</b> | <b>Total</b>        |
|--|--------------------|--------------------|---|---------------------|
| Gross premiums written                       | \$ 125,029         | \$ 157,307         | \$ (13,100)                                 | \$ 269,236          |
| Reinsurance premiums ceded                   | (36,286)           | (11,953)           | 13,100                                      | (35,139)            |
| Net premiums written                         | 88,743             | 145,354            |   | 234,097             |
| Change in unearned premiums                  | 92,653             | 12,576             |   | 105,229             |
| Net premiums earned                          | 181,396            | 157,930            |   | 339,326             |
| Losses and loss expenses                     | 217,081            | 101,383            |   | 318,464             |
| Policy acquisition costs                     | 26,520             | 34,026             | (121)                                       | 60,425              |
| General and administrative expenses          | 7,972              | 17,851             | 4,297                                       | 30,120              |
| Share compensation expenses                  | 1,809              | 1,164              | 3,039                                       | 6,012               |
| <b>Underwriting (loss) income</b>            | <b>\$ (71,986)</b> | <b>\$ 3,506</b>    | <b>\$ (7,215)</b>                           | <b>\$ (75,695)</b>  |
| Net investment income                        | 25,984             | 11,737             | (1,342)                                     | 36,379              |
| Net realized (losses) on investments         | (12,528)           | (1,139)            |   | (13,667)            |
| Net unrealized (losses) gains on investments | (15,946)           | 1,297              |   | (14,649)            |
| Other income                                 | 121                | 1,269              | (121)                                       | 1,269               |
| Finance expenses                             | (213)              | (7,201)            | (7,103)                                     | (14,517)            |
| Foreign exchange (losses)                    | (22,919)           | (22,014)           |   | (44,933)            |
| <b>Net (loss) before taxes</b>               | <b>(97,487)</b>    | <b>(12,545)</b>    | <b>(15,781)</b>                             | <b>(125,813)</b>    |
| Income tax (expense)                         | (31)               | (456)              |   | (487)               |
| <b>Net (loss)</b>                            | <b>\$ (97,518)</b> | <b>\$ (13,001)</b> | <b>\$ (15,781)</b>                          | <b>\$ (126,300)</b> |
| <b>Selected ratios (1):</b>                  |                    |                    |   |                     |
| Losses and loss expenses                     | 119.7%             | 64.2%              |   | 93.9%               |
| Policy acquisition costs                     | 14.6%              | 21.5%              |   | 17.8%               |
| General and administrative expenses          | 5.4%               | 12.0%              |   | 10.6%               |
| Expense ratio                                | 20.0%              | 33.5%              |   | 28.4%               |
| <b>Combined ratio</b>                        | <b>139.7%</b>      | <b>97.7%</b>       |   | <b>122.3%</b>       |

|                     |                     |                     |                 |                     |
|---------------------|---------------------|---------------------|-----------------|---------------------|
| <b>Total assets</b> | <b>\$ 2,741,721</b> | <b>\$ 1,763,614</b> | <b>\$ 4,261</b> | <b>\$ 4,509,596</b> |
|---------------------|---------------------|---------------------|-----------------|---------------------|

(1) Ratios are based on net premiums earned. The general and administrative expense ratio includes share compensation expenses.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

The following tables summarize the underwriting results of our operating segments and corporate segment:

| <b>Nine months ended September 30, 2009</b> | <b>Validus Re</b> | <b>Talbot</b>    | <b>Corporate<br/>&amp;<br/>Eliminations</b> | <b>Total</b>      |
|---|-------------------|------------------|---|-------------------|
| Gross premiums written                      | \$ 734,390        | \$ 690,357       | \$ (58,796)                                 | \$ 1,365,951      |
| Reinsurance premiums ceded                  | (94,794)          | (166,491)        | 58,796                                      | (202,489)         |
| Net premiums written                        | 639,596           | 523,866          |   | 1,163,462         |
| Change in unearned premiums                 | (101,684)         | (40,102)         |   | (141,786)         |
| Net premiums earned                         | 537,912           | 483,764          |   | 1,021,676         |
| Losses and loss expenses                    | 142,570           | 248,166          |   | 390,736           |
| Policy acquisition costs                    | 90,346            | 102,378          | (2,599)                                     | 190,125           |
| General and administrative expenses         | 45,928            | 65,565           | 13,822                                      | 125,315           |
| Share compensation expenses                 | 4,986             | 5,804            | 8,058                                       | 18,848            |
| <b>Underwriting income (loss)</b>           | <b>\$ 254,082</b> | <b>\$ 61,851</b> | <b>\$ (19,281)</b>                          | <b>\$ 296,652</b> |
| Net investment income                       | 64,989            | 22,816           | (4,538)                                     | 83,267            |
| Net realized (losses) on investments        | (14,282)          | (6,360)          |   | (20,642)          |
| Net unrealized gains on investments         | 95,693            | 14,146           |   | 109,839           |
| Other income                                | 3,034             | 2,440            | (2,599)                                     | 2,875             |
| Finance expenses                            | (1,233)           | (7,688)          | (20,811)                                    | (29,732)          |
| Foreign exchange (losses) gains             | (641)             | (427)            | 56  | (1,012)           |
| Gain on bargain purchase, net of expenses   |                   |                  | 287,099                                     | 287,099           |
| <b>Net income before taxes</b>              | <b>401,642</b>    | <b>86,778</b>    | <b>239,926</b>                              | <b>728,346</b>    |
| Income tax (expense) benefit                | (107)             | 3,408            |   | 3,301             |
| <b>Net income</b>                           | <b>\$ 401,535</b> | <b>\$ 90,186</b> | <b>\$ 239,926</b>                           | <b>\$ 731,647</b> |
| <b>Selected ratios (1)</b>                  |                   |                  |   |                   |
| Losses and loss expenses                    | 26.5%             | 51.3%            |   | 38.2%             |
| Policy acquisition costs                    | 16.8%             | 21.2%            |   | 18.6%             |
| General and administrative expenses         | 9.5%              | 14.8%            |   | 14.1%             |
| Expense ratio                               | 26.3%             | 36.0%            |   | 32.7%             |
| <b>Combined ratio</b>                       | <b>52.8%</b>      | <b>87.3%</b>     |   | <b>70.9%</b>      |

|                     |                     |                     |                  |                     |
|---------------------|---------------------|---------------------|------------------|---------------------|
| <b>Total assets</b> | <b>\$ 5,087,544</b> | <b>\$ 2,049,647</b> | <b>\$ 39,880</b> | <b>\$ 7,177,071</b> |
|---------------------|---------------------|---------------------|------------------|---------------------|

(1) Ratios are based on net premiums earned. The general and administrative expense ratio includes share compensation expenses.



**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

| <b>Nine months ended September 30, 2008</b> | <b>Validus Re</b> | <b>Talbot</b>    | <b>Corporate<br/>&amp;<br/>Eliminations</b> | <b>Total</b>     |
|---|-------------------|------------------|---|------------------|
| Gross premiums written                      | \$ 643,898        | \$ 556,335       | \$ (29,484)                                 | \$ 1,170,749     |
| Reinsurance premiums ceded                  | (61,237)          | (89,685)         | 29,484                                      | (121,438)        |
| Net premiums written                        | 582,661           | 466,650          |   | 1,049,311        |
| Change in unearned premiums                 | (93,498)          | (15,325)         |   | (108,823)        |
| Net premiums earned                         | 489,163           | 451,325          |   | 940,488          |
| Losses and loss expenses                    | 324,673           | 255,905          |   | 580,578          |
| Policy acquisition costs                    | 72,232            | 101,458          | (145)                                       | 173,545          |
| General and administrative expenses         | 27,306            | 58,561           | 15,272                                      | 101,139          |
| Share compensation expenses                 | 4,632             | 3,266            | 11,920                                      | 19,818           |
| <b>Underwriting income (loss)</b>           | <b>\$ 60,320</b>  | <b>\$ 32,135</b> | <b>\$ (27,047)</b>                          | <b>\$ 65,408</b> |
| Net investment income                       | 76,736            | 34,445           | (2,324)                                     | 108,857          |
| Realized gain on repurchase of debentures   |                   |                  | 8,752                                       | 8,752            |
| Net realized (losses) gains on investments  | (13,711)          | 5,363            |   | (8,348)          |
| Net unrealized (losses) on investments      | (58,617)          | (13,991)         |   | (72,608)         |
| Other income                                | 145               | 3,666            | (145)                                       | 3,666            |
| Finance expenses                            | (655)             | (25,821)         | (22,320)                                    | (48,796)         |
| Foreign exchange (losses)                   | (15,647)          | (20,196)         |   | (35,843)         |
| <b>Net income (loss) before taxes</b>       | <b>48,571</b>     | <b>15,601</b>    | <b>(43,084)</b>                             | <b>21,088</b>    |
| Income tax (expense)                        | (78)              | (4,914)          |   | (4,992)          |
| <b>Net income (loss)</b>                    | <b>\$ 48,493</b>  | <b>\$ 10,687</b> | <b>\$ (43,084)</b>                          | <b>\$ 16,096</b> |
| <b>Selected ratios (1)</b>                  |                   |                  |   |                  |
| Losses and loss expenses                    | 66.4%             | 56.7%            |   | 61.7%            |
| Policy acquisition costs                    | 14.8%             | 22.5%            |   | 18.5%            |
| General and administrative expenses         | 6.5%              | 13.7%            |   | 12.9%            |
| Expense ratio                               | 21.3%             | 36.2%            |   | 31.4%            |
| Combined ratio                              | 87.7%             | 92.9%            |   | 93.1%            |

|                     |                     |                     |                 |                     |
|---------------------|---------------------|---------------------|-----------------|---------------------|
| <b>Total assets</b> | <b>\$ 2,741,721</b> | <b>\$ 1,763,614</b> | <b>\$ 4,261</b> | <b>\$ 4,509,596</b> |
|---------------------|---------------------|---------------------|-----------------|---------------------|

(1) Ratios are based on net premiums earned. The general and administrative expense ratio includes share compensation expenses.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

The Company's exposures are generally diversified across geographic zones. The following tables set forth the gross premiums written allocated to the territory of coverage exposure for the periods indicated:

**Three months ended September 30, 2009**

|                                       | <b>Gross premiums written</b> |                   |                     |                   |               |
|---------------------------------------|-------------------------------|-------------------|---------------------|-------------------|---------------|
|                                       | <b>Validus<br/>Re</b>         | <b>Talbot</b>     | <b>Eliminations</b> | <b>Total</b>      | <b>%</b>      |
| United States                         | \$ 51,352                     | \$ 15,204         | \$ (1,114)          | \$ 65,442         | 19.8%         |
| Worldwide excluding United States     |                               |                   |                     |                   |               |
| (1)                                   | 4,861                         | 70,954            | (2,329)             | 73,486            | 22.2%         |
| Europe                                | 3,110                         | 14,525            | 140                 | 17,775            | 5.4%          |
| Latin America and Caribbean           | 16,921                        | 30,074            | (16,833)            | 30,162            | 9.1%          |
| Japan                                 | 2,470                         | 947               | (273)               | 3,144             | 0.9%          |
| Canada                                | (183)                         | 1,619             | 183                 | 1,619             | 0.5%          |
| Sub-total, non United States          | 27,179                        | 118,119           | (19,112)            | 126,186           | 38.1%         |
| Worldwide including United States (1) | 10,028                        | 18,152            | (597)               | 27,583            | 8.3%          |
| Marine and Aerospace (2)              | 36,145                        | 75,850            | (178)               | 111,817           | 33.8%         |
| <b>Total</b>                          | <b>\$ 124,704</b>             | <b>\$ 227,325</b> | <b>\$ (21,001)</b>  | <b>\$ 331,028</b> | <b>100.0%</b> |

**Three months ended September 30, 2008**

|                                       | <b>Gross premiums written</b> |                   |                     |                   |               |
|---------------------------------------|-------------------------------|-------------------|---------------------|-------------------|---------------|
|                                       | <b>Validus<br/>Re</b>         | <b>Talbot</b>     | <b>Eliminations</b> | <b>Total</b>      | <b>%</b>      |
| United States                         | \$ 82,468                     | \$ 11,435         | \$                  | \$ 93,903         | 34.8%         |
| Worldwide excluding United States     |                               |                   |                     |                   |               |
| (1)                                   | 10,555                        | 49,263            | (8,489)             | 51,329            | 19.1%         |
| Europe                                | 2,166                         | 13,589            |                     | 15,755            | 5.9%          |
| Latin America and Caribbean           | 22                            | 17,628            |                     | 17,650            | 6.6%          |
| Japan                                 | 251                           | 426               |                     | 677               | 0.3%          |
| Canada                                |                               | 2,261             |                     | 2,261             | 0.8%          |
| Sub-total, non United States          | 12,994                        | 83,167            | (8,489)             | 87,672            | 32.7%         |
| Worldwide including United States (1) | 4,846                         | 12,105            | (4,611)             | 12,340            | 4.5%          |
| Marine and Aerospace (2)              | 24,721                        | 50,600            |                     | 75,321            | 28.0%         |
| <b>Total</b>                          | <b>\$ 125,029</b>             | <b>\$ 157,307</b> | <b>\$ (13,100)</b>  | <b>\$ 269,236</b> | <b>100.0%</b> |

(1) Represents risks in two or more geographic zones.

- (2) Not classified as geographic area as marine and aerospace risks can span multiple geographic areas and are not fixed locations in some instances.

**Table of Contents****Validus Holdings, Ltd.**

Notes to Consolidated Financial Statements (Unaudited)

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

**Nine months ended September 30, 2009**  
**Gross premiums written**

|                                   | <b>Validus<br/>Re</b> | <b>Talbot</b>     | <b>Eliminations</b> | <b>Total</b>        | <b>%</b>      |
|-----------------------------------|-----------------------|-------------------|---------------------|---------------------|---------------|
| United States                     | \$ 336,211            | \$ 62,096         | \$ (6,201)          | \$ 392,106          | 28.7%         |
| Worldwide excluding United States |                       |                   |                     |                     |               |
| (1)                               | 45,075                | 198,145           | (11,611)            | 231,609             | 17.0%         |
| Europe                            | 50,468                | 52,434            | (3,073)             | 99,829              | 7.3%          |
| Latin America and Caribbean       | 37,040                | 62,670            | (31,726)            | 67,984              | 5.0%          |
| Japan                             | 19,177                | 4,654             | (273)               | 23,558              | 1.7%          |
| Canada                            | 469                   | 7,998             | (469)               | 7,998               | 0.6%          |
| Sub-total, non United States      | 152,229               | 325,901           | (47,152)            | 430,978             | 31.6%         |
| Worldwide including United States |                       |                   |                     |                     |               |
| (1)                               | 64,279                | 49,214            | (2,884)             | 110,609             | 8.1%          |
| Marine and Aerospace (2)          | 181,671               | 253,146           | (2,559)             | 432,258             | 31.6%         |
| <b>Total</b>                      | <b>\$ 734,390</b>     | <b>\$ 690,357</b> | <b>\$ (58,796)</b>  | <b>\$ 1,365,951</b> | <b>100.0%</b> |

**Nine months ended September 30, 2008**  
**Gross premiums written**

|                                   | <b>Validus<br/>Re</b> | <b>Talbot</b>     | <b>Eliminations</b> | <b>Total</b>        | <b>%</b>      |
|-----------------------------------|-----------------------|-------------------|---------------------|---------------------|---------------|
| United States                     | \$ 342,661            | \$ 48,513         | \$ (1,979)          | \$ 389,195          | 33.2%         |
| Worldwide excluding United States |                       |                   |                     |                     |               |
| (1)                               | 37,096                | 166,499           | (8,489)             | 195,106             | 16.7%         |
| Europe                            | 41,900                | 44,599            |                     | 86,499              | 7.4%          |
| Latin America and Caribbean       | 5,657                 | 33,155            |                     | 38,812              | 3.3%          |
| Japan                             | 9,699                 | 3,323             |                     | 13,022              | 1.1%          |
| Canada                            |                       | 7,976             |                     | 7,976               | 0.7%          |
| Sub-total, non United States      | 94,352                | 255,552           | (8,489)             | 341,415             | 29.2%         |
| Worldwide including United States |                       |                   |                     |                     |               |
| (1)                               | 69,758                | 49,377            | (19,016)            | 100,119             | 8.6%          |
| Marine and Aerospace (2)          | 137,127               | 202,893           |                     | 340,020             | 29.0%         |
| <b>Total</b>                      | <b>\$ 643,898</b>     | <b>\$ 556,335</b> | <b>\$ (29,484)</b>  | <b>\$ 1,170,749</b> | <b>100.0%</b> |

(1) Represents risks  
in two or more  
geographic

zones.

- (2) Not classified as geographic area as marine and aerospace risks can span multiple geographic areas and are not fixed locations in some instances.

**Table of Contents****ITEM 2. 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 and nine months ended September 30, 2009 and 2008 and the Company's consolidated financial condition and liquidity and capital resources at September 30, 2009 and December 31, 2008. This discussion and analysis should be read in conjunction with the audited consolidated financial statements and related notes for the fiscal year ended December 31, 2008, the discussions of critical accounting policies and the qualitative and quantitative disclosure about market risk contained in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008.

The Company was formed on October 19, 2005 and completed the acquisitions of Talbot Holdings Ltd. ( Talbot ) and IPC on July 2, 2007 and September 4, 2009, respectively. 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 of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and in Part II, Item 1A of the Company's Quarterly Report on Form 10-Q for the three months ended June 30, 2009 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.

**Executive Overview**

The Company underwrites from two distinct global operating subsidiaries, Validus Re and Talbot. Validus Re, the Company's principal reinsurance operating subsidiary, operates as a Bermuda-based provider of short-tail reinsurance products on a global basis and incorporates historical IPC business. Talbot, the Company's principal insurance operating subsidiary, operates through its two underwriting platforms: Talbot Underwriting Ltd, which manages Syndicate 1183 at Lloyd's of London ( Lloyd's ) which writes short-tail insurance products on a worldwide basis, and Underwriting Risk Services Ltd, which is an underwriting agency writing primarily yachts and onshore energy business on behalf of the Talbot syndicate and others.

The Company's strategy is to concentrate primarily on short-tail risks, which is 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 September 4, 2009, the Company acquired all of the outstanding shares of IPC (the IPC Acquisition ). Pursuant to an Amalgamation Agreement dated July 9, 2009 among IPC, Validus Holdings, Ltd and Validus, Ltd. (the Amalgamation Agreement ), the Company acquired all of IPC's outstanding common shares in exchange for the Company's common shares and cash. IPC's operations focused on short-tail lines of reinsurance. 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 other short-tail reinsurance on a worldwide basis. The acquisition of IPC was undertaken to increase the Company's capital base and gain a strategic advantage in the current reinsurance market, where capital and capacity has been depleted. This acquisition creates a leading Bermuda carrier in the short-tail reinsurance and insurance market that facilitates stronger relationships with major reinsurance intermediaries.

**Business Outlook and Trends**

The Company was formed in October 2005 in response to the supply/demand imbalance resulting from the large industry losses in 2004 and 2005. In the aggregate, the Company observed substantial increases in premium rates in 2006 compared to 2005 levels. During the years ended December 31, 2007 and 2008, the Company had experienced increased competition in most lines of business. Capital provided by new entrants or by the commitment of additional capital by existing insurers and reinsurers had increased the supply of insurance and reinsurance which

**Table of Contents**

resulted in a softening of rates in most lines. However, during 2008, the insurance and reinsurance industry incurred material losses and capital declines due to Hurricanes Ike and Gustav and the global financial crisis.

In the wake of these events, the January 2009 renewal season saw decreased competition and increased premium rates due to relatively scarce capital and increased demand. During 2009, the Company observed reinsurance demand stabilization and modest increases in credit market liquidity. The July 2009 renewal season continued to show notable rate increases as compared to the July 2008 renewal season. For the nine months ended September 30, 2009, there have been few notable large losses affecting the worldwide (re)insurance industry and no major hurricanes making landfall in the United States. Should this benign loss experience continue, it is possible that rates at the January 1, 2010 renewal period may show downward pressure; although, currently no such market pricing information is available. Validus Re gross premiums written at January 1, 2009 grew by 26.0% from the prior year period. For the nine months ended September 30, 2009, Validus Re and Talbot gross premiums written grew by 14.1% and 24.1%, respectively, from the comparable period in the prior year. These increases were largely due to rate increases coupled with modest exposure growth and the addition of new underwriting teams.

**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. The Company's objective is to generate superior returns on capital that appropriately reward shareholders for the risks assumed and to grow premiums written only when returns meet or exceed internal requirements. Details of annualized return on average equity are provided below.

|                                     | <b>Three months ended</b>     |                               | <b>Nine months ended</b>      |                               | <b>Year ended</b>                |
|-------------------------------------|-------------------------------|-------------------------------|-------------------------------|-------------------------------|----------------------------------|
|                                     | <b>September 30,<br/>2009</b> | <b>September 30,<br/>2008</b> | <b>September 30,<br/>2009</b> | <b>September 30,<br/>2008</b> | <b>December<br/>31,<br/>2008</b> |
| Annualized return on average equity | 65.3%                         | (25.4)%                       | 38.7%                         | 1.1%                          | 2.7%                             |

The increases in annualized return on average equity were driven primarily by an increase in net income for the three and nine months ended September 30, 2009. Net income for the three months ended September 30, 2009 increased by \$625.5 million, or 495.2% compared to the three months ended September 30, 2008, due primarily to the gain on bargain purchase of IPC and the large event losses incurred for the three months ended September 30, 2008. Net income for the nine months ended September 30, 2009 increased by \$715.6 million compared to the nine months ended September 30, 2008.

Annualized return on average equity is calculated by dividing the net income for the period by the average shareholders' equity during the period. Average shareholders' equity is the average of the beginning, ending and intervening quarter end shareholders' equity balances.

*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 increased by \$4.83, or 20.3%, from \$23.78 at December 31, 2008 to \$28.61 at September 30, 2009. The increase was substantially due to earnings generated in the nine months ended September 30, 2009, partially offset by dividend payments totaling \$0.60 per share and per share equivalent in the period. 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 *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 \$0.20 per common share and common share equivalent in each of the first three





**Table of Contents**

quarters of 2009. On November 4, 2009, the Company announced a quarterly cash dividend of \$0.20 per each common share and \$0.20 per common share equivalent for which each outstanding warrant is then exercisable, payable on December 31, 2009 to holders of record on December 15, 2009.

*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) and gain on bargain purchase, net of 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 income (loss) for the three months ended September 30, 2009 and 2008 was \$124.4 million and (\$75.7) million, respectively. Underwriting income for the nine months ended September 30, 2009 and 2008 was \$296.7 million and \$65.4 million, respectively. Underwriting income is a Non-GAAP financial measure as described in detail and reconciled in the section below entitled *Underwriting Income*.

**Critical Accounting Policies and Estimates**

There are certain accounting policies that the Company considers to be critical due to the judgment and uncertainty inherent in the application of those policies. In calculating financial statement estimates, the use of different assumptions could produce materially different estimates. The Company believes the following critical accounting policies affect significant estimates used in the preparation of our consolidated financial statements:

Reserve for losses and loss expenses;

Premiums;

Reinsurance premiums ceded and reinsurance recoverable; and

Investment valuation.

Critical accounting policies and estimates are discussed further in Item 7, *Management's Discussion and Analysis of Results of Operations and Financial Condition* in the Company's Annual Report on Form 10-K for the year ended December 31, 2008.

**Segment Reporting**

Management has determined that the Company operates in two reportable segments. The two segments are its significant operating subsidiaries, Validus Re and Talbot.

**Results of Operations**

Validus Re 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.

**Table of Contents**

The following table presents results of operations for the three and nine months ended September 30, 2009 and 2008:

| <b>(Dollars in thousands)</b>                 | <b>Three months ended</b> |                 | <b>Nine months ended</b> |                 |
|---|---------------------------|-----------------|--------------------------|-----------------|
|   | <b>September 30,</b>      |                 | <b>September 30,</b>     |                 |
|   | <b>2009</b>               | <b>2008 (a)</b> | <b>2009</b>              | <b>2008 (a)</b> |
| Gross premiums written                        | \$ 331,028                | \$ 269,236      | \$ 1,365,951             | \$ 1,170,749    |
| Reinsurance premiums ceded                    | (67,687)                  | (35,139)        | (202,489)                | (121,438)       |
| Net premiums written                          | 263,341                   | 234,097         | 1,163,462                | 1,049,311       |
| Change in unearned premiums                   | 111,376                   | 105,229         | (141,786)                | (108,823)       |
| Net premiums earned                           | 374,717                   | 339,326         | 1,021,676                | 940,488         |
| Losses and loss expenses                      | 134,152                   | 318,464         | 390,736                  | 580,578         |
| Policy acquisition costs                      | 64,236                    | 60,425          | 190,125                  | 173,545         |
| General and administrative expenses           | 46,036                    | 30,120          | 125,315                  | 101,139         |
| Share compensation expenses                   | 5,862                     | 6,012           | 18,848                   | 19,818          |
| Total underwriting deductions                 | 250,286                   | 415,021         | 725,024                  | 875,080         |
| Underwriting income (loss) (b)                | 124,431                   | (75,695)        | 296,652                  | 65,408          |
| Net investment income                         | 29,532                    | 36,379          | 83,267                   | 108,857         |
| Other income                                  | 1,101                     | 1,269           | 2,875                    | 3,666           |
| Finance expenses                              | (11,257)                  | (14,517)        | (29,732)                 | (48,796)        |
| Operating income (loss) before taxes (b)      | 143,807                   | (52,564)        | 353,062                  | 129,135         |
| Tax benefit (expense)                         | 1,799                     | (487)           | 3,301                    | (4,992)         |
| Net operating income (loss) (a) (b)           | 145,606                   | (53,051)        | 356,363                  | 124,143         |
| Gain on bargain purchase, net of expenses     | 302,950                   |                 | 287,099                  |                 |
| Realized gain on repurchase of debentures     |                           |                 |                          | 8,752           |
| Net realized gains (losses) on investments    | 5,429                     | (13,667)        | (20,642)                 | (8,348)         |
| Net unrealized gains (losses) on investments  | 50,437                    | (14,649)        | 109,839                  | (72,608)        |
| Foreign exchange (losses)                     | (5,244)                   | (44,933)        | (1,012)                  | (35,843)        |
| Net income (loss)                             | \$ 499,178                | \$ (126,300)    | \$ 731,647               | \$ 16,096       |
| Selected ratios:                              |                           |                 |                          |                 |
| Net premiums written / Gross premiums written | 79.6%                     | 86.9%           | 85.2%                    | 89.6%           |
| Losses and loss expenses                      | 35.8%                     | 93.9%           | 38.2%                    | 61.7%           |
| Policy acquisition costs                      | 17.1%                     | 17.8%           | 18.6%                    | 18.5%           |
| General and administrative expenses           | 13.8%                     | 10.6%           | 14.1%                    | 12.9%           |
| Expense ratio                                 | 30.9%                     | 28.4%           | 32.7%                    | 31.4%           |

|   |       |        |       |       |
|---|-------|--------|-------|-------|
| Combined ratio  | 66.7% | 122.3% | 70.9% | 93.1% |
| a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.   |       |        |       |       |
| b) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income (loss) 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. A  
reconciliation  
underwriting  
income  
(loss) measure to  
net income, the  
most comparable  
U.S. GAAP  
financial  
measure, is  
presented in the  
section below  
entitled  
Underwriting  
Income.

**Table of Contents**

|                                     | <b>Three months ended<br/>September 30,</b> |                 | <b>Nine months ended<br/>September 30,</b> |                 |
|-------------------------------------|---|-----------------|--|-----------------|
|                                     | <b>2009</b>                                 | <b>2008 (a)</b> | <b>2009</b>                                | <b>2008 (a)</b> |
| <b>Validus Re</b>                   |   |                 |  |                 |
| Gross premiums written              | \$ 124,704                                  | \$ 125,029      | \$ 734,390                                 | \$ 643,898      |
| Reinsurance premiums ceded          | (38,435)                                    | (36,286)        | (94,794)                                   | (61,237)        |
| Net premiums written                | 86,269                                      | 88,743          | 639,596                                    | 582,661         |
| Change in unearned premiums         | 113,499                                     | 92,653          | (101,684)                                  | (93,498)        |
| Net premiums earned                 | 199,768                                     | 181,396         | 537,912                                    | 489,163         |
| Losses and loss expenses            | 45,987                                      | 217,081         | 142,570                                    | 324,673         |
| Policy acquisition costs            | 32,648                                      | 26,520          | 90,346                                     | 72,232          |
| General and administrative expenses | 17,987                                      | 7,972           | 45,928                                     | 27,306          |
| Share compensation expenses         | 1,766                                       | 1,809           | 4,986                                      | 4,632           |
| Total underwriting deductions       | 98,388                                      | 253,382         | 283,830                                    | 428,843         |
| Underwriting income (loss) (b)      | 101,380                                     | (71,986)        | 254,082                                    | 60,320          |
| <b>Talbot</b>                       |   |                 |  |                 |
| Gross premiums written              | \$ 227,325                                  | \$ 157,307      | \$ 690,357                                 | \$ 556,335      |
| Reinsurance premiums ceded          | (50,253)                                    | (11,953)        | (166,491)                                  | (89,685)        |
| Net premiums written                | 177,072                                     | 145,354         | 523,866                                    | 466,650         |
| Change in unearned premiums         | (2,123)                                     | 12,576          | (40,102)                                   | (15,325)        |
| Net premiums earned                 | 174,949                                     | 157,930         | 483,764                                    | 451,325         |
| Losses and loss expenses            | 88,165                                      | 101,383         | 248,166                                    | 255,905         |
| Policy acquisition costs            | 33,106                                      | 34,026          | 102,378                                    | 101,458         |
| General and administrative expenses | 23,424                                      | 17,851          | 65,565                                     | 58,561          |
| Share compensation expenses         | 1,371                                       | 1,164           | 5,804                                      | 3,266           |
| Total underwriting deductions       | 146,066                                     | 154,424         | 421,913                                    | 419,190         |
| Underwriting income (loss) (b)      | 28,883                                      | 3,506           | 61,851                                     | 32,135          |
| <b>Corporate &amp; Eliminations</b> |   |                 |  |                 |
| Gross premiums written              | \$ (21,001)                                 | \$ (13,100)     | \$ (58,796)                                | \$ (29,484)     |
| Reinsurance premiums ceded          | 21,001                                      | 13,100          | 58,796                                     | 29,484          |
| Net premiums written                |   |                 |  |                 |

Change in unearned premiums

Net premiums earned

Losses and loss expenses

|                                     |            |             |            |           |
|-------------------------------------|------------|-------------|------------|-----------|
| Policy acquisition costs            | (1,518)    | (121)       | (2,599)    | (145)     |
| General and administrative expenses | 4,625      | 4,297       | 13,822     | 15,272    |
| Share compensation expenses         | 2,725      | 3,039       | 8,058      | 11,920    |
| Total underwriting deductions       | 5,832      | 7,215       | 19,281     | 27,047    |
| Underwriting income (loss) (b)      | (5,832)    | (7,215)     | (19,281)   | (27,047)  |
| Total underwriting income (b)       | \$ 124,431 | \$ (75,695) | \$ 296,652 | \$ 65,408 |

a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

b) 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.



**Table of Contents****Three months ended September 30, 2009 compared to three months ended September 30, 2008**

Net income (loss) for the three months ended September 30, 2009 was \$499.2 million compared to (\$126.3) million for the three months ended September 30, 2008, an increase of \$625.5 million or 495.2%. The primary factors driving the increase in net income were:

Gain on bargain purchase, net of expenses of \$303.0 million on the IPC Acquisition;

Increase in underwriting income of \$200.1 million due primarily to reduced losses and loss expenses of \$184.3 and increased net premiums earned of \$35.4 million. For the three months ended September 30, 2008, the Company incurred \$183.4 million and \$22.1 million, respectively, as a result of Hurricanes Ike and Gustav;

Increase in net realized gains on investments of \$19.1 million due to the disposition of selected fixed maturities to finance the purchase of IPC;

Increase in net unrealized gains on investments of \$65.1 million, respectively, due to improved market conditions for fixed income securities; and

Decreased foreign exchange (losses) of \$39.7 million was due to the increased value of assets denominated in foreign currencies relative to the U.S. dollar reporting currency for the three months ended September 30, 2009, as compared to the three months ended September 30, 2008. Foreign exchange (losses) for the three months ended September 30, 2009 were (\$5.2) million, as compared to (\$44.9) million for the three months ended September 30, 2008.

The change in net income for the three months ended September 30, 2009 of \$625.5 million is described in the following table:

**Three months ended September 30, 2009**  
**Increase (decrease) over the three months ended September 30,**  
**2008 (a)**

| <b>(Dollars in thousands)</b>                              | <b>Validus</b> |               | <b>Corporate<br/>and<br/>other<br/>reconciling</b> |              |
|--|----------------|---------------|--|--------------|
|  | <b>Re</b>      | <b>Talbot</b> | <b>items</b>                                       | <b>Total</b> |
| Hurricanes Ike and Gustav net losses and loss expenses (b) | \$ 172,635     | \$ 32,878     | \$   | \$ 205,513   |
| Hurricanes Ike and Gustav net reinstatement premiums (b)   | (19,268)       | (392)         |  | (19,660)     |
| Other underwriting income                                  | 19,999         | (7,109)       | 1,383  | 14,273       |
| Underwriting income (c)                                    | 173,366        | 25,377        | 1,383  | 200,126      |
| Net investment income                                      | (2,564)        | (4,108)       | (175)  | (6,847)      |
| Other income   | 1,726          | (497)         | (1,397)  | (168)        |
| Finance expenses   | (180)          | 3,275         | 165  | 3,260        |
|  | 172,348        | 24,047        | (24)   | 196,371      |
| Taxes  | (10)           | 2,296         |  | 2,286        |
|  | 172,338        | 26,343        | (24)   | 198,657      |
| Gain on bargain purchase, net of expenses                  |                |               | 302,950  | 302,950      |
| Net realized (losses) gains on investments                 | 17,925         | 1,171         |  | 19,096       |
| Net unrealized gains (losses) on investments               | 56,839         | 8,247         |  | 65,086       |
| Foreign exchange (losses) gains                            | 23,658         | 16,031        |  | 39,689       |

|                   |            |           |            |            |
|-------------------|------------|-----------|------------|------------|
| <b>Net income</b> | \$ 270,760 | \$ 51,792 | \$ 302,926 | \$ 625,478 |
|-------------------|------------|-----------|------------|------------|

46

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**Table of Contents**

- (a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.
  
- (b) Hurricanes Ike and Gustav net losses and loss expenses and net reinstatement premiums recognized for the three months ended September 30, 2008; therefore, figures exclude loss development in subsequent periods.
  
- (c) 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 September 30, 2009 were \$331.0 million compared to \$269.2 million for the three months ended September 30, 2008, an increase of \$61.8 million or 23.0%. The increase in gross premiums written was driven primarily by the property, marine and specialty lines which increased by \$17.6 million, \$12.5 million and \$31.6 million, respectively. Details of gross premiums written by line of business are provided below.

| (Dollars in thousands) | Gross premiums written |               |                    |               |              |
|------------------------|------------------------|---------------|--------------------|---------------|--------------|
|                        | Three months ended     |               | Three months ended |               | % Change     |
|                        | September 30, 2009     | (a)           | September 30, 2008 | (a)           |              |
| Property               | \$ 141,480             | 42.7%         | \$ 123,831         | 46.0%         | 14.3%        |
| Marine                 | 95,772                 | 29.0%         | 83,273             | 30.9%         | 15.0%        |
| Specialty              | 93,776                 | 28.3%         | 62,132             | 23.1%         | 50.9%        |
| <b>Total</b>           | <b>\$ 331,028</b>      | <b>100.0%</b> | <b>\$ 269,236</b>  | <b>100.0%</b> | <b>23.0%</b> |

(a) The results of operations for IPC are consolidated only from the

September 2009  
date of  
acquisition.  
Consequently,  
2008 data does  
not include IPC  
financial results.

*Validus Re.* Validus Re gross premiums written for the three months ended September 30, 2009 were \$124.7 million compared to \$125.0 million for the three months ended September 30, 2008, a decrease of \$0.3 million or 0.3%. Details of Validus Re gross premiums written by line of business are provided below.

| (Dollars in thousands) | Three months ended |               | Gross premiums written                          |               | %<br>Change   |
|------------------------|--------------------|---------------|---|---------------|---------------|
|                        | September 30, 2009 |               | Three months ended<br>September 30, 2008<br>(a) |               |               |
| Property               | \$ 80,578          | 64.6%         | \$ 97,545                                       | 78.0%         | (17.4)%       |
| Marine                 | 28,408             | 22.8%         | 19,154  | 15.3%         | 48.3%         |
| Specialty              | 15,718             | 12.6%         | 8,330   | 6.7%          | 88.7%         |
| <b>Total</b>           | <b>\$ 124,704</b>  | <b>100.0%</b> | <b>\$ 125,029</b>                               | <b>100.0%</b> | <b>(0.3)%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

The decrease in Validus Re gross premiums written was driven by a decrease in the property lines of \$17.0 million offset by \$9.3 million and \$7.4 million increases in the marine and specialty lines, respectively. The decrease in the property line was due primarily to a \$15.2 million reduction in reinstatement premiums on Hurricanes Ike and Gustav losses in 2008. The increase in the marine line was due primarily to an additional \$12.5 million of off-shore energy gross premiums written recognized for the three months ended September 30, 2009. Gross premiums written under the quota share, surplus treaty and excess of loss contracts with Talbot increased by \$7.9 million as compared to the three months ended September 30, 2008. The quota share, surplus treaty and excess of loss contracts with Talbot are eliminated upon consolidation.

**Table of Contents**

*Talbot.* Talbot gross premiums written for the three months ended September 30, 2009 were \$227.3 million compared to \$157.3 million for the three months ended September 30, 2008, an increase of \$70.0 million or 44.5%. The \$227.3 million of gross premiums written translated at third quarter 2008 rates of exchange would have been \$238.4 million during the three months ended September 30, 2009, an increase of \$81.1 million, or 51.5%. Details of Talbot gross premiums written by line of business are provided below.

| (Dollars in thousands) | Gross premiums written |                    |                    |                    |              |
|------------------------|------------------------|--------------------|--------------------|--------------------|--------------|
|                        | Three months ended     |                    | Three months ended |                    | % Change     |
|                        | September 30, 2009     | September 30, 2008 | September 30, 2009 | September 30, 2008 |              |
| Property               | \$ 79,155              | 34.8%              | \$ 35,194          | 22.4%              | 124.9%       |
| Marine                 | 69,621                 | 30.6%              | 66,676             | 42.4%              | 4.4%         |
| Specialty              | 78,549                 | 34.6%              | 55,437             | 35.2%              | 41.7%        |
| <b>Total</b>           | <b>\$ 227,325</b>      | <b>100.0%</b>      | <b>\$ 157,307</b>  | <b>100.0%</b>      | <b>44.5%</b> |

The increase in the property lines was due primarily to \$31.6 million of gross premiums written on the onshore energy lines and an \$11.2 million increase in gross premiums written by Validus Reasegueros, Inc., which acts as an approved Lloyd's coverholder for Syndicate 1183 targeting the Latin American and Caribbean markets, and commenced operations during 2008. The increase in the specialty lines was due primarily to \$20.0 million of additional gross premiums written by the new aviation team.

**Reinsurance Premiums Ceded**

Reinsurance premiums ceded for the three months ended September 30, 2009 were \$67.7 million compared to \$35.1 million for the three months ended September 30, 2008, an increase of \$32.5 million. This was due primarily to an increase of \$28.6 million on the property lines retrocession as described below.

| (Dollars in thousands) | Reinsurance premiums ceded |                    |                    |                    |              |
|------------------------|----------------------------|--------------------|--------------------|--------------------|--------------|
|                        | Three months ended         |                    | Three months ended |                    | % Change     |
|                        | September 30, 2009         | September 30, 2008 | September 30, 2009 | September 30, 2008 |              |
| Property               | \$ 56,466                  | 83.4%              | \$ 27,823          | 79.1%              | 102.9%       |
| Marine                 | 6,504                      | 9.6%               | 4,977              | 14.2%              | 30.7%        |
| Specialty              | 4,717                      | 7.0%               | 2,339              | 6.7%               | 101.7%       |
| <b>Total</b>           | <b>\$ 67,687</b>           | <b>100.0%</b>      | <b>\$ 35,139</b>   | <b>100.0%</b>      | <b>92.6%</b> |

- (a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC

financial results.

*Validus Re.* Validus Re reinsurance premiums ceded for the three months ended September 30, 2009 were \$38.4 million compared to \$36.3 million for the three months ended September 30, 2008, an increase of \$2.1 million.

**Reinsurance premiums ceded**

| (Dollars in thousands) | Three months ended |               | Three months ended        |               | %<br>Change |
|------------------------|--------------------|---------------|---------------------------|---------------|-------------|
|                        | September 30, 2009 |               | September 30, 2008<br>(a) |               |             |
| Property               | \$ 33,991          | 88.4%         | \$ 32,265                 | 88.9%         | 5.3%        |
| Marine                 | 4,444              | 11.6%         | 3,871                     | 10.7%         | 14.8%       |
| Specialty              |                    | 0.0%          | 150                       | 0.4%          | (100.0)%    |
| <b>Total</b>           | <b>\$ 38,435</b>   | <b>100.0%</b> | <b>\$ 36,286</b>          | <b>100.0%</b> | <b>5.9%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

Reinsurance premiums ceded on the property lines increased by \$1.7 million, due to the purchase of an additional \$34.0 million of catastrophe retrocessional coverage for IPC's U.S. property exposures, off-set by the

**Table of Contents**

advanced second quarter 2009 renewal of retrocessional coverage via ultimate net loss agreements that incepted in 2008 during the three months ended September 30, 2008.

*Talbot.* Talbot reinsurance premiums ceded for the three months ended September 30, 2009 were \$50.3 million compared to \$12.0 million for the three months ended September 30, 2008, an increase of \$38.3 million. The increase was due primarily to increased reinsurance premiums ceded on the property lines of business.

| (Dollars in thousands) | Reinsurance premiums ceded |               |                    |               |               |
|------------------------|----------------------------|---------------|--------------------|---------------|---------------|
|                        | Three months ended         |               | Three months ended |               | % Change      |
|                        | September 30, 2009         |               | September 30, 2008 |               |               |
| Property               | \$ 40,728                  | 81.0%         | \$ 4,466           | 37.4%         | 812.0%        |
| Marine                 | 4,317                      | 8.6%          | 3,663              | 30.6%         | 17.9%         |
| Specialty              | 5,208                      | 10.4%         | 3,824              | 32.0%         | 36.2%         |
| <b>Total</b>           | <b>\$ 50,253</b>           | <b>100.0%</b> | <b>\$ 11,953</b>   | <b>100.0%</b> | <b>320.4%</b> |

Reinsurance premiums ceded on the property lines increased by \$36.3 million, due primarily to \$23.7 million of reinsurance premiums ceded on the additional gross premiums written on onshore energy lines, as discussed above. Reinsurance premiums ceded under third party quota share, surplus treaty and excess of loss contracts on the property lines increased by \$27.6 million, as compared to the three months ended September 30, 2008. Reinsurance premiums ceded under the quota share, surplus treaty and excess of loss contracts with Validus Re for the three months ended September 30, 2009 were \$21.0 million compared to \$13.1 million for the three months ended September 30, 2008, an increase of \$7.9 million. The quota share, surplus treaty and excess of loss with Validus Re are eliminated upon consolidation.

**Net Premiums Written**

Net premiums written for the three months ended September 30, 2009 were \$263.3 million compared to \$234.1 million for the three months ended September 30, 2008, an increase of \$29.2 million, or 12.5%. The ratios of net premiums written to gross premiums written for the three months ended September 30, 2009 and 2008 were 79.6% and 86.9%, respectively. Details of net premiums written by line of business are provided below.

| (Dollars in thousands) | Net premiums written |               |                           |               |              |
|------------------------|----------------------|---------------|---------------------------|---------------|--------------|
|                        | Three months ended   |               | Three months ended        |               | % Change     |
|                        | September 30, 2009   |               | September 30, 2008<br>(a) |               |              |
| Property               | \$ 85,014            | 32.3%         | \$ 96,008                 | 41.1%         | (11.5)%      |
| Marine                 | 89,268               | 33.9%         | 78,296                    | 33.4%         | 14.0%        |
| Specialty              | 89,059               | 33.8%         | 59,793                    | 25.5%         | 48.9%        |
| <b>Total</b>           | <b>\$ 263,341</b>    | <b>100.0%</b> | <b>\$ 234,097</b>         | <b>100.0%</b> | <b>12.5%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of



acquisition.  
Consequently,  
2008 data does  
not include IPC  
financial results.

*Validus Re.* Validus Re net premiums written for the three months ended September 30, 2009 were \$86.3 million compared to \$88.7 million for the three months ended September 30, 2008, a decrease of \$2.5 million or 2.8%. Details of net premiums written by line of business are provided below.

| (Dollars in thousands) | Net premiums written |               |                    |               |               |
|------------------------|----------------------|---------------|--------------------|---------------|---------------|
|                        | Three months ended   |               | Three months ended |               | % Change      |
|                        | September 30, 2009   |               | September 30, 2008 |               |               |
| Property               | \$ 46,587            | 54.0%         | \$ 65,280          | 73.6%         | (28.6)%       |
| Marine                 | 23,964               | 27.8%         | 15,283             | 17.2%         | 56.8%         |
| Specialty              | 15,718               | 18.2%         | 8,180              | 9.2%          | 92.2%         |
| <b>Total</b>           | <b>\$ 86,269</b>     | <b>100.0%</b> | <b>\$ 88,743</b>   | <b>100.0%</b> | <b>(2.8)%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

**Table of Contents**

The decrease in Validus Re net premiums written was driven by a decrease in the property lines of \$18.7 million. This decrease was due primarily to a \$15.2 million reduction in reinstatement premiums on Hurricanes Ike and Gustav losses, as discussed above and increase in ceded premium of \$2.1. The ratios of net premiums written to gross premiums written were 69.2% and 71.0% for the three months ended September 30, 2009 and 2008, respectively. *Talbot*. *Talbot* net premiums written for the three months ended September 30, 2009 were \$177.1 million compared to \$145.4 million for the three months ended September 30, 2008, an increase of \$31.7 million or 21.8%. Details of net premiums written by line of business are provided below:

| (Dollars in thousands) | Net premiums written |                    |                    |                    |              |
|------------------------|----------------------|--------------------|--------------------|--------------------|--------------|
|                        | Three months ended   |                    | Three months ended |                    | % Change     |
|                        | September 30, 2009   | September 30, 2008 | September 30, 2009 | September 30, 2008 |              |
| Property               | \$ 38,427            | 21.7%              | \$ 30,728          | 21.1%              | 25.1%        |
| Marine                 | 65,304               | 36.9%              | 63,013             | 43.4%              | 3.6%         |
| Specialty              | 73,341               | 41.4%              | 51,613             | 35.5%              | 42.1%        |
| <b>Total</b>           | <b>\$177,072</b>     | <b>100.0%</b>      | <b>\$ 145,354</b>  | <b>100.0%</b>      | <b>21.8%</b> |

The increase 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 September 30, 2009 and 2008 were 77.9% and 92.4%, respectively. This decrease was due primarily to the 25.0% ratio of net premiums written to gross premiums written on the onshore energy lines for the three months ended September 30, 2009.

**Change in Unearned Premiums**

Change in unearned premiums for the three months ended September 30, 2009 was \$111.4 million compared to \$105.2 million for the three months ended September 30, 2008, a change of \$6.1 million or 5.8%.

| (Dollars in thousands)                | Change in unearned premiums |                        |             |
|---------------------------------------|-----------------------------|------------------------|-------------|
|                                       | Three months ended          | Three months ended     | % Change    |
|                                       | September 30, 2009          | September 30, 2008 (a) |             |
| Change in gross unearned premium      | \$ 95,638                   | \$ 96,183              | (0.6)%      |
| Change in prepaid reinsurance premium | 15,738                      | 9,046                  | 74.0%       |
| <b>Net change in unearned premium</b> | <b>\$ 111,376</b>           | <b>\$ 105,229</b>      | <b>5.8%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does

not include IPC  
financial results.

*Validus Re.* Validus Re's change in unearned premiums for the three months ended September 30, 2009 were \$113.5 million compared to \$92.7 million for the three months ended September 30, 2008, a change of \$20.8 million or 22.5%.

|                                       | <b>Change in unearned premiums</b>                           |  |                     |
|---------------------------------------|--|--|---------------------|
|                                       | <b>Three<br/>months<br/>ended<br/>September<br/>30, 2009</b> | <b>Three months<br/>ended<br/>September 30,<br/>2008 (a)</b> | <b>%<br/>Change</b> |
| <b>(Dollars in thousands)</b>         |  |  |                     |
| Change in gross unearned premium      | \$ 99,768  | \$ 75,463  | 32.2%               |
| Change in prepaid reinsurance premium | 13,731   | 17,190   | (20.1)%             |
| <b>Net change in unearned premium</b> | <b>\$ 113,499</b>  | <b>\$ 92,653</b>   | <b>22.5%</b>        |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

**Table of Contents**

The increase in gross unearned premium was due primarily to an additional \$32.5 million of gross unearned premium resulting from the consolidation of IPCRe for the three months ended September 30, 2009. *Talbot*. The *Talbot* change in unearned premiums for the three months ended September 30, 2009 was (\$2.1) million compared to \$12.6 million for the three months ended September 30, 2008, a change of \$14.7 million, or 116.9%.

|                                       | Change in unearned premiums           |                                       |                 |
|---------------------------------------|---------------------------------------|---------------------------------------|-----------------|
|                                       | Three months ended September 30, 2009 | Three months ended September 30, 2008 | % Change        |
| <b>(Dollars in thousands)</b>         |                                       |                                       |                 |
| Change in gross unearned premium      | \$ (4,130)                            | \$ 20,720                             | (119.9)%        |
| Change in prepaid reinsurance premium | 2,007                                 | (8,144)                               | (124.6)%        |
| <b>Net change in unearned premium</b> | <b>\$ (2,123)</b>                     | <b>\$ 12,576</b>                      | <b>(116.9)%</b> |

The difference in gross unearned premiums arose principally from the increased gross premiums written in the property lines, specifically onshore energy exposures and premiums written by Validus Reaseguros, Inc., which acts as an approved Lloyd's coverholder for Syndicate 1183 on the property treaty lines, during the three months ended September 30, 2009, as compared to the three months ended September 30, 2008. The lower change in prepaid reinsurance premiums in the three months ended September 30, 2009 is reflective of the increased amounts of onshore energy exposures and premiums written by Validus Reaseguros, Inc., which have increased levels of ceded reinsurance. This results in less seasonality in the ceded reinsurance and hence a small change in prepaid reinsurance for the three months ended September 30, 2009.

**Net Premiums Earned**

Net premiums earned for the three months ended September 30, 2009 were \$374.7 million compared to \$339.3 million for the three months ended September 30, 2008, an increase of \$35.4 million or 10.4%. The increase in net premiums earned was driven by increased premiums earned of \$18.4 million and \$17.0 million in the Validus Re and *Talbot* segments, respectively.

|                               | Net premiums earned                   |               |                                       |               | % Change     |
|-------------------------------|---------------------------------------|---------------|---------------------------------------|---------------|--------------|
|                               | Three months ended September 30, 2009 |               | Three months ended September 30, 2008 |               |              |
| <b>(Dollars in thousands)</b> |                                       |               |                                       |               |              |
| Property                      | \$ 177,916                            | 47.4%         | \$ 165,028                            | 48.6%         | 7.8%         |
| Marine                        | 114,114                               | 30.5%         | 101,110                               | 29.8%         | 12.9%        |
| Specialty                     | 82,687                                | 22.1%         | 73,188                                | 21.6%         | 13.0%        |
| <b>Total</b>                  | <b>\$ 374,717</b>                     | <b>100.0%</b> | <b>\$ 339,326</b>                     | <b>100.0%</b> | <b>10.4%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of

acquisition.  
Consequently,  
2008 data does  
not include IPC  
financial results.

*Validus Re.* Validus Re net premiums earned for the three months ended September 30, 2009 were \$199.8 million compared to \$181.4 million for the three months ended September 30, 2008, an increase of \$18.4 million or, 10.1%. The increase in net premiums earned was due primarily to \$31.8 million of property net premiums earned resulting from the consolidation of IPCRe Limited ( IPCRe ), which offset the increase in ceded earned premiums attributable to purchases of retrocessional cover during the three months ended September 30, 2009.

| (Dollars in thousands) | Net premiums earned |               |                    |               |              |
|------------------------|---------------------|---------------|--------------------|---------------|--------------|
|                        | Three months ended  |               | Three months ended |               | %<br>Change  |
|                        | September 30, 2009  |               | September 30, 2008 |               |              |
| Property               | \$ 141,547          | 70.9%         | \$ 132,307         | 73.0%         | 7.0%         |
| Marine                 | 35,397              | 17.7%         | 29,980             | 16.5%         | 18.1%        |
| Specialty              | 22,824              | 11.4%         | 19,109             | 10.5%         | 19.4%        |
| <b>Total</b>           | <b>\$199,768</b>    | <b>100.0%</b> | <b>\$ 181,396</b>  | <b>100.0%</b> | <b>10.1%</b> |

**Table of Contents**

- (a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

The increase in Validus Re net premiums earned was driven by an increase in the property lines of \$9.2 million due primarily to \$31.8 million of property net premiums earned resulting from the consolidation of IPCRe, offset by the \$15.2 million decrease in reinstatement premiums earned as compared to the three months ended September 30, 2008, as discussed above.

*Talbot*. Talbot net premiums earned for the three months ended September 30, 2009 were \$174.9 million compared to \$157.9 million for the three months ended September 30, 2008, an increase of \$17.0 million or 10.8%.

| (Dollars in thousands) | Net premiums earned |               |                    |               |              |
|------------------------|---------------------|---------------|--------------------|---------------|--------------|
|                        | Three months ended  |               | Three months ended |               | % Change     |
|                        | September 30, 2009  |               | September 30, 2008 |               |              |
| Property               | \$ 36,369           | 20.8%         | \$ 32,721          | 20.7%         | 11.1%        |
| Marine                 | 78,717              | 45.0%         | 71,130             | 45.1%         | 10.7%        |
| Specialty              | 59,863              | 34.2%         | 54,079             | 34.2%         | 10.7%        |
| <b>Total</b>           | <b>\$ 174,949</b>   | <b>100.0%</b> | <b>\$ 157,930</b>  | <b>100.0%</b> | <b>10.8%</b> |

The increase in net premiums earned is due primarily to the increased levels of net premiums written by the new underwriting teams over the twelve months ended September 30, 2009, as compared with the twelve months ended September 30, 2008, as discussed above.

**Losses and Loss Expenses**

Losses and loss expenses for the three months ended September 30, 2009 were \$134.2 million compared to \$318.5 million for the three months ended September 30, 2008, a decrease of \$184.3 million or 57.9%. The loss ratios, defined as losses and loss expenses divided by net premiums earned, for the three months ended September 30, 2009 and 2008 were 35.8% and 93.9%, respectively. Details of loss ratios by line of business are provided below.

|                  | Three months ended<br>September 30,<br>2009 | Three months ended<br>September 30,<br>2008 (a) | Percentage point<br>change |
|------------------|---|---|----------------------------|
| Property         | 13.5%                                       | 122.4%  | (108.9)                    |
| Marine           | 65.5%                                       | 99.6%   | (34.1)                     |
| Specialty        | 42.7%                                       | 21.4%   | 21.3                       |
| <b>All lines</b> | <b>35.8%</b>                                | <b>93.9%</b>                                    | <b>(58.1)</b>              |

- (a)

The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

The following table sets forth a reconciliation of gross and net reserves for losses and loss expenses by segment for the three months ended September 30, 2009:

**Table of Contents****Three months ended September 30, 2009**

| <b>(Dollars in thousands)</b>            | <b>Validus</b> | <b>Talbot</b> | <b>Eliminations</b> | <b>Total</b> |
|--|----------------|---------------|---------------------|--------------|
| Gross reserves at period beginning       | \$ 489,340     | \$ 845,537    | \$ (22,942)         | \$ 1,311,935 |
| Losses recoverable at period beginning   | (61,798)       | (130,810)     | 22,942              | (169,666)    |
| Net reserves at period beginning         | 427,542        | 714,727       |                     | 1,142,269    |
| Net reserves acquired in IPC acquisition | 304,957        |               |                     | 304,957      |
| Incurring losses- current year           | 65,259         | 100,919       |                     | 166,178      |
| Change in prior accident years           | (19,272)       | (12,754)      |                     | (32,026)     |
| Incurring losses                         | 45,987         | 88,165        |                     | 134,152      |
| Exchange rate effects                    | 2,383          | (4,992)       |                     | (2,609)      |
| Paid losses                              | (55,242)       | (70,885)      |                     | (126,127)    |
| Net reserves at period end               | 725,627        | 727,015       |                     | 1,452,642    |
| Losses recoverable                       | 57,608         | 143,064       | (28,571)            | 172,101      |
| Gross reserves at period end             | \$ 783,235     | \$ 870,079    | \$ (28,571)         | \$ 1,624,743 |

The amount of recorded reserves represents management's best estimate of expected losses and loss expenses on premiums earned. Favorable loss development on prior years totaled \$32.0 million. Favorable loss reserve development benefitted the Company's loss ratio by 8.5 percentage points for the three months ended September 30, 2009. For the three months ended September 30, 2009, the Company did not experience any notable losses. For the three months ended September 30, 2008, the Company incurred \$183.4 million and \$22.1 million of losses attributable to Hurricanes Ike and Gustav, which represent 54.0 and 6.5 percentage points of the loss ratio, respectively.

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 of recent losses. The Company's actual ultimate net loss may vary materially from estimates.

At September 30, 2009 and 2008, 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 in Item 7, *Management's Discussion and Analysis of Results of Operations and Financial Condition* in the Company's Annual Report on Form 10-K for the year ended December 31, 2008. The Company did not make any significant changes in the assumptions or methodology used in its reserving process for the three months ended September 30, 2009.

**As at September 30, 2009**

| <b>(Dollars in thousands)</b> | <b>Gross case reserves</b> | <b>Gross IBNR</b> | <b>Total gross reserve for losses and loss expenses</b> |
|-------------------------------|----------------------------|-------------------|---|
| Property                      | \$ 393,729                 | \$ 322,935        | \$ 716,664  |
| Marine                        | 354,584                    | 249,262           | 603,846   |
| Specialty                     | 129,543                    | 174,690           | 304,233   |



|              |            |            |              |
|--------------|------------|------------|--------------|
| <b>Total</b> | \$ 877,856 | \$ 746,887 | \$ 1,624,743 |
|--------------|------------|------------|--------------|

**As at September 30, 2009**

| <b>(Dollars in thousands)</b> | <b>Net case<br/>reserves</b> | <b>Net IBNR</b>   | <b>Total net reserve for<br/>losses</b> |
|-------------------------------|------------------------------|-------------------|---|
|                               |                              |                   | <b>and loss expenses</b>                |
| Property                      | \$ 390,524                   | \$ 304,084        | \$ 694,608                              |
| Marine                        | 261,032                      | 231,781           | 492,813                                 |
| Specialty                     | 115,231                      | 149,990           | 265,221                                 |
| <b>Total</b>                  | <b>\$ 766,787</b>            | <b>\$ 685,855</b> | <b>\$ 1,452,642</b>                     |

**Table of Contents**

During the three months ended September 30, 2008, the Company incurred losses related to Hurricanes Ike and Gustav of \$183.4 million and \$22.1 million, respectively, as detailed in the chart below.

| <b>(Dollars in thousands)</b> | <b>Net Losses and<br/>Loss</b> | <b>Net<br/>Reinstatement</b> | <b>Net Effect on<br/>Net<br/>(Loss) Income</b> |
|-------------------------------|--------------------------------|------------------------------|--|
|                               | <b>Expenses (1)</b>            | <b>Premiums</b>              | <b>(2)</b>                                     |
| <b>Hurricane Ike</b>          |                                |                              |  |
| <i>Validus Re</i>             |                                |                              |  |
| Property                      | \$ 120,286                     | \$ (13,867)                  | \$ 106,419                                     |
| Marine                        | 36,778                         | (4,098)                      | 32,680   |
| Specialty                     | 125                            |                              | 125  |
| All lines                     | 157,189                        | (17,965)                     | 139,224  |
| <br>                          |                                |                              |  |
| <i>Talbot</i>                 |                                |                              |  |
| Property                      | 15,161                         | (386)                        | 14,775   |
| Marine                        | 10,478                         | (6)                          | 10,472   |
| Specialty                     | 544                            |                              | 544  |
| All lines                     | 26,183                         | (392)                        | 25,791   |
| <br>                          |                                |                              |  |
| <i>Total</i>                  |                                |                              |  |
| Property                      | 135,447                        | (14,253)                     | 121,194  |
| Marine                        | 47,256                         | (4,104)                      | 43,152   |
| Specialty                     | 669                            |                              | 669  |
| All lines                     | \$ 183,372                     | \$ (18,357)                  | \$ 165,015                                     |
| <br>                          |                                |                              |  |
| <b>Hurricane Gustav</b>       |                                |                              |  |
| <i>Validus Re</i>             |                                |                              |  |
| Property                      | \$ 13,946                      | \$ (1,303)                   | \$ 12,643                                      |
| Marine                        | 1,500                          |                              | 1,500  |
| Specialty                     |                                |                              |  |
| All lines                     | 15,446                         | (1,303)                      | 14,143   |
| <br>                          |                                |                              |  |
| <i>Talbot</i>                 |                                |                              |  |
| Property                      | 3,695                          |                              | 3,695  |
| Marine                        | 2,500                          |                              | 2,500  |
| Specialty                     | 500                            |                              | 500  |
| All lines                     | 6,695                          |                              | 6,695  |

|                                  |            |             |    |         |
|----------------------------------|------------|-------------|----|---------|
| <i>Total</i>                     |            |             |    |         |
| Property                         | 17,641     | (1,303)     |    | 16,338  |
| Marine                           | 4,000      |             |    | 4,000   |
| Specialty                        | 500        |             |    | 500     |
| All lines                        | \$ 22,141  | \$ (1,303)  | \$ | 20,838  |
| <b>Hurricanes Ike and Gustav</b> |            |             |    |         |
| Property                         | \$ 153,088 | \$ (15,556) | \$ | 137,532 |
| Marine                           | 51,256     | (4,104)     |    | 47,152  |
| Specialty                        | 1,169      |             |    | 1,169   |
| All lines                        | \$ 205,513 | \$ (19,660) | \$ | 185,853 |

- (1) Net of reinsurance.
- (2) Net effect on net (loss) income includes the sum of estimates of net claims and claim expenses incurred, and earned reinstatement premiums assumed and ceded.

**Table of Contents**

*Validus Re.* Validus Re losses and loss expenses for the three months ended September 30, 2009 were \$46.0 million compared to \$217.1 million for the three months ended September 30, 2008, a decrease of \$171.1 million or 78.8%. Validus Re net paid losses for the three months ended September 30, 2009 were \$55.2 million compared to \$40.2 million for the three months ended September 30, 2008, an increase of \$15.1 million or 37.6%, primarily as a result of losses paid on Hurricane Ike. The loss ratio, defined as losses and loss expenses divided by net premiums earned, was 23.0% and 119.7% for the three months ended September 30, 2009 and 2008, respectively. For the three months ended September 30, 2009, Validus Re did not experience any notable loss events. For the three months ended September 30, 2008, Validus Re incurred \$157.2 million and \$15.4 million of losses attributable to Hurricanes Ike and Gustav, which represent 86.7 and 8.5 percentage points of the loss ratio, respectively. Validus Re segment loss ratios, excluding prior year development and loss events identified above, for the three months ended September 30, 2009 and 2008 were 32.6% and 26.4%, respectively. Details of loss ratios by line of business and period of incurrence are provided below.

|                  |                                | <b>2009</b>  | <b>2008 (a)</b> | <b>Percentage<br/>point<br/>change</b> |
|------------------|--------------------------------|--------------|-----------------|--|
| Property         | current year                   | 28.2%        | 123.2%          | (95.0)                                 |
| Property         | change in prior accident years | (23.3)%      | (4.8)%          | (18.5)                                 |
| Property         | loss ratio                     | 4.9%         | 118.4%          | (113.5)                                |
| Marine           | current year                   | 32.7%        | 174.6%          | (141.9)                                |
| Marine           | change in prior accident years | 47.8%        | 14.7%           | 33.1                                   |
| Marine           | loss ratio                     | 80.5%        | 189.3%          | (108.8)                                |
| Specialty        | current year                   | 60.3%        | 27.8%           | 32.5                                   |
| Specialty        | change in prior accident years | (13.8)%      | (8.6)%          | (5.2)                                  |
| Specialty        | loss ratio                     | 46.5%        | 19.2%           | 27.3                                   |
| All lines        | current year                   | 32.6%        | 121.6%          | (89.0)                                 |
| All lines        | change in prior accident years | (9.6)%       | (1.9)%          | (7.7)                                  |
| <b>All lines</b> | <b>loss ratio</b>              | <b>23.0%</b> | <b>119.7%</b>   | <b>(96.7)</b>                          |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

For the three months ended September 30, 2009, the property lines include \$39.9 million related to current year losses and \$33.0 million of favorable development relating to prior accident years. This favorable development is attributable to reduced loss estimates for Hurricane Ike and the October 2007 Peruvian mining loss, as well as lower than expected claim development elsewhere. For the three months ended September 30, 2008, Validus Re's property lines incurred \$120.3 million and \$13.9 million of losses attributable to Hurricanes Ike and Gustav, which represented 90.9 and 10.5 percentage points of the loss ratio, respectively. Validus Re property line loss ratios, excluding prior year development and loss events identified above, for the three months ended September 30, 2009 and 2008 were 28.2% and 21.8%, respectively.

For the three months ended September 30, 2009, the marine lines include \$11.6 million related to current year losses and \$16.9 million of adverse development relating to prior accident years. This adverse development is primarily attributable to increased loss estimates for Hurricanes Ike and Gustav. For the three months ended September 30, 2008, Validus Re's marine lines incurred \$36.8 million and \$1.5 million of losses attributable to Hurricanes Ike and Gustav, which represented 122.7 and 5.0 percentage points of the loss ratio, respectively. Validus Re marine line loss ratios, excluding prior year development and loss events identified above, for the three months ended September 30, 2009 and 2008 were 32.7% and 46.9%, respectively.

For the three months ended September 30, 2009, the specialty lines include \$13.8 million related to current year losses and \$3.1 million of favorable development relating to prior accident years. For the three months ended

**Table of Contents**

September 30, 2008, Validus Re's specialty lines incurred \$0.1 million of losses attributable to Hurricane Ike, which represented 0.7 percentage points of the loss ratio. Validus Re specialty lines loss ratios, excluding prior year development and the loss event identified above, for the three months ended September 30, 2009 and 2008 were 60.3% and 27.1%, respectively. This difference is primarily attributable to a larger than expected number of specialty lines losses, as well as higher than expected 2009 claim development elsewhere.

*Talbot.* Talbot losses and loss expenses for the three months ended September 30, 2009 were \$88.2 million compared to \$101.4 million for the three months ended September 30, 2008, a decrease of \$13.2 million, or 13.0%. The loss ratio was 50.4% and 64.2% for the three months ended September 30, 2009 and 2008, respectively. For the three months ended September 30, 2009, Talbot did not experience any notable loss events. For the three months ended September 30, 2008, Talbot incurred \$26.2 million and \$6.7 million of losses attributable to Hurricanes Ike and Gustav, which represent 16.6 and 4.2 percentage points of the loss ratio, respectively. For the three months ended September 30, 2009, \$100.9 million of losses and loss expenses related to current year losses and \$12.8 million related to favorable development of prior accident years. Details of loss ratios by line of business and calendar period are provided below.

|                  |                                | <b>Three months ended<br/>September 30,</b> |             | <b>Percentage<br/>point<br/>change</b> |
|------------------|--------------------------------|---|-------------|--|
|                  |                                | <b>2009</b>                                 | <b>2008</b> |  |
| Property         | current year                   | 56.1%                                       | 139.0%      | (82.9)                                 |
| Property         | change in prior accident years | (8.9)%                                      | (0.2)%      | (8.7)                                  |
| Property         | loss ratio                     | 47.2%                                       | 138.8%      | (91.6)                                 |
| Marine           | current year                   | 58.7%                                       | 79.0%       | (20.3)                                 |
| Marine           | change in prior accident years | 0.1%  | (17.2)%     | 17.3                                   |
| Marine           | loss ratio                     | 58.8%                                       | 61.8%       | (3.0)                                  |
| Specialty        | current year                   | 57.3%                                       | 41.3%       | 16.0                                   |
| Specialty        | change in prior accident years | (16.0)%                                     | (19.1)%     | 3.1                                    |
| Specialty        | loss ratio                     | 41.3%                                       | 22.2%       | 19.1                                   |
| All lines        | current year                   | 57.7%                                       | 78.5%       | (20.8)                                 |
| All lines        | change in prior accident years | (7.3)%                                      | (14.3)%     | 7.0                                    |
| <b>All lines</b> | <b>loss ratio</b>              | 50.4%                                       | 64.2%       | (13.8)                                 |

For the three months ended September 30, 2009, the property lines include \$20.4 million related to current year losses and \$3.2 million of favorable development relating to prior accident years. For the three months ended September 30, 2008, Talbot's property lines incurred \$15.2 million and \$3.7 million of losses attributable to Hurricanes Ike and Gustav, which represented 46.3 and 11.3 percentage points of the loss ratio, respectively. Talbot property line loss ratio, excluding prior year development for the three months ended September 30, 2009 and 2008 were 56.1% and 81.4%, respectively.

For the three months ended September 30, 2009, the marine lines include \$46.2 million related to current year. For the three months ended September 30, 2008, Talbot's marine lines incurred \$10.5 million and \$2.5 million of losses attributable to Hurricanes Ike and Gustav, which represented 14.7 and 3.5 percentage points of the loss ratio, respectively. Talbot marine line loss ratios, excluding prior year development, for the three months ended

September 30, 2009 and 2008 were 58.7% and 60.8%, respectively.

For the three months ended September 30, 2009, the specialty lines include \$34.3 million relating to current year losses and \$9.6 million due to favorable development on prior accident years. This favorable development is primarily due to further favorable development on the financial institutions lines. For the three months ended September 30, 2008, Talbot's specialty lines incurred \$0.5 million and \$0.5 million of losses attributable to Hurricanes Ike and Gustav, which represented 1.0 and 0.9 percentage points of the loss ratio, respectively. Talbot

**Table of Contents**

specialty lines loss ratios, excluding prior year development and the loss events identified above, for the three months ended September 30, 2009 and 2008 were 57.3% and 39.4%, respectively.

**Policy Acquisition Costs**

Policy acquisition costs for the three months ended September 30, 2009 were \$64.2 million compared to \$60.4 million for the three months ended September 30, 2008, an increase of \$3.8 million or 6.3%. Policy acquisition costs as a percent of net premiums earned for the three months ended September 30, 2009 and 2008 were 17.1% and 17.8%, respectively.

| (Dollars in thousands) | Policy acquisition costs |               |                    |               |             |
|------------------------|--------------------------|---------------|--------------------|---------------|-------------|
|                        | Three months ended       |               | Three months ended |               | %<br>Change |
|                        | September 30, 2009       |               | September 30, 2008 |               |             |
| Property               | \$ 24,919                | 38.8%         | \$ 24,189          | 40.0%         | 3.0%        |
| Marine                 | 21,586                   | 33.6%         | 20,796             | 34.4%         | 3.8%        |
| Specialty              | 17,731                   | 27.6%         | 15,440             | 25.6%         | 14.8%       |
| <b>Total</b>           | <b>\$ 64,236</b>         | <b>100.0%</b> | <b>\$ 60,425</b>   | <b>100.0%</b> | <b>6.3%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

*Validus Re.* Validus Re policy acquisition costs for the three months ended September 30, 2009 were \$32.6 million compared to \$26.5 million for the three months ended September 30, 2008, an increase of \$6.1 million or 23.1%.

| (Dollars in thousands) | Policy acquisition costs |               |                    |               |              |
|------------------------|--------------------------|---------------|--------------------|---------------|--------------|
|                        | Three months ended       |               | Three months ended |               | %<br>Change  |
|                        | September 30, 2009       |               | September 30, 2008 |               |              |
| Property               | \$ 22,884                | 70.1%         | \$ 19,027          | 71.8%         | 20.3%        |
| Marine                 | 6,392                    | 19.6%         | 4,990              | 18.8%         | 28.1%        |
| Specialty              | 3,372                    | 10.3%         | 2,503              | 9.4%          | 34.7%        |
| <b>Total</b>           | <b>\$ 32,648</b>         | <b>100.0%</b> | <b>\$ 26,520</b>   | <b>100.0%</b> | <b>23.1%</b> |

(a) The results of operations for IPC are consolidated



only from the  
September 2009  
date of  
acquisition.  
Consequently,  
2008 data does  
not include IPC  
financial results.

Policy acquisition costs include brokerage, commission and excise tax and are generally driven by contract terms and are normally a set percentage of premiums and are also net of ceding commission income on retrocessions. Policy acquisition costs as a percent of net premiums earned for the three months ended September 30, 2009 and 2008 were 16.3% and 14.6%, respectively. The policy acquisition ratio increased on the property and marine lines due primarily to the effects of Hurricanes Ike and Gustav reinstatement premiums earned without related policy acquisition costs for three months ended September 30, 2008. The policy acquisition ratio increased on the specialty lines due primarily to an upwards premium adjustment on a specialty lines proportional contract with a high portion of policy acquisition costs for three months ended September 30, 2008.

*Talbot.* Talbot policy acquisition costs for the three months ended September 30, 2009 were \$33.1 million compared to \$34.0 million for the three months ended September 30, 2008, a decrease of \$0.9 million or 2.7%.

| (Dollars in thousands) | Policy acquisition costs |               |                    |               |               |
|------------------------|--------------------------|---------------|--------------------|---------------|---------------|
|                        | Three months ended       |               | Three months ended |               | %<br>Change   |
|                        | September 30, 2009       |               | September 30, 2008 |               |               |
| Property               | \$ 3,553                 | 10.7%         | \$ 5,283           | 15.5%         | (32.7)%       |
| Marine                 | 15,194                   | 45.9%         | 15,806             | 46.5%         | (3.9)%        |
| Specialty              | 14,359                   | 43.4%         | 12,937             | 38.0%         | 11.0%         |
| <b>Total</b>           | <b>\$33,106</b>          | <b>100.0%</b> | <b>\$ 34,026</b>   | <b>100.0%</b> | <b>(2.7)%</b> |

**Table of Contents**

Policy acquisition costs as a percent of net premiums earned were 18.9% and 21.5%, respectively, for the three months ended September 30, 2009 and 2008. This decrease is primarily due to the high value of commissions receivable on quota share and surplus treaties and the onshore energy lines within the property lines.

**General and Administrative Expenses**

General and administrative expenses for the three months ended September 30, 2009 were \$46.0 million compared to \$30.1 million for the three months ended September 30, 2008, an increase of \$15.9 million or 52.8%. The increase was a result of increased expenses in both the Validus Re and Talbot segments.

| (Dollars in thousands)   | General and administrative expenses |               |                    |               |              |
|--------------------------|-------------------------------------|---------------|--------------------|---------------|--------------|
|                          | Three months ended                  |               | Three months ended |               | % Change     |
|                          | September 30, 2009                  |               | September 30, 2008 | (a)           |              |
| Validus Re               | \$ 17,987                           | 39.1%         | \$ 7,972           | 26.4%         | 125.6%       |
| Talbot                   | 23,424                              | 50.9%         | 17,851             | 59.3%         | 31.2%        |
| Corporate & Eliminations | 4,625                               | 10.0%         | 4,297              | 14.3%         | 7.6%         |
| <b>Total</b>             | <b>\$ 46,036</b>                    | <b>100.0%</b> | <b>\$ 30,120</b>   | <b>100.0%</b> | <b>52.8%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

General and administrative expense ratios for the three months ended September 30, 2009 and 2008 was 13.8% and 10.6%, respectively. General and administrative expense ratio is the sum of general and administrative expenses and share compensation expense divided by net premiums earned.

| (Dollars in thousands)     | Three months ended |                                      | Three months ended     |                                      |
|----------------------------|--------------------|--------------------------------------|------------------------|--------------------------------------|
|                            | September 30, 2009 |                                      | September 30, 2008 (a) |                                      |
|                            | Expenses           | Expenses as % of Net Earned Premiums | Expenses               | Expenses as % of Net Earned Premiums |
| General and Administrative | \$ 46,036          | 12.2%                                | \$ 30,120              | 8.8%                                 |
| Share Compensation         | 5,862              | 1.6%                                 | 6,012                  | 1.8%                                 |
| <b>Total</b>               | <b>\$ 51,898</b>   | <b>13.8%</b>                         | <b>\$ 36,132</b>       | <b>10.6%</b>                         |

(a) The results of operations for

IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

General and administrative expenses of \$46.0 million in the three months ended September 30, 2009 represents 12.2 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 September 30, 2009 were \$18.0 million compared to \$8.0 million for the three months ended September 30, 2008, an increase of \$10.0 million or 125.6%. General and administrative expenses have increased primarily as a result of an additional accrual for the performance bonus compared to a performance bonus reduction for the three months ended September 30, 2008 and the increase in staff to 121 at September 30, 2009 from 86 at September 30, 2008. General and administrative expenses are generally comprised of salaries and benefits, professional fees, rent and office expenses. Validus Re's general and administrative expenses as a percent of net premiums earned for the three months ended September 30, 2009 and 2008 were 9.0% and 4.4%, respectively.

*Talbot.* Talbot general and administrative expenses for the three months ended September 30, 2009 were \$23.4 million compared to \$17.9 million for the three months ended September 30, 2008, an increase of \$5.6 million or 31.2%. General and administrative expenses have increased primarily as a result of the increase in staff to 213 at September 30, 2009 from 175 at September 30, 2008 and expenses related to the new onshore energy and aviation

**Table of Contents**

underwriting teams. Talbot's general and administrative expenses as a percent of net premiums earned for the three months ended September 30, 2009 and 2008 were 13.4% and 11.3%, respectively.

*Corporate & Eliminations.* Corporate general and administrative expenses for the three months ended September 30, 2009 were \$4.6 million compared to \$4.3 million for the three months ended September 30, 2008, an increase of \$0.3 million or 7.6%. Corporate general and administrative expenses are comprised of executive and board expenses, internal and external audit expenses and other cost relating to the Company as a whole.

**Share Compensation Expense**

Share compensation expense for the three months ended September 30, 2009 were \$5.9 million compared to \$6.0 million for the three months ended September 30, 2008, a decrease of \$0.2 million or 2.5%. 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)   | Share compensation expenses           |               |                                       |               |               |
|--------------------------|---------------------------------------|---------------|---------------------------------------|---------------|---------------|
|                          | Three months ended September 30, 2009 |               | Three months ended September 30, 2008 |               | % Change      |
| Validus Re               | \$ 1,766                              | 30.1%         | \$ 1,809                              | 30.1%         | (2.4)%        |
| Talbot                   | 1,371                                 | 23.4%         | 1,164                                 | 19.4%         | 17.8%         |
| Corporate & Eliminations | 2,725                                 | 46.5%         | 3,039                                 | 50.5%         | (10.3)%       |
| <b>Total</b>             | <b>\$ 5,862</b>                       | <b>100.0%</b> | <b>\$ 6,012</b>                       | <b>100.0%</b> | <b>(2.5)%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

Share compensation expense of \$5.9 million in the three months ended September 30, 2009 represents 1.6 percentage points of the general and administrative expense ratio.

*Validus Re.* Validus Re share compensation expense for the three months ended September 30, 2009 was \$1.8 million compared to \$1.8 million for the three months ended September 30, 2008. Share compensation expense as a percent of net premiums earned for the three months ended September 30, 2009 and 2008 were 0.9% and 1.0%, respectively.

*Talbot.* Talbot share compensation expense for the three months ended September 30, 2009 was \$1.4 million compared to \$1.2 million for the three months ended September 30, 2008. Share compensation expense as a percent of net premiums earned for the three months ended September 30, 2009 and 2008 was 0.8% and 0.7%, respectively.

*Corporate & Eliminations.* Corporate share compensation expense for the three months ended September 30, 2009 was \$2.7 million compared to \$3.0 million for the three months ended September 30, 2008, a decrease of \$0.3 million or 10.3%. This decrease was due primarily to several share award issuances with vesting periods greater than one year that vested during the year ended December 31, 2008 and therefore had no further amortization expense during the three months ended September 30, 2009.

**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 acquisition costs combined with general and administrative expenses by net premiums earned. The following table presents the losses and loss expenses ratio, policy acquisition cost ratio, general and administrative expense ratio, expense ratio and combined ratio for the three months ended September 30, 2009 and 2008.

**Table of Contents**

|  | <b>Three months<br/>ended<br/>September 30,<br/>2009</b> | <b>Three months<br/>ended<br/>September 30,<br/>2008 (a)</b> | <b>Percentage<br/>point<br/>change</b> |
|--|--|--|--|
| Losses and loss expenses ratio               | 35.8%  | 93.9%  | (58.1)                                 |
| Policy acquisition cost ratio                | 17.1%  | 17.8%  | (0.7)                                  |
| General and administrative expense ratio (1) | 13.8%  | 10.6%  | 3.2                                    |
| Expense ratio                                | 30.9%  | 28.4%  | 2.5                                    |
| <b>Combined ratio</b>                        | <b>66.7%</b>   | <b>122.3%</b>  | <b>(55.6)</b>                          |

(1) Includes general and administrative expense and share compensation expense.

|  | <b>Three months<br/>ended<br/>September 30,<br/>2009</b> | <b>Three months<br/>ended<br/>September 30,<br/>2008 (a)</b> | <b>Percentage<br/>point<br/>change</b> |
|--|--|--|--|
| <i>Validus Re</i>                        |  |  |  |
| Losses and loss expenses ratio           | 23.0%  | 119.7%   | (96.7)                                 |
| Policy acquisition cost ratio            | 16.3%  | 14.6%  | 1.7                                    |
| General and administrative expense ratio | 9.9%   | 5.4%   | 4.5                                    |
| Expense ratio                            | 26.2%  | 20.0%  | 6.2                                    |
| <b>Combined ratio</b>                    | <b>49.2%</b>   | <b>139.7%</b>  | <b>(90.5)</b>                          |

|  | <b>Three months<br/>ended<br/>September 30,<br/>2009</b> | <b>Three months<br/>ended<br/>September 30,<br/>2008</b> | <b>Percentage<br/>point<br/>change</b> |
|--|--|--|--|
| <i>Talbot</i>                            |  |  |  |
| Losses and loss expenses ratio           | 50.4%  | 64.2%  | (13.8)                                 |
| Policy acquisition cost ratio            | 18.9%  | 21.5%  | (2.6)                                  |
| General and administrative expense ratio | 14.2%  | 12.0%  | 2.2                                    |
| Expense ratio                            | 33.1%  | 33.5%  | (0.4)                                  |
| <b>Combined ratio</b>                    | <b>83.5%</b>   | <b>97.7%</b>   | <b>(14.2)</b>                          |

(a)

The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

### Underwriting Income (Loss)

Underwriting income (loss) for the three months ended September 30, 2009 was \$124.4 million compared to (\$75.7) million for the three months ended September 30, 2008, an increase of \$200.1 million, or 264.4%.

|                               | Three months ended September 30, |              |                    |              |               |
|-------------------------------|----------------------------------|--------------|--------------------|--------------|---------------|
|                               |                                  | % of<br>Sub  |                    | % of<br>Sub  | %<br>Change   |
| <b>(Dollars in thousands)</b> | <b>2009</b>                      | <b>total</b> | <b>2008 (a)</b>    | <b>total</b> |               |
| Validus Re                    | \$ 101,380                       | 77.8%        | \$ (71,986)        | 105.1%       | 240.8%        |
| Talbot                        | 28,883                           | 22.2%        | 3,506              | (5.1)%       | 723.8%        |
| Sub total                     | 130,263                          | 100.0%       | (68,480)           | 100.0%       | 290.2%        |
| Corporate & Eliminations      | (5,832)                          |              | (7,215)            |              | 19.2%         |
| <b>Total</b>                  | <b>\$ 124,431</b>                |              | <b>\$ (75,695)</b> |              | <b>264.4%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

The underwriting results of an insurance or reinsurance company are also often measured by reference to its underwriting income, which is a non-GAAP measure as previously defined. 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 Operations and Comprehensive Income line items, as described below.

**Table of Contents**

| <b>(Dollars in thousands)</b>                | <b>Three months<br/>ended<br/>September 30,<br/>2009</b> | <b>Three months<br/>ended<br/>September 30,<br/>2008 (a)</b> |
|--|--|--|
| <b>Underwriting income (loss)</b>            | \$ 124,431   | \$ (75,695)  |
| Net investment income                        | 29,532   | 36,379   |
| Other income                                 | 1,101  | 1,269  |
| Finance expenses                             | (11,257)   | (14,517)   |
| Foreign exchange (losses) gains              | (5,244)  | (44,933)   |
| Gain on bargain purchase, net of expenses    | 302,950  |  |
| Net realized gains (losses) on investments   | 5,429  | (13,667)   |
| Net unrealized gains (losses) on investments | 50,437   | (14,649)   |
| <b>Net income (loss) before tax</b>          | <b>\$ 497,379</b>  | <b>\$ (125,813)</b>  |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

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 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 bonus component of 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 September 30, 2009 was \$29.5 million compared to \$36.4 million for the three months ended September 30, 2008, a decrease of \$6.8 million or 18.8%. Net investment income decreased as a result of reduced market yields and higher quarterly average cash balances. Net investment income is comprised of accretion of premium or discount on fixed maturities, interest on coupon-paying bonds, short-term

**Table of Contents**

investments and cash and cash equivalents, partially offset by investment management fees. The components of net investment income for the three months ended September 30, 2009 and 2008 are as presented below.

| <b>(Dollars in thousands)</b>               | <b>Three months<br/>ended<br/>September 30,<br/>2009</b> | <b>Three months<br/>ended<br/>September 30,<br/>2008 (a)</b> | <b>%<br/>Change</b> |
|---|--|--|---------------------|
| Fixed maturities and short-term investments | \$ 29,427  | \$ 32,443  | (9.3)%              |
| Cash and cash equivalents                   | 742  | 4,308  | (82.8)%             |
| Securities lending income                   | 171  | 261  | (34.5)%             |
| <b>Total gross investment income</b>        | <b>30,340</b>  | <b>37,012</b>  | <b>(18.0)%</b>      |
| Investment expenses                         | (808)  | (633)  | 27.6%               |
| <b>Net investment income</b>                | <b>\$ 29,532</b>   | <b>\$ 36,379</b>   | <b>(18.8)%</b>      |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

Investment management fees incurred relate to BlackRock Financial Management, Inc. ( BlackRock ) and Goldman Sachs Asset Management L.P. and its affiliates ( GSAM ). Each of Merrill Lynch & Co, Inc. ( Merrill Lynch ), a wholly owned subsidiary of Bank of America Corp., and Goldman Sachs are major shareholders of the Company. BlackRock is considered a related party due to its merger in February 2006 with Merrill Lynch Investment Managers. Investment management fees earned by BlackRock for the three months ended September 30, 2009 and 2008 were \$0.6 million and \$0.3 million, respectively. Investment management fees earned by GSAM for the three months ended September 30, 2009 and 2008 were \$0.4 million and \$0.3 million, respectively. Management believes that the fees charged were consistent with those that would have been charged in arm's-length transactions with unrelated third parties.

Annualized effective investment yield is based on the weighted average investments held calculated on a simple period average and excludes net unrealized gains (losses), foreign exchange gains (losses) on investments and the foreign exchange effect of insurance balances. The Company's annualized effective investment yield was 2.56% and 4.49% for the three months ended September 30, 2009 and 2008, respectively, and the average duration at September 30, 2009 was 2.2 years (December 31, 2008 1.8 years).

**Finance Expenses**

Finance expenses for the three months ended September 30, 2009 were \$11.3 million compared to \$14.5 million for the three months ended September 30, 2008, a decrease of \$3.3 million or 22.5%. The decrease was primarily a result of a \$2.1 million decrease in Talbot third party FAL expense.

Finance expenses also include the amortization of debt offering costs and discounts and fees related to our credit facilities.

| <b>(Dollars in thousands)</b>                    | <b>Three months ended<br/>September 30,</b> |                  | <b>%</b>       |
|--|---|------------------|----------------|
|  | <b>2009</b>                                 | <b>2008 (a)</b>  | <b>Change</b>  |
| 9.069% Junior Subordinated Deferrable Debentures | \$ 3,588                                    | \$ 3,588         | 0.0%           |
| 8.480% Junior Subordinated Deferrable Debentures | 3,348                                       | 3,509            | (4.6)%         |
| Credit facilities                                | 395   | 218              | 81.2%          |
| Talbot FAL facilities                            | 62  | 44               | 40.9%          |
| Talbot other interest                            |   | (194)            | NM             |
| Talbot third party FAL facility                  | 3,864                                       | 7,352            | (47.4)%        |
| <b>Finance expenses</b>                          | <b>\$ 11,257</b>                            | <b>\$ 14,517</b> | <b>(22.5)%</b> |

NM: Not Meaningful

**Table of Contents**

- (a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

Capital in Lloyd's entities, whether personal or corporate, is required to be set annually for the prospective year and held by Lloyd's in trust (Funds at Lloyd's or FAL). In underwriting years up to and including 2007, Talbot's FAL has been provided both by Talbot and by third parties, thereafter Talbot's FAL has been provided exclusively by the Company. Because the third party FAL providers remain on risk until each year of account that their support closes (normally after three years), Talbot must retain third party FAL even if a third party FAL provider has ceased to support the active underwriting year. This is achieved by placing such FAL in escrow outside Lloyd's. Thus the total FAL facility available to the Company is the total FAL for active and prior underwriting years, although the Company can only apply specific FAL against losses incurred by an underwriting year that such FAL is contracted to support.

For each year of account up to and including the 2007 year of account, between 30% and 40% of an amount equivalent to each underwriting year's profit is payable to Talbot third party FAL providers. However, some of these costs are fixed. There are no FAL finance charges related to the 2008 and 2009 years of account as there were no third party FAL providers in those periods.

The FAL finance charges relate to total syndicate profit (underwriting income, investment income and realized and unrealized capital gains and losses). FAL finance charges and total syndicate profits are analyzed by underwriting year of account as follows:

| Underwriting Year of Account<br>(Dollars in thousands) | Three months ended September 30,<br>FAL Finance Charges as<br>% of Total |          |                           |           |                  |          |
|--|--|----------|---------------------------|-----------|------------------|----------|
|  | FAL Finance<br>Charges   |          | Total Syndicate<br>Profit |           | Syndicate Profit |          |
|  | 2009   | 2008     | 2009                      | 2008      | 2009             | 2008 (1) |
| 2006 (1)   | \$   | \$ 4,801 | \$                        | \$ 12,614 | NM               | 38.1%    |
| 2007   | 3,864  | 2,551    | 11,696                    | 5,583     | 33.0%            | 45.7%    |
| 2008   |  |          | 5,936                     | (19,051)  | NM               | NM       |
| 2009   |  |          | 24,254                    |           | NM               | NM       |
| <b>Total</b>   | \$ 3,864   | \$ 7,352 | \$ 41,886                 | \$ (854)  | 9.2%             | (860.9)% |
| Percentage excluding years in deficit                  |  |          |                           |           | 9.2%             | 40.4%    |

- (1) The earliest year of account includes the run-off of prior (closed) years of account.

NM: Not Meaningful

FAL finance charges are based on syndicate profit but include fixed elements. FAL finance charges for the three months ended September 30, 2009 were \$3.8 million compared to \$7.4 million for the three months ended September 30, 2008, a decrease of \$3.5 million. This decrease was due to the absence of FAL finance charges related to the 2006 year of account, which is now closed.

Total syndicate profit, as set out in the table below, is reconciled to the Talbot segment net income by the addition or subtraction of items noted below.

| <b>(Dollars in thousands)</b>                  | <b>Three months<br/>ended<br/>September 30,<br/>2009</b> | <b>Three months<br/>ended<br/>September 30,<br/>2008</b> |
|--|--|--|
| <b>Total syndicate profit</b>                  | \$ 41,886  | \$ (854)   |
| FAL Finance expenses                           | (3,864)  | (7,352)  |
| Managing agent's fee (1)                       | 2,428  | 2,302  |
| Managing agent's profit commission (2)         | 5,145  | 3,241  |
| Investment income (3)                          | 4,077  | 2,613  |
| Other segment operating income (expenses), net | (10,310)   | (10,291)   |
| Share compensation (expenses)                  | (1,371)  | (1,163)  |
| Intangible amortization (expenses)             | (1,040)  | (1,040)  |
| Tax benefit (expense)                          | 1,840  | (457)  |
| <b>Talbot segment net income</b>               | <b>\$ 38,791</b>   | <b>\$ (13,001)</b>                                       |

(1) 1.5% of syndicate capacity; corresponding syndicate expense reflected in total syndicate profit, above.

(2) 15.0% of syndicate profit; corresponding syndicate expense reflected in total syndicate profit, above.

(3) On FAL and on non-syndicate cash balances.

**Table of Contents****Gain on Bargain Purchase, Net of Expenses**

On September 4, 2009, the Company acquired all of the outstanding shares of IPC from a group of institutional and other investors. Pursuant to the Amalgamation Agreement, the Company acquired all of IPC's outstanding common shares in exchange for the Company's common shares and cash. The purchase price paid by the Company was \$1,746.2 million for net assets acquired of \$2,076.9 million. The Company expensed as incurred \$27.7 million of transaction expenses and \$21.7 million for amortization of intangibles related to the acquisition for the three months ended September 30, 2009, resulting in a gain on bargain purchase of \$303.0 million for the three months ended September 30, 2009. Transaction expenses are comprised of primarily legal, corporate advisory, IPC employee termination benefits and audit related services.

**Net Realized (Losses) Gains on Investments**

Net realized gains on investments for the three months ended September 30, 2009 were \$5.4 million compared to losses of (\$13.7) million for the three months ended September 30, 2008. The net realized gains for the three months ended September 30, 2009 resulted primarily from the disposition of selected fixed maturities to finance the purchase of IPC.

On August 28, 2009, the Company sold short equity index futures contracts with a goal of hedging IPC's mutual fund equity portfolio exposure. The contracts were closed when the equity positions were fully redeemed on September 9, 2009. The Company experienced a (\$3.3) million realized investment (loss) as a result of the futures contracts.

**Net Unrealized Gains (Losses) on Investments**

Net unrealized gains on investments for the three months ended September 30, 2009 were \$50.4 million compared to losses of (\$14.6) million for the three months ended September 30, 2008. The net unrealized gains in the three months ended September 30, 2009 resulted primarily from improved market conditions for fixed income securities.

The net unrealized gains on investments for the three months ended September 30, 2009 included a \$2.0 million unrealized gain on the fund of hedge funds purchased in the IPC Acquisition. The fund of hedge funds was included in other investments on the balance sheet as at September 30, 2009.

Net unrealized gains 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. Certain non-Agency RMBS securities were identified as trading in inactive markets. The change in fair value for the identified non-Agency RMBS securities was a \$0.6 million decrease in net unrealized loss on investments for the three months ended September 30, 2009. Further details are provided in the Investments section below.

**Other Income**

Other income for the three months ended September 30, 2009 was \$1.1 million compared to \$1.3 million for the three months ended September 30, 2008, a decrease of \$0.2 million or 13.2%.

**Foreign Exchange Gains (Losses)**

Foreign exchange (losses) for the three months ended September 30, 2009 were (\$5.2) million compared to (\$44.9) million for the three months ended September 30, 2008, a decrease of \$39.7 million. The decrease in foreign exchange (losses) was due primarily to the increased value of assets denominated in foreign currencies relative to the U.S. dollar reporting currency for the three months ended September 30, 2009, as compared to the three months ended September 30, 2008. For the three months ended September 30, 2009, Validus Re recognized foreign exchange gains of \$0.7 million that were offset by Talbot foreign exchange (losses) of (\$6.0) million. For the three months ended September 30, 2009, Talbot segment foreign exchange (losses) were (\$6.0) million compared to (losses) of (\$22.0) million for the three months ended September 30, 2008, a decrease of \$16.0 million. The decrease in Talbot segment foreign exchange (losses) was due primarily to; (1) a \$5.5 million increased gain on the recurring revaluation of net unearned premiums and deferred acquisition costs; (2) a \$15.2 million increase due to the absence, in the three months ended September 30, 2009, of a non-recurring loss on revaluation of foreign exchange to reporting currency and the sale of U.S. dollars for the three months ended September 30, 2008; and (3) an (\$8.1) million (loss) related to a prior year tax adjustment. The British pound sterling to U.S. dollar exchange rates were 1.65 and 1.59 at June 30, 2009 and

September 30, 2009, respectively. Certain premiums receivable and liabilities for losses incurred in currencies other than the U.S. dollar are exposed to the risk of changes in value resulting from fluctuations in foreign exchange rates and may affect financial results in the future.

**Table of Contents**

At September 30, 2009, Talbot's balance sheet includes net unearned premiums and deferred acquisition costs denominated in foreign currencies of approximately \$89.3 million and \$19.3 million, respectively. These balances consisted of British pounds sterling and Canadian dollars of \$63.3 million and \$6.7 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. During the three months ended September 30, 2009, this translation process resulted in foreign exchange gains that will reverse in future periods as net unearned premiums and deferred acquisition costs are earned together with (losses) arising from the reversal of losses incurred in previous periods. Additional foreign exchange (losses) gains may be incurred on the translation of net unearned premiums and deferred acquisition costs arising from insurance and reinsurance premiums written in future periods.

**Tax Benefit (Expense)**

Tax benefit for the three months ended September 30, 2009 was \$1.8 million compared to an (expense) of (\$0.5) million for the three months ended September 30, 2008, a change of \$2.3 million.



**Table of Contents**

The following table presents results of operations for the three and nine months ended September 30, 2009 and 2008:

| <b>(Dollars in thousands)</b>                 | <b>Three months ended<br/>September 30,</b> |                 | <b>Nine months ended<br/>September 30,</b> |                 |
|---|---|-----------------|--|-----------------|
|   | <b>2009</b>                                 | <b>2008 (a)</b> | <b>2009</b>                                | <b>2008 (a)</b> |
| Gross premiums written                        | \$ 331,028                                  | \$ 269,236      | \$ 1,365,951                               | \$ 1,170,749    |
| Reinsurance premiums ceded                    | (67,687)                                    | (35,139)        | (202,489)                                  | (121,438)       |
| Net premiums written                          | 263,341                                     | 234,097         | 1,163,462                                  | 1,049,311       |
| Change in unearned premiums                   | 111,376                                     | 105,229         | (141,786)                                  | (108,823)       |
| Net premiums earned                           | 374,717                                     | 339,326         | 1,021,676                                  | 940,488         |
| Losses and loss expenses                      | 134,152                                     | 318,464         | 390,736                                    | 580,578         |
| Policy acquisition costs                      | 64,236                                      | 60,425          | 190,125                                    | 173,545         |
| General and administrative expenses           | 46,036                                      | 30,120          | 125,315                                    | 101,139         |
| Share compensation expenses                   | 5,862                                       | 6,012           | 18,848                                     | 19,818          |
| Total underwriting deductions                 | 250,286                                     | 415,021         | 725,024                                    | 875,080         |
| Underwriting income (loss) (b)                | 124,431                                     | (75,695)        | 296,652                                    | 65,408          |
| Net investment income                         | 29,532                                      | 36,379          | 83,267                                     | 108,857         |
| Other income                                  | 1,101                                       | 1,269           | 2,875                                      | 3,666           |
| Finance expenses                              | (11,257)                                    | (14,517)        | (29,732)                                   | (48,796)        |
| Operating income (loss) before taxes (b)      | 143,807                                     | (52,564)        | 353,062                                    | 129,135         |
| Tax benefit (expense)                         | 1,799                                       | (487)           | 3,301                                      | (4,992)         |
| Net operating income (loss) (a) (b)           | 145,606                                     | (53,051)        | 356,363                                    | 124,143         |
| Gain on bargain purchase, net of expenses     | 302,950                                     |                 | 287,099                                    |                 |
| Realized gain on repurchase of debentures     |   |                 |  | 8,752           |
| Net realized gains (losses) on investments    | 5,429                                       | (13,667)        | (20,642)                                   | (8,348)         |
| Net unrealized gains (losses) on investments  | 50,437                                      | (14,649)        | 109,839                                    | (72,608)        |
| Foreign exchange (losses)                     | (5,244)                                     | (44,933)        | (1,012)                                    | (35,843)        |
| Net income (loss)                             | \$ 499,178                                  | \$ (126,300)    | \$ 731,647                                 | \$ 16,096       |
| Selected ratios:                              |   |                 |  |                 |
| Net premiums written / Gross premiums written | 79.6%                                       | 86.9%           | 85.2%                                      | 89.6%           |
| Losses and loss expenses                      | 35.8%                                       | 93.9%           | 38.2%                                      | 61.7%           |
| Policy acquisition costs                      | 17.1%                                       | 17.8%           | 18.6%                                      | 18.5%           |
| General and administrative expenses           | 13.8%                                       | 10.6%           | 14.1%                                      | 12.9%           |
| Expense ratio                                 | 30.9%                                       | 28.4%           | 32.7%                                      | 31.4%           |

|                |       |        |       |       |
|----------------|-------|--------|-------|-------|
| Combined ratio | 66.7% | 122.3% | 70.9% | 93.1% |
|----------------|-------|--------|-------|-------|

- a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.
- b) Non-GAAP Financial Measures. In presenting the Company's results, management has included and discussed underwriting income (loss) 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. A  
reconciliation  
underwriting  
income  
(loss) measure to  
net income, the  
most comparable  
U.S. GAAP  
financial  
measure, is  
presented in the  
section below  
entitled  
Underwriting  
Income.

**Table of Contents**

|                                     | <b>Three months ended<br/>September 30,</b> |                 | <b>Nine months ended<br/>September 30,</b> |                 |
|-------------------------------------|---|-----------------|--|-----------------|
|                                     | <b>2009</b>                                 | <b>2008 (a)</b> | <b>2009</b>                                | <b>2008 (a)</b> |
| <b>Validus Re</b>                   |   |                 |  |                 |
| Gross premiums written              | \$ 124,704                                  | \$ 125,029      | \$ 734,390                                 | \$ 643,898      |
| Reinsurance premiums ceded          | (38,435)                                    | (36,286)        | (94,794)                                   | (61,237)        |
| Net premiums written                | 86,269                                      | 88,743          | 639,596                                    | 582,661         |
| Change in unearned premiums         | 113,499                                     | 92,653          | (101,684)                                  | (93,498)        |
| Net premiums earned                 | 199,768                                     | 181,396         | 537,912                                    | 489,163         |
| Losses and loss expenses            | 45,987                                      | 217,081         | 142,570                                    | 324,673         |
| Policy acquisition costs            | 32,648                                      | 26,520          | 90,346                                     | 72,232          |
| General and administrative expenses | 17,987                                      | 7,972           | 45,928                                     | 27,306          |
| Share compensation expenses         | 1,766                                       | 1,809           | 4,986                                      | 4,632           |
| Total underwriting deductions       | 98,388                                      | 253,382         | 283,830                                    | 428,843         |
| Underwriting income (loss) (b)      | 101,380                                     | (71,986)        | 254,082                                    | 60,320          |
| <b>Talbot</b>                       |   |                 |  |                 |
| Gross premiums written              | \$ 227,325                                  | \$ 157,307      | \$ 690,357                                 | \$ 556,335      |
| Reinsurance premiums ceded          | (50,253)                                    | (11,953)        | (166,491)                                  | (89,685)        |
| Net premiums written                | 177,072                                     | 145,354         | 523,866                                    | 466,650         |
| Change in unearned premiums         | (2,123)                                     | 12,576          | (40,102)                                   | (15,325)        |
| Net premiums earned                 | 174,949                                     | 157,930         | 483,764                                    | 451,325         |
| Losses and loss expenses            | 88,165                                      | 101,383         | 248,166                                    | 255,905         |
| Policy acquisition costs            | 33,106                                      | 34,026          | 102,378                                    | 101,458         |
| General and administrative expenses | 23,424                                      | 17,851          | 65,565                                     | 58,561          |
| Share compensation expenses         | 1,371                                       | 1,164           | 5,804                                      | 3,266           |
| Total underwriting deductions       | 146,066                                     | 154,424         | 421,913                                    | 419,190         |
| Underwriting income (loss) (b)      | 28,883                                      | 3,506           | 61,851                                     | 32,135          |
| <b>Corporate &amp; Eliminations</b> |   |                 |  |                 |
| Gross premiums written              | \$ (21,001)                                 | \$ (13,100)     | \$ (58,796)                                | \$ (29,484)     |
| Reinsurance premiums ceded          | 21,001                                      | 13,100          | 58,796                                     | 29,484          |
| Net premiums written                |   |                 |  |                 |
| Change in unearned premiums         |   |                 |  |                 |

## Net premiums earned

## Losses and loss expenses

|                                     |            |             |            |           |
|-------------------------------------|------------|-------------|------------|-----------|
| Policy acquisition costs            | (1,518)    | (121)       | (2,599)    | (145)     |
| General and administrative expenses | 4,625      | 4,297       | 13,822     | 15,272    |
| Share compensation expenses         | 2,725      | 3,039       | 8,058      | 11,920    |
| Total underwriting deductions       | 5,832      | 7,215       | 19,281     | 27,047    |
| Underwriting income (loss) (b)      | (5,832)    | (7,215)     | (19,281)   | (27,047)  |
| Total underwriting income (b)       | \$ 124,431 | \$ (75,695) | \$ 296,652 | \$ 65,408 |

a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

b) 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.

**Table of Contents****Nine months ended September 30, 2009 compared to nine months ended September 30, 2008**

Net income for the nine months ended September 30, 2009 was \$731.6 million compared to net income of \$16.1 million for the nine months ended September 30, 2008, an increase of \$715.6 million. The primary factors driving the increase in net income were:

Gain on bargain purchase, net of expenses of \$287.1 million on the IPC Acquisition;

Increase in underwriting income of \$231.2 million due primarily to reduced losses and loss expenses of \$189.8 and increased net premiums earned of \$81.2 million. For the nine months ended September 30, 2008, the Company incurred \$183.4 million and \$22.1 million, respectively, as a result of Hurricanes Ike and Gustav;

Increase in net unrealized gains on investments of \$182.4 million due to improved market conditions for fixed income securities; and

Decreased foreign exchange (losses) of \$34.8 million was due to the increased value of assets denominated in foreign currencies relative to the U.S. dollar reporting currency for the nine months ended September 30, 2009, as compared to the nine months ended September 30, 2008. Foreign exchange (losses) for the nine months ended September 30, 2009 were (\$1.0) million, as compared to (\$35.8) million for the nine months ended September 30, 2008.

Reduced finance expenses of \$19.1 million due to reduced FAL costs.

The items above were partially offset by the following factors:

Decrease in net investment income of \$25.6 million due to increased balances of cash and cash equivalents and lower returns on cash and fixed income investments.

The change in net income for the nine months ended September 30, 2009 of \$715.6 million is described in the following table:

|   |                   | <b>Nine months ended September 30, 2009</b>                         |               |              |              |
|---|-------------------|---|---------------|--------------|--------------|
|   |                   | <b>Increase (decrease) over the nine months ended September 30,</b> |               |              |              |
|   |                   | <b>2008 (a)</b>   |               |              |              |
|   |                   | <b>Corporate</b>  |               |              |              |
|   |                   | <b>and</b>  |               |              |              |
|   |                   | <b>other</b>  |               |              |              |
|   |                   | <b>reconciling</b>  |               |              |              |
|   |                   | <b>Validus</b>  |               |              |              |
|   |                   | <b>Re</b>   | <b>Talbot</b> | <b>items</b> | <b>Total</b> |
| <b>(Dollars in thousands)</b>             |                   |   |               |              |              |
| Hurricanes Ike and Gustav                 | net losses and    |   |               |              |              |
| loss expenses (b)                         |                   | \$ 172,635  | \$ 32,878     | \$           | \$ 205,513   |
| Hurricanes Ike and Gustav                 | net reinstatement |   |               |              |              |
| premiums (b)                              |                   | (19,268)  | (392)         |              | (19,660)     |
| Other underwriting income                 |                   | 40,395  | (2,770)       | 7,766        | 45,391       |
| Underwriting income (c)                   |                   | 193,762   | 29,716        | 7,766        | 231,244      |
| Net investment income                     |                   | (11,747)  | (11,629)      | (2,214)      | (25,590)     |
| Other income                              |                   | 2,889   | (1,226)       | (2,454)      | (791)        |
| Finance expenses                          |                   | (578)   | 18,133        | 1,509        | 19,064       |
|   |                   | 184,326   | 34,994        | 4,607        | 223,927      |
| Taxes                                     |                   | (29)  | 8,322         |              | 8,293        |
|   |                   | 184,297   | 43,316        | 4,607        | 232,220      |
| Gain on bargain purchase, net of expenses |                   |   |               | 287,099      | 287,099      |
| Realized gain on repurchase of debentures |                   |   |               | (8,752)      | (8,752)      |

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|  |                   |                  |                   |                   |
|--|-------------------|------------------|-------------------|-------------------|
| Net realized (losses) gains on investments   | (571)             | (11,723)         |                   | (12,294)          |
| Net unrealized gains (losses) on investments | 154,310           | 28,137           |                   | 182,447           |
| Foreign exchange (losses) gains              | 15,006            | 19,769           | 56                | 34,831            |
| <b>Net income</b>                            | <b>\$ 353,042</b> | <b>\$ 79,499</b> | <b>\$ 283,010</b> | <b>\$ 715,551</b> |

68

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**Table of Contents**

- (a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.
- (b) Hurricanes Ike and Gustav net losses and loss expenses and net reinstatement premiums recognized for the nine months ended September 30, 2008; therefore, figures exclude loss development in subsequent periods.
- (c) 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 nine months ended September 30, 2009 were \$1,366.0 million compared to \$1,170.7 million for the nine months ended September 30, 2008, an increase of \$195.2 million or 16.7%. The increase in gross premiums written was driven primarily by the property and marine lines which increased by \$101.2 million and \$50.4 million, respectively. Details of gross premiums written by line of business are provided below.

| (Dollars in thousands) | Gross premiums written |               |                     |               |              |
|------------------------|------------------------|---------------|---------------------|---------------|--------------|
|                        | Nine months ended      |               | Nine months ended   |               | % Change     |
|                        | September 30, 2009     |               | September 30, 2008  |               |              |
| Property               | \$ 679,207             | 49.7%         | \$ 577,976          | 49.4%         | 17.5%        |
| Marine                 | 386,303                | 28.3%         | 335,856             | 28.7%         | 15.0%        |
| Specialty              | 300,441                | 22.0%         | 256,917             | 21.9%         | 16.9%        |
| <b>Total</b>           | <b>\$ 1,365,951</b>    | <b>100.0%</b> | <b>\$ 1,170,749</b> | <b>100.0%</b> | <b>16.7%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009

date of  
acquisition.  
Consequently,  
2008 data does  
not include IPC  
financial results.

*Validus Re.* Validus Re gross premiums written for the nine months ended September 30, 2009 were \$734.4 million compared to \$643.9 million for the nine months ended September 30, 2008, an increase of \$90.5 million or 14.1%. Details of Validus Re gross premiums written by line of business are provided below.

| (Dollars in thousands) | Gross premiums written |               |                    |               |              |
|------------------------|------------------------|---------------|--------------------|---------------|--------------|
|                        | Nine months ended      |               | Nine months ended  |               | %<br>Change  |
|                        | September 30, 2009     | (a)           | September 30, 2008 | (a)           |              |
| Property               | \$ 499,143             | 67.9%         | \$ 471,963         | 73.3%         | 5.8%         |
| Marine                 | 153,913                | 21.0%         | 111,945            | 17.4%         | 37.5%        |
| Specialty              | 81,334                 | 11.1%         | 59,990             | 9.3%          | 35.6%        |
| <b>Total</b>           | <b>\$ 734,390</b>      | <b>100.0%</b> | <b>\$ 643,898</b>  | <b>100.0%</b> | <b>14.1%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

Validus Re gross premiums written increased across the property, marine and specialty lines by \$27.2 million, \$42.0 million and \$21.3 million, respectively. The increase in the property line was due primarily to gross premiums written on various new contracts where favorable changes in risk adjusted pricing met Validus Re's thresholds and rate increases on existing business. The increase in the marine line was due primarily to additional gross premiums written on proportional contracts where underlying insurance coverage terms have become more favorable. The

**Table of Contents**

gross and net amount of reinsurance limits exposed in the Gulf of Mexico have been reduced in 2009 despite the increased gross premiums written, due to more restrictive coverage terms and, in the case of gross limits, the non-renewal of the Company's collateralized quota share facility. The property and marine lines also benefited from \$21.6 million and \$5.4 million, respectively, of increased gross premiums written as a result of Talbot quota share, surplus treaty and excess of loss contracts. The quota share, surplus treaty and excess of loss contracts with Talbot are eliminated upon consolidation.

*Talbot.* Talbot gross premiums written for the nine months ended September 30, 2009 were \$690.4 million compared to \$556.3 million for the nine months ended September 30, 2008, an increase of \$134.0 million or 24.1%. The \$690.4 million of gross premiums written translated at third quarter 2008 rates of exchange would have been \$737.9 million during the nine months ended September 30, 2009, an increase of \$181.6 million or 32.6%. Details of Talbot gross premiums written by line of business are provided below.

| <b>(Dollars in thousands)</b> | <b>Gross premiums written</b> |               |                           |               |                     |
|-------------------------------|-------------------------------|---------------|---------------------------|---------------|---------------------|
|                               | <b>Nine months ended</b>      |               | <b>Nine months ended</b>  |               | <b>%<br/>Change</b> |
|                               | <b>September 30, 2009</b>     |               | <b>September 30, 2008</b> |               |                     |
| Property                      | \$ 218,650                    | 31.7%         | \$ 122,984                | 22.1%         | 77.8%               |
| Marine                        | 244,688                       | 35.4%         | 230,777                   | 41.5%         | 6.0%                |
| Specialty                     | 227,019                       | 32.9%         | 202,574                   | 36.4%         | 12.1%               |
| <b>Total</b>                  | <b>\$ 690,357</b>             | <b>100.0%</b> | <b>\$ 556,335</b>         | <b>100.0%</b> | <b>24.1%</b>        |

The increase in the property lines was due primarily to \$74.5 million of gross premiums written on the onshore energy lines and an \$18.0 million increase in gross premiums written by Validus Reaseguros, Inc., which acts as an approved Lloyd's coverholder for Syndicate 1183 targeting the Latin American and Caribbean markets, and commenced operations during 2008. The increase in the marine lines was due primarily to additional gross premiums written on proportional contracts where underlying insurance coverage terms have become more favorable. The increase in the specialty lines was due primarily to \$20.0 million of additional gross premiums written by the new aviation team.

**Reinsurance Premiums Ceded**

Reinsurance premiums ceded for the nine months ended September 30, 2009 were \$202.5 million compared to \$121.4 million for the nine months ended September 30, 2008, an increase of \$81.1 million, or 66.7%. This was due primarily to an increase of \$89.4 million on the property lines retrocession as described below.

| <b>(Dollars in thousands)</b> | <b>Reinsurance premiums ceded</b> |               |                           |               |                     |
|-------------------------------|-----------------------------------|---------------|---------------------------|---------------|---------------------|
|                               | <b>Nine months ended</b>          |               | <b>Nine months ended</b>  |               | <b>%<br/>Change</b> |
|                               | <b>September 30, 2009</b>         |               | <b>September 30, 2008</b> |               |                     |
| Property                      | \$ 137,118                        | 67.7%         | \$ 47,719                 | 39.2%         | 187.3%              |
| Marine                        | 28,097                            | 13.9%         | 36,616                    | 30.2%         | (23.3)%             |
| Specialty                     | 37,274                            | 18.4%         | 37,103                    | 30.6%         | 0.5%                |
| <b>Total</b>                  | <b>\$ 202,489</b>                 | <b>100.0%</b> | <b>\$ 121,438</b>         | <b>100.0%</b> | <b>66.7%</b>        |

(a) The results of operations for IPC are consolidated

only from the  
September 2009  
date of  
acquisition.

Consequently,  
2008 data does  
not include IPC  
financial results.

*Validus Re.* Validus Re reinsurance premiums ceded for the nine months ended September 30, 2009 were \$94.8 million compared to \$61.2 million for the nine months ended September 30, 2008, an increase of \$33.6 million, or 54.8%.

**Table of Contents**

| (Dollars in thousands) | Reinsurance premiums ceded |               |                    |               | %<br>Change  |
|------------------------|----------------------------|---------------|--------------------|---------------|--------------|
|                        | Nine months ended          |               | Nine months ended  |               |              |
|                        | September 30, 2009         | (a)           | September 30, 2008 | (a)           |              |
| Property               | \$ 80,014                  | 84.4%         | \$ 37,158          | 60.7%         | 115.3%       |
| Marine                 | 13,211                     | 13.9%         | 23,526             | 38.4%         | (43.8)%      |
| Specialty              | 1,569                      | 1.7%          | 553                | 0.9%          | 183.7%       |
| <b>Total</b>           | <b>\$ 94,794</b>           | <b>100.0%</b> | <b>\$ 61,237</b>   | <b>100.0%</b> | <b>54.8%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

Reinsurance premiums ceded on the property lines increased by \$42.9 million, due primarily to the due to the purchase of an additional \$34.0 million of catastrophe retrocessional coverage for IPC's U.S. property exposures. The decrease in the marine line was due primarily to the nonrenewal of a collateralized quota share retrocession treaty to which Validus Re ceded \$18.6 million for the nine months ended September 30, 2008.

Talbot. Talbot reinsurance premiums ceded for the nine months ended September 30, 2009 were \$166.5 million compared to \$89.7 million for the nine months ended September 30, 2008, an increase of \$76.8 million. The increase is primarily due to reinsurance premiums ceded on the onshore energy lines, as discussed above, and increased reinsurance premiums ceded under the quota share, surplus treaty and excess of loss contracts with Validus Re.

| (Dollars in thousands) | Reinsurance premiums ceded |               |                    |               | %<br>Change  |
|------------------------|----------------------------|---------------|--------------------|---------------|--------------|
|                        | Nine months ended          |               | Nine months ended  |               |              |
|                        | September 30, 2009         | (a)           | September 30, 2008 | (a)           |              |
| Property               | \$ 95,690                  | 57.5%         | \$ 27,532          | 30.7%         | 247.6%       |
| Marine                 | 27,184                     | 16.3%         | 19,956             | 22.3%         | 36.2%        |
| Specialty              | 43,617                     | 26.2%         | 42,197             | 47.0%         | 3.4%         |
| <b>Total</b>           | <b>\$ 166,491</b>          | <b>100.0%</b> | <b>\$ 89,685</b>   | <b>100.0%</b> | <b>85.6%</b> |

Property reinsurance premiums ceded on the onshore energy lines were \$50.0 million, 16.0% of these premiums were ceded to Validus Re. Reinsurance premiums ceded under the quota share, surplus treaty and excess of loss contracts with Validus Re for the nine months ended September 30, 2009 were \$58.8 million compared to \$29.5 million for the nine months ended September 30, 2008, an increase of \$29.3 million. Reinsurance premiums ceded under the quota share, surplus treaty and excess of loss contracts with Validus Re on the property and marine lines increased by \$21.6 million and \$5.4 million, respectively, as compared to the nine months ended September 30,

2008. The quota share, surplus treaty and excess of loss contracts with Validus Re are eliminated upon consolidation.

### Net Premiums Written

Net premiums written for the nine months ended September 30, 2009 were \$1,163.5 million compared to \$1,049.3 million for the nine months ended September 30, 2008, an increase of \$114.2 million, or 10.9%. The ratios of net premiums written to gross premiums written for the nine months ended September 30, 2009 and 2008 were 85.2% and 89.6%, respectively. Details of net premiums written by line of business are provided below.

| (Dollars in thousands) | Net premiums written |               |                     |               |              |
|------------------------|----------------------|---------------|---------------------|---------------|--------------|
|                        | Nine months ended    |               | Nine months ended   |               | %<br>Change  |
|                        | September 30, 2009   |               | September 30, 2008  | (a)           |              |
| Property               | \$ 542,089           | 46.6%         | \$ 530,257          | 50.6%         | 2.2%         |
| Marine                 | 358,206              | 30.8%         | 299,240             | 28.5%         | 19.7%        |
| Specialty              | 263,167              | 22.6%         | 219,814             | 20.9%         | 19.7%        |
| <b>Total</b>           | <b>\$ 1,163,462</b>  | <b>100.0%</b> | <b>\$ 1,049,311</b> | <b>100.0%</b> | <b>10.9%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

**Table of Contents**

Premium rates in most lines have increased during the nine months ended September 30, 2009 as compared to the same period in 2008. As a result of the Company's strategy to grow premiums written only when returns meet or exceed internal requirements, net premiums written have increased compared with the nine months ended September 30, 2008.

*Validus Re.* Validus Re net premiums written for the nine months ended September 30, 2009 were \$639.6 million compared to \$582.7 million for the nine months ended September 30, 2008, an increase of \$56.9 million or 9.8%. Details of net premiums written by line of business are provided below.

| (Dollars in thousands) | Net premiums written |               |                    |               |             |
|------------------------|----------------------|---------------|--------------------|---------------|-------------|
|                        | Nine months ended    |               | Nine months ended  |               | % Change    |
|                        | September 30, 2009   |               | September 30, 2008 | (a)           |             |
| Property               | \$ 419,129           | 65.5%         | \$ 434,805         | 74.6%         | (3.6)%      |
| Marine                 | 140,702              | 22.0%         | 88,419             | 15.2%         | 59.1%       |
| Specialty              | 79,765               | 12.5%         | 59,437             | 10.2%         | 34.2%       |
| <b>Total</b>           | <b>\$ 639,596</b>    | <b>100.0%</b> | <b>\$ 582,661</b>  | <b>100.0%</b> | <b>9.8%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

The increase in Validus Re net premiums written was driven by an increase in the marine line of \$52.3 million. This increase was a result of increased gross premiums written and decreased reinsurance premium ceded in the marine line, as discussed above. The ratios of net premiums written to gross premiums written were 87.1% and 90.5% for the nine months ended September 30, 2009 and 2008, respectively.

*Talbot.* Talbot net premiums written for the nine months ended September 30, 2009 were \$523.9 million compared to \$466.7 million for the nine months ended September 30, 2008, an increase of \$57.2 million or 12.3%. Details of net premiums written by line of business are provided below:

| (Dollars in thousands) | Net premiums written |               |                    |               |              |
|------------------------|----------------------|---------------|--------------------|---------------|--------------|
|                        | Nine months ended    |               | Nine months ended  |               | % Change     |
|                        | September 30, 2009   |               | September 30, 2008 |               |              |
| Property               | \$ 122,960           | 23.5%         | \$ 95,452          | 20.5%         | 28.8%        |
| Marine                 | 217,504              | 41.5%         | 210,821            | 45.1%         | 3.2%         |
| Specialty              | 183,402              | 35.0%         | 160,377            | 34.4%         | 14.4%        |
| <b>Total</b>           | <b>\$ 523,866</b>    | <b>100.0%</b> | <b>\$ 466,650</b>  | <b>100.0%</b> | <b>12.3%</b> |



The increase 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 nine months ended September 30, 2009 and 2008 were 75.9% and 83.9%, respectively. This decrease was due primarily to the 32.9% ratio of net premiums written to gross premiums written on the onshore energy lines for the nine months ended September 30, 2009.

**Change in Unearned Premiums**

Change in unearned premiums for the nine months ended September 30, 2009 was (\$141.8) million compared to (\$108.8) million for the nine months ended September 30, 2008, a change of \$33.0 million or 30.3%.

**Table of Contents**

|                                       | <b>Change in unearned premiums</b>                          |   |                     |
|---------------------------------------|---|---|---------------------|
|                                       | <b>Nine<br/>months<br/>ended<br/>September<br/>30, 2009</b> | <b>Nine months ended<br/>September 30,<br/>2008 (a)</b> | <b>%<br/>Change</b> |
| <b>(Dollars in thousands)</b>         |   |   |                     |
| Change in gross unearned premium      | \$ (236,202)  | \$ (150,532)  | 56.9%               |
| Change in prepaid reinsurance premium | 94,416  | 41,709  | 126.4%              |
| <b>Net change in unearned premium</b> | <b>\$ (141,786)</b>   | <b>\$ (108,823)</b>                                     | <b>30.3%</b>        |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

*Validus Re.* Validus Re's change in unearned premiums for the nine months ended September 30, 2009 was (\$101.7) million compared to (\$93.5) million for the nine months ended September 30, 2008, a change of \$8.2 million, or 8.8%.

|                                       | <b>Change in unearned premiums</b>                          |   |                     |
|---------------------------------------|---|---|---------------------|
|                                       | <b>Nine<br/>months<br/>ended<br/>September<br/>30, 2009</b> | <b>Nine months ended<br/>September 30,<br/>2008 (a)</b> | <b>%<br/>Change</b> |
| <b>(Dollars in thousands)</b>         |   |   |                     |
| Change in gross unearned premium      | \$ (138,856)  | \$ (109,200)  | 27.2%               |
| Change in prepaid reinsurance premium | 37,172  | 15,702  | 136.7%              |
| <b>Net change in unearned premium</b> | <b>\$ (101,684)</b>   | <b>\$ (93,498)</b>                                      | <b>8.8%</b>         |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition.

Consequently,  
2008 data does  
not include IPC  
financial results.

The difference in gross unearned premiums reflects the benefit of earning premiums on the increased gross premiums written of \$90.5 million, or 14.1%, from \$643.9 million for the nine months ended September 30, 2008 to \$734.4 million for the nine months ended September 30, 2009. In respect of prepaid reinsurance premiums, the change is a result primarily of the additional retrocessional coverage for the nine months ended September 30, 2009, as discussed above.

*Talbot.* The Talbot change in unearned premiums for the nine months ended September 30, 2009 was (\$40.1) million compared to (\$15.3) million for the nine months ended September 30, 2008, a change of \$24.8 million, or 161.7%.

|                                       | <b>Change in unearned premiums</b>                          |   |                     |
|---------------------------------------|---|---|---------------------|
|                                       | <b>Nine<br/>months<br/>ended<br/>September<br/>30, 2009</b> | <b>Nine months<br/>ended<br/>September 30,<br/>2008</b> | <b>%<br/>Change</b> |
| <b>(Dollars in thousands)</b>         |   |   |                     |
| Change in gross unearned premium      | \$ (97,346)   | \$ (41,332)   | 135.5%              |
| Change in prepaid reinsurance premium | 57,244  | 26,007  | 120.1%              |
| <b>Net change in unearned premium</b> | <b>\$ (40,102)</b>  | <b>\$ (15,325)</b>                                      | <b>161.7%</b>       |

The difference in gross unearned premiums arises principally from the increased gross premiums written in the property lines, specifically onshore energy exposures and premiums written by Validus Reaseguros, Inc. on the property treaty lines, for the nine months ended September 30, 2009, as compared to the nine months ended September 30, 2008. The increase in the change in prepaid reinsurance is reflective of the higher levels of ceded reinsurance, principally in the property line for the nine months ended September 30, 2009, as compared to the nine months ended September 30, 2008.

#### **Net Premiums Earned**

Net premiums earned for the nine months ended September 30, 2009 were \$1,021.7 million compared to \$940.5 million for the nine months ended September 30, 2008, an increase of \$81.2 million or 8.6%. The increase in net premiums earned was driven primarily by increased premiums earned at Validus Re of \$48.7 million.

**Table of Contents**

| (Dollars in thousands) | Net premiums earned |               |                    |               | %<br>Change |
|------------------------|---------------------|---------------|--------------------|---------------|-------------|
|                        | Nine months ended   |               | Nine months ended  |               |             |
|                        | September 30, 2009  |               | September 30, 2008 | (a)           |             |
| Property               | \$ 471,879          | 46.2%         | \$ 452,655         | 48.2%         | 4.2%        |
| Marine                 | 303,367             | 29.7%         | 274,110            | 29.1%         | 10.7%       |
| Specialty              | 246,430             | 24.1%         | 213,723            | 22.7%         | 15.3%       |
| <b>Total</b>           | <b>\$ 1,021,676</b> | <b>100.0%</b> | <b>\$ 940,488</b>  | <b>100.0%</b> | <b>8.6%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

*Validus Re.* Validus Re net premiums earned for the nine months ended September 30, 2009 were \$537.9 million compared to \$489.2 million for the nine months ended September 30, 2008, an increase of \$48.7 million or 10.0%. The increase in net premiums earned was due primarily to \$31.8 million of property net premiums earned resulting from the consolidation of IPCRe.

| (Dollars in thousands) | Net premiums earned |               |                    |               | %<br>Change  |
|------------------------|---------------------|---------------|--------------------|---------------|--------------|
|                        | Nine months ended   |               | Nine months ended  |               |              |
|                        | September 30, 2009  |               | September 30, 2008 | (a)           |              |
| Property               | \$ 374,199          | 69.6%         | \$ 361,027         | 73.8%         | 3.6%         |
| Marine                 | 94,384              | 17.5%         | 75,109             | 15.4%         | 25.7%        |
| Specialty              | 69,329              | 12.9%         | 53,027             | 10.8%         | 30.7%        |
| <b>Total</b>           | <b>\$ 537,912</b>   | <b>100.0%</b> | <b>\$ 489,163</b>  | <b>100.0%</b> | <b>10.0%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently,

2008 data does  
not include IPC  
financial results.

The increase in net premiums earned is due primarily to increased gross premiums written of \$90.5 million, or 14.1%, from \$643.9 million for the nine months ended September 30, 2008 to \$734.4 million for the nine months ended September 30, 2009. Contracts written on a risks-attaching basis are generally earned over twenty four months and therefore have less immediate effect on premiums earned than contracts written on a losses-occurring basis which are generally earned on a twelve month basis.

*Talbot.* Talbot net premiums earned for the nine months ended September 30, 2009 were \$483.8 million compared to \$451.3 million for the nine months ended September 30, 2008, an increase of \$32.4 million or 7.2%.

| (Dollars in thousands) | Net premiums earned |               |                    |               |             |
|------------------------|---------------------|---------------|--------------------|---------------|-------------|
|                        | Nine months ended   |               | Nine months ended  |               | %<br>Change |
|                        | September 30, 2009  |               | September 30, 2008 |               |             |
| Property               | \$ 97,680           | 20.2%         | \$ 91,628          | 20.3%         | 6.6%        |
| Marine                 | 208,983             | 43.2%         | 199,001            | 44.1%         | 5.0%        |
| Specialty              | 177,101             | 36.6%         | 160,696            | 35.6%         | 10.2%       |
| <b>Total</b>           | <b>\$ 483,764</b>   | <b>100.0%</b> | <b>\$ 451,325</b>  | <b>100.0%</b> | <b>7.2%</b> |

The increase in net premiums earned is due primarily to the increased levels of net premiums written across all major business lines over the twelve months ended September 30, 2009, as compared with the twelve months ended September 30, 2008.

#### Losses and Loss Expenses

Losses and loss expenses for the nine months ended September 30, 2009 were \$390.7 million compared to \$580.6 million for the nine months ended September 30, 2008, a decrease of \$189.8 million or 32.7%. The loss ratios, defined as losses and loss expenses divided by net premiums earned, for the nine months ended September 30, 2009 and 2008 were 38.2% and 61.7%, respectively. Details of loss ratios by line of business are provided below.

**Table of Contents**

|                  | <b>Nine months<br/>ended<br/>September 30,<br/>2009</b> | <b>Nine months<br/>ended<br/>September 30,<br/>2008 (a)</b> | <b>Percentage<br/>point<br/>change</b> |
|------------------|---|---|--|
| Property         | 17.6%   | 68.4%   | (50.8)                                 |
| Marine           | 62.1%   | 75.0%   | (12.9)                                 |
| Specialty        | 48.5%   | 30.5%   | 18.0                                   |
| <b>All lines</b> | <b>38.2%</b>  | <b>61.7%</b>  | <b>(23.5)</b>                          |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

The following table sets forth a reconciliation of gross and net reserves for losses and loss expenses by segment for the nine months ended September 30, 2009:

| <b>(Dollars in thousands)</b>            | <b>Nine months ended September 30, 2009</b> |               |                     |              |
|--|---|---------------|---------------------|--------------|
|  | <b>Validus</b>                              | <b>Talbot</b> | <b>Eliminations</b> | <b>Total</b> |
| Gross reserves at period beginning       | \$ 535,888                                  | \$ 790,199    | \$ (20,784)         | \$ 1,305,303 |
| Losses recoverable at period beginning   | (84,523)                                    | (145,057)     | 20,784              | (208,796)    |
| Net reserves at period beginning         | 451,365                                     | 645,142       |                     | 1,096,507    |
| Net reserves acquired in IPC acquisition | 304,957                                     |               |                     | 304,957      |
| Incurring losses- current year           | 166,663                                     | 277,403       |                     | 444,066      |
| Change in prior accident years           | (24,093)                                    | (29,237)      |                     | (53,330)     |
| Incurring losses                         | 142,570                                     | 248,166       |                     | 390,736      |
| Exchange rate effects                    | 4,967                                       | 18,859        |                     | 23,826       |
| Paid losses                              | (178,232)                                   | (185,152)     |                     | (363,384)    |
| Net reserves at period end               | 725,627                                     | 727,015       |                     | 1,452,642    |
| Losses recoverable                       | 57,608                                      | 143,064       | (28,571)            | 172,101      |
| Gross reserves at period end             | \$ 783,235                                  | \$ 870,079    | \$ (28,571)         | \$ 1,624,743 |

The amount of recorded reserves represents management's best estimate of expected losses and loss expenses on premiums earned. Favorable loss development on prior years totaled \$53.3 million. Favorable loss reserve

development benefitted the Company's loss ratio by 5.2 percentage points for the nine months ended September 30, 2009. For the nine months ended September 30, 2009, the Company incurred \$12.3 million and \$11.0 million of losses attributable to windstorm Klaus and a commercial flight loss, respectively, which represent 1.2 and 1.1 percentage points of the loss ratio, respectively. For the nine months ended September 30, 2008, the Company incurred \$183.4 million, \$22.1 million and \$11.7 million of losses attributable to Hurricane Ike, Hurricane Gustav and certain U.S. storm and flood loss events, which represent 19.5, 2.4 and 1.2 percentage points of the loss ratio, respectively. In addition, Item 2 of the Company's Quarterly Report on Form 10-Q for the three months ended March 31, 2008 discloses \$41.5 million of losses attributable to separately identified losses, which, for the nine months ended September 30, 2008, represented 4.7 percentage points of the loss ratio.

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 of recent losses. The Company's actual ultimate net loss may vary materially from estimates.

At September 30, 2009 and 2008, 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 in Item 7, Management's Discussion and Analysis of Results of Operations and Financial Condition in the Company's Annual Report on Form 10-K for the year ended December 31, 2008. The Company did not make any significant changes in the assumptions or methodology used in its reserving process for the nine months ended September 30, 2009.

**Table of Contents**

| (Dollars in thousands) | As at September 30, 2009 |                   |  |
|------------------------|--------------------------|-------------------|--|
|                        | Gross case reserves      | Gross IBNR        | Total gross reserve for losses and loss expenses |
| Property               | \$ 393,729               | \$ 322,935        | \$ 716,664                                       |
| Marine                 | 354,584                  | 249,262           | 603,846  |
| Specialty              | 129,543                  | 174,690           | 304,233  |
| <b>Total</b>           | <b>\$ 877,856</b>        | <b>\$ 746,887</b> | <b>\$ 1,624,743</b>                              |

| (Dollars in thousands) | As at September 30, 2009 |                   |  |
|------------------------|--------------------------|-------------------|--|
|                        | Net case reserves        | Net IBNR          | Total net reserve for losses and loss expenses |
| Property               | \$ 390,524               | \$ 304,084        | \$ 694,608                                     |
| Marine                 | 261,032                  | 231,781           | 492,813  |
| Specialty              | 115,231                  | 149,990           | 265,221  |
| <b>Total</b>           | <b>\$ 766,787</b>        | <b>\$ 685,855</b> | <b>\$ 1,452,642</b>                            |

*Validus Re.* Validus Re losses and loss expenses for the nine months ended September 30, 2009 were \$142.6 million compared to \$324.7 million for the nine months ended September 30, 2008, a decrease of \$182.1 million or 56.1%. Validus Re net paid losses for the nine months ended September 30, 2009 were \$178.2 million compared to \$81.5 million for the nine months ended September 30, 2008, an increase of \$96.7 million, or 118.7%, primarily as a result of losses paid on Hurricane Ike. The loss ratio, defined as losses and loss expenses divided by net premiums earned, was 26.5% and 66.4% for the nine months ended September 30, 2009 and 2008, respectively. For the nine months ended September 30, 2009, Validus Re incurred \$11.9 million and \$2.7 million of losses attributable to windstorm Klaus and a commercial flight loss, respectively, which represent 2.2 and 0.5 percentage points of the loss ratio, respectively. For the nine months ended September 30, 2008, Validus Re incurred \$157.2 million, \$15.4 million and \$10.2 million of losses attributable to Hurricane Ike, Hurricane Gustav and certain U.S. storm and flood loss events, which represented 32.1, 3.2 and 2.1 percentage points of the loss ratio, respectively. In addition, Item 2 of the Company's Quarterly Report on Form 10-Q for the three months ended March 31, 2008 discloses \$30.2 million of Validus Re losses attributable to separately identified losses, which, for the nine months ended September 30, 2008, represented 6.8 percentage points of the loss ratio.

|   | 2009    | 2008 (a) | Percentage point change |
|---|---------|----------|-------------------------|
| Property current year                   | 25.4%   | 67.9%    | (42.5)                  |
| Property change in prior accident years | (11.0)% | (3.9)%   | (7.1)                   |
| Property loss ratio                     | 14.4%   | 64.0%    | (49.6)                  |
| Marine current year                     | 47.8%   | 93.1%    | (45.3)                  |



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|                  |                                |        |        |        |
|------------------|--------------------------------|--------|--------|--------|
| Marine           | change in prior accident years | 23.2%  | 9.7%   | 13.5   |
| Marine           | loss ratio                     | 71.0%  | 102.8% | (31.8) |
| Specialty        | current year                   | 38.3%  | 35.0%  | 3.3    |
| Specialty        | change in prior accident years | (7.1)% | (3.8)% | (3.3)  |
| Specialty        | loss ratio                     | 31.2%  | 31.2%  |        |
| All lines        | current year                   | 31.0%  | 68.2%  | (37.2) |
| All lines        | change in prior accident years | (4.5)% | (1.8)% | (2.7)  |
| <b>All lines</b> | <b>loss ratio</b>              | 26.5%  | 66.4%  | (39.9) |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

**Table of Contents**

For the nine months ended September 30, 2009, the property lines include \$94.9 million related to current year losses and \$41.0 million of favorable development relating to prior accident years. The favorable development is attributable to the reclassification of losses from onshore energy exposures during the 2007 California wildfires to the marine line and reduced loss estimates for Hurricane Ike, the June 2008 Midwest flood event and October 2007 Peruvian mining loss, as well as lower than expected claim development elsewhere. For the nine months ended September 30, 2009, Validus Re's property lines incurred \$11.9 million of losses attributable to windstorm Klaus, which represented 3.2 percentage points of the loss ratio. For the nine months ended September 30, 2008, Validus Re's property lines incurred \$120.3 million, \$13.9 million and \$10.2 million of losses attributable to Hurricane Ike, Hurricane Gustav and certain U.S. storm and flood loss events which represented 33.3, 3.9 and 2.8 percentage points of the loss ratio, respectively. In addition, Item 2 of the Company's Quarterly Report on Form 10-Q for the three months ended March 31, 2008 discloses \$30.2 million of Validus Re's property lines losses attributable to separately identified losses, which, for the nine months ended September 30, 2008, represented 9.2 percentage points of the loss ratio. Validus Re property line loss ratios, excluding prior year development and loss events identified above, for the nine months ended September 30, 2009 and 2008 were 22.2% and 18.7%, respectively.

For the nine months ended September 30, 2009, the marine lines include \$45.1 million related to current year losses and \$21.9 million of adverse development relating to prior accident years due primarily to the reclassification of losses from onshore energy exposures during the 2007 California wildfires from the property line and increased loss estimates for Hurricanes Ike and Gustav. For the nine months ended September 30, 2008, Validus Re marine lines incurred \$36.8 million and \$1.5 million of losses attributable to Hurricanes Ike and Gustav, which represented 49.0 and 2.0 percentage points of the loss ratio, respectively. Validus Re marine line loss ratios, excluding prior year development and loss events identified above, for the nine months ended September 30, 2009 and 2008 were 47.8% and 42.1%, respectively.

For the nine months ended September 30, 2009, the specialty lines include \$26.6 million related to current year losses and \$4.9 million of favorable development relating to prior accident years. For the nine months ended September 30, 2008, Validus Re specialty lines incurred \$0.1 million of losses attributable to Hurricane Ike, which represented 0.2 percentage points of the loss ratio. Validus Re specialty lines loss ratios, excluding prior year development and loss events identified above, for the nine months ended September 30, 2009 and 2008 were 34.4% and 34.8%, respectively.

*Talbot.* Talbot losses and loss expenses for the nine months ended September 30, 2009 were \$248.2 million compared to \$255.9 million for the nine months ended September 30, 2008, a decrease of \$7.7 million, or 3.0%. The loss ratio was 51.3% and 56.7% for the nine months ended September 30, 2009 and 2008, respectively. Favorable loss development on prior years totaled \$29.2 million, primarily on the property lines of business. Favorable loss reserve development benefitted the segment loss ratio by 6.0 percentage points for the nine months ended September 30, 2009. For the nine months ended September 30, 2009, Talbot incurred \$8.3 million of losses attributable to a commercial flight loss, which represented 1.7 percentage points of the segment loss ratio. For the nine months ended September 30, 2008, Talbot incurred \$26.2 million and \$6.7 million of losses attributable to Hurricanes Ike and Gustav, which represented 5.8 and 1.5 percentage points of the segment loss ratio, respectively. In addition, Item 2 of the Company's Quarterly Report on Form 10-Q for the three months ended March 31, 2008 discloses \$11.3 million of losses attributable to separately identified losses, which, for the nine months ended September 30, 2008, represented 2.5 percentage points of the segment loss ratio. Details of loss ratios by line of business and calendar period are provided below.

**Table of Contents**

|                  |                                | <b>Nine months ended September<br/>30,</b> |                 | <b>Percentage<br/>point<br/>change</b> |
|------------------|--------------------------------|--|-----------------|--|
|                  |                                | <b>2009</b>                                | <b>2008 (a)</b> |  |
| Property         | current year                   | 49.6%                                      | 93.3%           | (43.7)                                 |
| Property         | change in prior accident years | (20.0)%                                    | (7.2)%          | (12.8)                                 |
| Property         | loss ratio                     | 29.6%                                      | 86.1%           | (56.5)                                 |
| Marine           | current year                   | 59.9%                                      | 68.0%           | (8.1)                                  |
| Marine           | change in prior accident years | (1.8)%                                     | (3.5)%          | 1.7                                    |
| Marine           | loss ratio                     | 58.1%                                      | 64.5%           | (6.4)                                  |
| Specialty        | current year                   | 58.6%                                      | 47.4%           | 11.2                                   |
| Specialty        | change in prior accident years | (3.4)%                                     | (17.1)%         | 13.7                                   |
| Specialty        | loss ratio                     | 55.2%                                      | 30.3%           | 24.9                                   |
| All lines        | current year                   | 57.3%                                      | 65.8%           | (8.5)                                  |
| All lines        | change in prior accident years | (6.0)%                                     | (9.1)%          | 3.1                                    |
| <b>All lines</b> | <b>loss ratio</b>              | 51.3%                                      | 56.7%           | (5.4)                                  |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

For the nine months ended September 30, 2009, the property lines include \$48.5 million related to current year losses and \$19.5 million of favorable loss development relating to prior accident years. This favorable development is primarily attributable to lower than expected claims development together with \$2.3 million of favorable development relating to Hurricane Katrina. For the nine months ended September 30, 2008, the property lines incurred \$15.2 million and \$3.7 million of losses attributable to Hurricanes Ike and Gustav, which represented 16.5 and 4.0 percentage points of the loss ratio, respectively. In addition, Item 2 of the Company's Quarterly Report on Form 10-Q for the three months ended March 31, 2008 discloses \$11.3 million of losses attributable to separately identified losses, which, for the nine months ended September 30, 2008, represented 12.3 percentage points of Talbot's property lines loss ratio. Talbot property line loss ratio, excluding prior year development and the loss events identified above, for the nine months ended September 30, 2009 and 2008 were 49.3% and 58.9%, respectively.

For the nine months ended September 30, 2009, the marine lines include \$125.1 million related to current year losses and \$3.7 million of favorable development relating to prior accident years. For the nine months ended

September 30, 2008, the marine lines incurred \$10.5 million and \$2.5 million of losses attributable to Hurricanes Ike and Gustav, which represented 5.3 and 1.3 percentage points of the loss ratio, respectively. Talbot marine line loss ratios, excluding prior year development and the loss events identified above, for the nine months ended September 30, 2009 and 2008 were 59.9% and 61.4%, respectively.

For the nine months ended September 30, 2009, the specialty lines include \$103.8 million relating to current year losses and \$6.0 million due to favorable development on prior accident years. For the nine months ended September 30, 2009, Talbot incurred \$8.3 million of losses attributable to a commercial flight loss, which represents 4.7 percentage points of the loss ratio. For the nine months ended September 30, 2008, the specialty lines incurred \$0.5 million and \$0.5 million of losses attributable to Hurricanes Ike and Gustav, which represented 0.3 and 0.3 percentage points of the loss ratio, respectively. Talbot specialty lines loss ratios, excluding prior year development and the loss events identified above, for the nine months ended September 30, 2009 and 2008 were 53.9% and 46.8%, respectively.

**Policy Acquisition Costs**

Policy acquisition costs for the nine months ended September 30, 2009 were \$190.1 million compared to \$173.5 million for the nine months ended September 30, 2008, an increase of \$16.6 million or 9.6%. Policy acquisition costs as a percent of net premiums earned for the nine months ended September 30, 2009 and 2008 were 18.6% and 18.5%, respectively.

**Table of Contents**

| (Dollars in thousands) | Policy acquisition costs |               |                    |               |             |
|------------------------|--------------------------|---------------|--------------------|---------------|-------------|
|                        | Nine months ended        |               | Nine months ended  |               | %<br>Change |
|                        | September 30, 2009       |               | September 30, 2008 | (a)           |             |
| Property               | \$ 73,219                | 38.5%         | \$ 71,147          | 41.0%         | 2.9%        |
| Marine                 | 64,515                   | 33.9%         | 55,941             | 32.2%         | 15.3%       |
| Specialty              | 52,391                   | 27.6%         | 46,457             | 26.8%         | 12.8%       |
| <b>Total</b>           | <b>\$ 190,125</b>        | <b>100.0%</b> | <b>\$ 173,545</b>  | <b>100.0%</b> | <b>9.6%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

*Validus Re.* Validus Re policy acquisition costs for the nine months ended September 30, 2009 were \$90.3 million compared to \$72.2 million for the nine months ended September 30, 2008, an increase of \$18.1 million or 25.1%.

| (Dollars in thousands) | Policy acquisition costs |               |                    |               |              |
|------------------------|--------------------------|---------------|--------------------|---------------|--------------|
|                        | Nine months ended        |               | Nine months ended  |               | %<br>Change  |
|                        | September 30, 2009       |               | September 30, 2008 | (a)           |              |
| Property               | \$ 61,126                | 67.7%         | \$ 54,437          | 75.4%         | 12.3%        |
| Marine                 | 20,054                   | 22.2%         | 10,496             | 14.5%         | 91.1%        |
| Specialty              | 9,166                    | 10.1%         | 7,299              | 10.1%         | 25.6%        |
| <b>Total</b>           | <b>\$ 90,346</b>         | <b>100.0%</b> | <b>\$ 72,232</b>   | <b>100.0%</b> | <b>25.1%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC

financial results.

Policy acquisition costs include brokerage, commission and excise tax and are generally driven by contract terms and are normally a set percentage of premiums and are also net of ceding commission income on retrocessions. Policy acquisition costs as a percent of net premiums earned for the nine months ended September 30, 2009 and 2008 were 16.8% and 14.8%, respectively. The policy acquisition ratio increased largely due to a 7.2 percentage point increase on the marine policy acquisition ratio. The increase in the marine policy acquisition ratio was due to an increased portion of gross premiums written being earned on proportional contracts, which generally experience higher acquisition costs.

*Talbot.* Talbot policy acquisition costs for the nine months ended September 30, 2009 were \$102.4 million compared to \$101.5 million for the nine months ended September 30, 2008, an increase of \$0.9 million or 0.9%.

| (Dollars in thousands) | Policy acquisition costs |               |                    |               |             |
|------------------------|--------------------------|---------------|--------------------|---------------|-------------|
|                        | Nine months ended        |               | Nine months ended  |               | %<br>Change |
|                        | September 30, 2009       |               | September 30, 2008 |               |             |
| Property               | \$ 14,692                | 14.4%         | \$ 16,855          | 16.6%         | (12.8)%     |
| Marine                 | 44,461                   | 43.4%         | 45,445             | 44.8%         | (2.2)%      |
| Specialty              | 43,225                   | 42.2%         | 39,158             | 38.6%         | 10.4%       |
| <b>Total</b>           | <b>\$ 102,378</b>        | <b>100.0%</b> | <b>\$ 101,458</b>  | <b>100.0%</b> | <b>0.9%</b> |

Policy acquisition costs as a percent of net premiums earned were 21.2% and 22.5%, respectively, for the nine months ended September 30, 2009 and 2008.

#### General and Administrative Expenses

General and administrative expenses for the nine months ended September 30, 2009 were \$125.3 million compared to \$101.1 million for the nine months ended September 30, 2008, an increase of \$24.2 million or 23.9%. The increase was primarily a result of increased Validus Re expenses partially offset by decreases in the Corporate segment.

**Table of Contents**

| (Dollars in thousands)   | General and administrative expenses |               |                    |               |              |
|--------------------------|-------------------------------------|---------------|--------------------|---------------|--------------|
|                          | Nine months ended                   |               | Nine months ended  |               | % Change     |
|                          | September 30, 2009                  |               | September 30, 2008 | (a)           |              |
| Validus Re               | \$ 45,928                           | 36.7%         | \$ 27,306          | 27.0%         | 68.2%        |
| Talbot                   | 65,565                              | 52.3%         | 58,561             | 57.9%         | 12.0%        |
| Corporate & Eliminations | 13,822                              | 11.0%         | 15,272             | 15.1%         | (9.5)%       |
| <b>Total</b>             | <b>\$ 125,315</b>                   | <b>100.0%</b> | <b>\$ 101,139</b>  | <b>100.0%</b> | <b>23.9%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

General and administrative expense ratios for the nine months ended September 30, 2009 and 2008 were 14.1% and 12.9%, respectively. General and administrative expense ratio is the sum of general and administrative expenses and share compensation expense divided by net premiums earned.

| (Dollars in thousands)     | Nine months ended  |                                      | Nine months ended      |                                      |
|----------------------------|--------------------|--------------------------------------|------------------------|--------------------------------------|
|                            | September 30, 2009 |                                      | September 30, 2008 (a) |                                      |
|                            | Expenses           | Expenses as % of Net Earned Premiums | Expenses               | Expenses as % of Net Earned Premiums |
| General and Administrative | \$ 125,315         | 12.3%                                | \$ 101,139             | 10.8%                                |
| Share Compensation         | 18,848             | 1.8%                                 | 19,818                 | 2.1%                                 |
| <b>Total</b>               | <b>\$ 144,163</b>  | <b>14.1%</b>                         | <b>\$ 120,957</b>      | <b>12.9%</b>                         |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently,

2008 data does  
not include IPC  
financial results.

General and administrative expenses of \$125.3 million in the nine months ended September 30, 2009 represents 12.3 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 nine months ended September 30, 2009 were \$45.9 million compared to \$27.3 million for the nine months ended September 30, 2008, an increase of \$18.6 million or 68.2%. General and administrative expenses have increased primarily as a result of the increase in staff to 121 at September 30, 2009 from 86 at September 30, 2008. General and administrative expenses are generally comprised of salaries and benefits, professional fees, rent and office expenses. Validus Re's general and administrative expenses as a percent of net premiums earned for the nine months ended September 30, 2009 and 2008 were 8.5% and 5.6%, respectively.

*Talbot.* Talbot general and administrative expenses for the nine months ended September 30, 2009 were \$65.6 million compared to \$58.6 million for the nine months ended September 30, 2008, an increase of \$7.0 million or 12.0%. General and administrative expenses have increased primarily as a result of the increase in staff to 213 at September 30, 2009 from 175 at September 30, 2008 and expenses related to the new onshore energy and aviation underwriting teams. Talbot's general and administrative expenses as a percent of net premiums earned for the nine months ended September 30, 2009 and 2008 were 13.6% and 13.0%, respectively.

*Corporate & Eliminations.* Corporate general and administrative expenses for the nine months ended September 30, 2009 were \$13.8 million compared to \$15.3 million for the nine months ended September 30, 2008, a decrease of \$1.5 million or 9.5%. Corporate general and administrative expenses are comprised of executive and board expenses, internal and external audit expenses and other cost relating to the Company as a whole.

#### **Share Compensation Expense**

Share compensation expense for the nine months ended September 30, 2009 was \$18.8 million compared to \$19.8 million for the nine months ended September 30, 2008, a decrease of \$1.0 million or 4.9%. 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.



**Table of Contents**

| (Dollars in thousands)   | Share compensation expenses             |               |  |               | %<br>Change   |
|--------------------------|---|---------------|--|---------------|---------------|
|                          | Nine months ended<br>September 30, 2009 |               | Nine months ended<br>September 30, 2008<br>(a) |               |               |
| Validus Re               | \$ 4,986                                | 26.4%         | \$ 4,632                                       | 23.4%         | 7.6%          |
| Talbot                   | 5,804                                   | 30.8%         | 3,266  | 16.5%         | 77.7%         |
| Corporate & Eliminations | 8,058                                   | 42.8%         | 11,920   | 60.1%         | (32.4)%       |
| <b>Total</b>             | <b>\$ 18,848</b>                        | <b>100.0%</b> | <b>\$ 19,818</b>                               | <b>100.0%</b> | <b>(4.9)%</b> |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

Share compensation expense of \$18.8 million in the nine months ended September 30, 2009 represents 1.8 percentage points of the general and administrative expense ratio.

*Validus Re.* Validus Re share compensation expense for the nine months ended September 30, 2009 was \$5.0 million compared to \$4.6 million for the nine months ended September 30, 2008, an increase of \$0.4 million or 7.6%. The increase was due to the impact of grants made during 2008. Share compensation expense as a percent of net premiums earned for the nine months ended September 30, 2009 and 2008 were 0.9% and 0.9%, respectively.

*Talbot.* Talbot share compensation expense for the nine months ended September 30, 2009 was \$5.8 million compared to \$3.3 million for the nine months ended September 30, 2008. The increase was due to additional grants for the nine months ended September 30, 2009 as a result of increased staff. Share compensation expense as a percent of net premiums earned for the nine months ended September 30, 2009 and 2008 were 1.2% and 0.7%, respectively.

*Corporate & Eliminations.* Corporate share compensation expense for the nine months ended September 30, 2009 was \$8.1 million compared to \$11.9 million for the nine months ended September 30, 2008, a decrease of \$3.9 million or 32.4%. This decrease was due primarily to several share award issuances with vesting periods greater than one year that vested during the year ended December 31, 2008 and therefore had no further amortization expense during the nine months ended September 30, 2009.

**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 acquisition costs combined with general and administrative expenses by net premiums earned. The following table presents the losses and loss expenses ratio, policy acquisition cost ratio, general and administrative expense ratio, expense ratio and combined ratio for the nine months ended September 30, 2009 and 2008.

**Percentage**

|  | <b>Nine months<br/>ended<br/>September 30,<br/>2009</b> | <b>Nine months<br/>ended<br/>September 30,<br/>2008 (a)</b> | <b>point<br/>change</b> |
|--|---|---|-------------------------|
| Losses and loss expenses ratio               | 38.2%   | 61.7%   | (23.5)                  |
| Policy acquisition cost ratio                | 18.6%   | 18.5%   | 0.1                     |
| General and administrative expense ratio (1) | 14.1%   | 12.9%   | 1.2                     |
| Expense ratio                                | 32.7%   | 31.4%   | 1.3                     |
| <b>Combined ratio</b>                        | <b>70.9%</b>  | <b>93.1%</b>  | <b>(22.2)</b>           |

(1) Includes general and administrative expense and share compensation expense

|  | <b>Nine months<br/>ended<br/>September 30,<br/>2009</b> | <b>Nine months<br/>ended<br/>September 30,<br/>2008 (a)</b> | <b>Percentage<br/>point<br/>change</b> |
|--|---|---|--|
| <i>Validus Re</i>                        |   |   |  |
| Losses and loss expenses ratio           | 26.5%   | 66.4%   | (39.9)                                 |
| Policy acquisition cost ratio            | 16.8%   | 14.8%   | 2.0                                    |
| General and administrative expense ratio | 9.5%  | 6.5%  | 3.0                                    |
| Expense ratio                            | 26.3%   | 21.3%   | 5.0                                    |
| <b>Combined ratio</b>                    | <b>52.8%</b>  | <b>87.7%</b>  | <b>(34.9)</b>                          |

**Table of Contents**

|  | <b>Nine months<br/>ended<br/>September 30,<br/>2009</b> | <b>Nine months<br/>ended<br/>September 30,<br/>2008</b> | <b>Percentage<br/>point<br/>change</b> |
|--|---|---|--|
| <i>Talbot</i>                            |   |   |  |
| Losses and loss expenses ratio           | 51.3%   | 56.7%   | (5.4)                                  |
| Policy acquisition cost ratio            | 21.2%   | 22.5%   | (1.3)                                  |
| General and administrative expense ratio | 14.8%   | 13.7%   | 1.1                                    |
| Expense ratio                            | 36.0%   | 36.2%   | (0.2)                                  |
| <b>Combined ratio</b>                    | <b>87.3%</b>  | <b>92.9%</b>  | <b>(5.6)</b>                           |

- (a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

**Underwriting Income**

Underwriting income for the nine months ended September 30, 2009 was \$296.7 million compared to \$65.4 million for the nine months ended September 30, 2008, an increase of \$231.2 million or 353.5%.

|                               | <b>Nine months ended September 30,</b> |                               |                  |                               | <b>%<br/>Change</b> |
|-------------------------------|--|-------------------------------|------------------|-------------------------------|---------------------|
|                               | <b>2009</b>                            | <b>% of<br/>Sub<br/>total</b> | <b>2008 (a)</b>  | <b>% of<br/>Sub<br/>total</b> |                     |
| <b>(Dollars in thousands)</b> |  |                               |                  |                               |                     |
| Validus Re                    | \$ 254,082                             | 80.4%                         | \$ 60,320        | 65.2%                         | 321.2%              |
| Talbot                        | 61,851                                 | 19.6%                         | 32,135           | 34.8%                         | 92.5%               |
| Sub total                     | 315,933                                | 100.0%                        | 92,455           | 100.0%                        | 241.7%              |
| Corporate & Eliminations      | (19,281)                               |                               | (27,047)         |                               | 28.7%               |
| <b>Total</b>                  | <b>\$ 296,652</b>                      |                               | <b>\$ 65,408</b> |                               | <b>353.5%</b>       |

- (a) The results of operations for IPC are consolidated

only from the  
September 2009  
date of  
acquisition.  
Consequently,  
2008 data does  
not include IPC  
financial results.

The underwriting results of an insurance or reinsurance company are also often measured by reference to its underwriting income, which is a non-GAAP measure as previously defined. 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 Operations and Comprehensive Income line items, as described below.

| <b>(Dollars in thousands)</b>                | <b>Nine months<br/>ended<br/>September 30,<br/>2009</b> | <b>Nine months<br/>ended<br/>September 30,<br/>2008 (a)</b> |
|--|---|---|
| <b>Underwriting income (loss)</b>            | \$ 296,652  | \$ 65,408   |
| Net investment income                        | 83,267  | 108,857   |
| Other income                                 | 2,875   | 3,666   |
| Finance expenses                             | (29,732)  | (48,796)  |
| Foreign exchange (losses) gains              | (1,012)   | (35,843)  |
| Gain on bargain purchase, net of expenses    | 287,099   |   |
| Realized gain on repurchase of debentures    |   | 8,752   |
| Net realized gains (losses) on investments   | (20,642)  | (8,348)   |
| Net unrealized gains (losses) on investments | 109,839   | (72,608)  |
| <b>Net income before taxes</b>               | <b>\$ 728,346</b>                                       | <b>\$ 21,088</b>  |

(a) The results of  
operations for  
IPC are  
consolidated  
only from the  
September 2009  
date of  
acquisition.  
Consequently,  
2008 data does  
not include IPC  
financial results.

**Table of Contents**

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 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 bonus component of 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 nine months ended September 30, 2009 was \$83.3 million compared to \$108.9 million for the nine months ended September 30, 2008, a decrease of \$25.6 million or 23.5%. Net investment income decreased as a result of reduced market yields and higher quarterly average cash balances. 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 nine months ended September 30, 2009 and 2008 are as presented below.

| <b>(Dollars in thousands)</b>               | <b>Nine months<br/>ended<br/>September 30,<br/>2009</b> | <b>Nine months<br/>ended<br/>September 30,<br/>2008 (a)</b> | <b>%<br/>Change</b> |
|---|---|---|---------------------|
| Fixed maturities and short-term investments | \$ 82,341   | \$ 98,654   | (16.5)%             |
| Securities lending income                   | 2,623   | 11,524  | (77.2)%             |
| Cash and cash equivalents                   | 683   | 1,150   | (40.6)%             |
| Total investment income                     | 85,647  | 111,328   | (23.1)%             |

|                              |    |         |    |         |         |
|------------------------------|----|---------|----|---------|---------|
| Investment expenses          |    | (2,380) |    | (2,471) | 3.7%    |
| <b>Net investment income</b> | \$ | 83,267  | \$ | 108,857 | (23.5)% |

(a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

**Table of Contents**

Investment management fees incurred relate to BlackRock Financial Management, Inc. ( BlackRock ) and Goldman Sachs Asset Management L.P. and its affiliates ( GSAM ). Each of Merrill Lynch & Co, Inc. ( Merrill Lynch ), a wholly owned subsidiary of Bank of America Corp., and Goldman Sachs are major shareholders of the Company. BlackRock is considered a related party due to its merger in February 2006 with Merrill Lynch Investment Managers. Investment management fees earned by BlackRock for the nine months ended September 30, 2009 and 2008 were \$1.6 million and \$1.2 million, respectively. Investment management fees earned by GSAM for the nine months ended September 30, 2009 and 2008 were \$1.1 million and \$1.0 million, respectively. Management believes that the fees charged were consistent with those that would have been charged in arm s-length transactions with unrelated third parties.

Annualized effective investment yield is based on the weighted average investments held calculated on a simple period average and excludes net unrealized gains (losses), foreign exchange gains (losses) on investments and the foreign exchange effect of insurance balances. The Company s annualized effective investment yield was 2.78% and 4.52% for the nine months ended September 30, 2009 and 2008, respectively, and the average duration at September 30, 2009 was 2.2 years (December 31, 2008 1.8 years).

**Finance Expenses**

Finance expenses for the nine months ended September 30, 2009 were \$29.7 million compared to \$48.8 million for the nine months ended September 30, 2008, a decrease of \$19.1 million or 39.1%. The decrease was primarily a result of an \$18.2 million decrease on Talbot third party FAL facility.

Finance expenses also include the amortization of debt offering costs and discounts and fees related to our credit facilities.

| (Dollars in thousands)                           | Nine months ended<br>September 30, |                  | %<br>Change    |
|--|------------------------------------|------------------|----------------|
|  | 2009                               | 2008 (a)         |                |
| 9.069% Junior Subordinated Deferrable Debentures | \$ 10,765                          | \$ 10,765        | 0.0%           |
| 8.480% Junior Subordinated Deferrable Debentures | 10,044                             | 11,517           | (12.8)%        |
| Credit facilities                                | 1,235                              | 692              | 78.5%          |
| Talbot FAL facilities                            | 167                                | 169              | (1.2)%         |
| Talbot other interest                            |                                    | (81)             | NM             |
| Talbot third party FAL facility                  | 7,521                              | 25,734           | (70.8)%        |
| <b>Finance expenses</b>                          | <b>\$ 29,732</b>                   | <b>\$ 48,796</b> | <b>(39.1)%</b> |

NM: Not Meaningful

- (a) The results of operations for IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

Capital in Lloyd's entities, whether personal or corporate, is required to be set annually for the prospective year and held by Lloyd's in trust (Funds at Lloyd's or FAL). In underwriting years up to and including 2007, Talbot's FAL has been provided both by Talbot and by third parties, thereafter Talbot's FAL has been provided exclusively by the Company. Because the third party FAL providers remain on risk until each year of account that their support closes (normally after three years), Talbot must retain third party FAL even if a third party FAL provider has ceased to support the active underwriting year. This is achieved by placing such FAL in escrow outside Lloyd's. Thus the total FAL facility available to the Company is the total FAL for active and prior underwriting years, although the Company can only apply specific FAL against losses incurred by an underwriting year that such FAL is contracted to support.

For each year of account up to and including the 2007 year of account, between 30% and 40% of an amount equivalent to each underwriting year's profit is payable to Talbot third party FAL providers. However, some of these costs are fixed. There are no FAL finance charges related to the 2008 and 2009 years of account as there were no third party FAL providers in those periods.



**Table of Contents**

The FAL finance charges relate to total syndicate profit (underwriting income, investment income and realized and unrealized capital gains and losses). FAL finance charges and total syndicate profits are analyzed by underwriting year of account as follows:

| Underwriting Year of Account<br>(Dollars in thousands) | Nine months ended September 30, |                  |                        |                  |  |              |
|--|---------------------------------|------------------|------------------------|------------------|--|--------------|
|  | FAL Finance Charges             |                  | Total Syndicate Profit |                  | FAL Finance Charges as % of Total Syndicate Profit |              |
|  | 2009                            | 2008             | 2009                   | 2008             | 2009   | 2008 (1)     |
| 2006 (1)   | \$                              | \$ 14,288        | \$                     | \$ 40,080        | NM   | 35.6%        |
| 2007   | 7,521                           | 11,447           | 21,611                 | 35,614           | 34.8%  | 32.1%        |
| 2008   |                                 |                  | 38,797                 | (39,219)         | NM   | NM           |
| 2009   |                                 |                  | 13,052                 |                  | NM   | NM           |
| <b>Total</b>   | <b>\$ 7,521</b>                 | <b>\$ 25,735</b> | <b>\$ 73,460</b>       | <b>\$ 36,475</b> | <b>10.2%</b>                                       | <b>70.6%</b> |
| Percentage excluding years in deficit                  |                                 |                  |                        |                  | 10.2%  | 34.0%        |

(1) The earliest year of account includes the run-off of prior (closed) years of account.

NM: Not Meaningful

FAL finance charges are based on syndicate profit but include fixed elements. FAL finance charges for the nine months ended September 30, 2009 were \$7.5 million compared to \$25.7 million for the nine months ended September 30, 2008, a decrease of \$18.2 million. This decrease was due to the absence of FAL finance charges related to the 2006 year of account, which has now closed.

Total syndicate profit, as set out in the table below, is reconciled to the Talbot segment net income by the addition or subtraction of items noted below.

| (Dollars in thousands)                         | Nine months ended September 30, 2009 | Nine months ended September 30, 2008 |
|--|--------------------------------------|--------------------------------------|
| <b>Total syndicate profit</b>                  | \$ 73,460                            | \$ 36,475                            |
| FAL Finance expenses                           | (7,521)                              | (25,735)                             |
| Managing agent's fee (1)                       | 6,930                                | 7,130                                |
| Managing agent's profit commission (2)         | 8,320                                | 13,394                               |
| Investment income (3)                          | 13,001                               | 7,900                                |
| Other segment operating income (expenses), net | 1,513                                | (17,189)                             |
| Share compensation (expenses)                  | (5,804)                              | (3,253)                              |
| Intangible amortization (expenses)             | (3,121)                              | (3,121)                              |
| Tax benefit (expense)                          | 3,408                                | (4,914)                              |

|                                  |    |        |    |        |
|----------------------------------|----|--------|----|--------|
| <b>Talbot segment net income</b> | \$ | 90,186 | \$ | 10,687 |
|----------------------------------|----|--------|----|--------|

(1) 1.5% of syndicate capacity; corresponding syndicate expense reflected in total syndicate profit, above.

(2) 15.0% of syndicate profit; corresponding syndicate expense reflected in total syndicate profit, above.

(3) On FAL and on non-syndicate cash balances.

#### **Gain on Bargain Purchase, Net of Expenses**

On September 4, 2009, the Company acquired all of the outstanding shares of IPC from a group of institutional and other investors. Pursuant to the Amalgamation Agreement, the Company acquired all of IPC's outstanding common shares in exchange for the Company's common shares and cash. The purchase price paid by the Company

**Table of Contents**

was \$1,746.2 million for net assets acquired of \$2,076.9 million. The Company expensed as incurred \$43.6 of transaction expenses and \$21.7 million for amortization of intangibles related to the acquisition for the nine months ended September 30, 2009, resulting in a gain on bargain purchase of \$287.1 million for the nine months ended September 30, 2009. Transaction expenses are comprised of primarily legal, corporate advisory, IPC employee termination benefits and audit related services.

**Net Realized Gains (Losses) on Investments**

Net realized (losses) on investments for the nine months ended September 30, 2009 were (\$20.6) million compared to (losses) of (\$8.3) million for the nine months ended September 30, 2008. Net realized losses resulted primarily from the sale of \$98.6 million of CMBS with relatively long weighted average lives, resulting in realized losses of \$19.5 million, which resulted in a corresponding offset in net unrealized gains (losses). The decision to reduce the Company's exposure to CMBS was made in light of deteriorating fundamentals in the sector.

On August 28, 2009, the Company sold short equity index futures contracts with a goal of hedging IPC's mutual fund equity portfolio exposure. The contracts were closed when the equity positions were fully redeemed on September 9, 2009. The Company experienced a \$3.3 million realized investment loss as a result of the futures contracts.

**Net Unrealized Gains (Losses) on Investments**

Net unrealized gains on investments for the nine months ended September 30, 2009 were \$109.8 million compared to losses of (\$72.6) million for the nine months ended September 30, 2008. The net unrealized gains in the nine months ended September 30, 2009 resulted from improved market conditions for fixed income securities.

The net unrealized gains on investments for the nine months ended September 30, 2009 included a \$2.0 million unrealized gain on the fund of hedge funds purchased in the IPC Acquisition. The fund of hedge funds was included in other investments on the balance sheet as at September 30, 2009.

Net unrealized gains 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 statements, certain market conditions allow for fair value measurements that incorporate unobservable inputs where active market transaction based measurements are unavailable. Certain non-Agency RMBS securities were identified as trading in inactive markets. The change in fair value for the identified non-Agency RMBS securities was a \$0.9 million increase in net unrealized loss on investments for the nine months ended September 30, 2009. Further details are provided in the Investments section below.

**Other Income**

Other income for the nine months ended September 30, 2009 was \$2.9 million compared to \$3.7 million for the nine months ended September 30, 2008, a decrease of \$0.8 million or 21.6%.

**Foreign Exchange Gains (Losses)**

Foreign exchange (losses) for the nine months ended September 30, 2009 were (\$1.0) million compared to (losses) of (\$35.8) million for the nine months ended September 30, 2008, a decrease of \$34.8 million. The decrease in foreign exchange (losses) was due primarily to the increased value of assets denominated in foreign currencies relative to the U.S. dollar reporting currency for the nine months ended September 30, 2009, as compared to the nine months ended September 30, 2008. For the nine months ended September 30, 2009, Validus Re and Talbot recognized foreign exchange (losses) of (\$0.6) million and (\$0.4) million, respectively. For the nine months ended September 30, 2009, the Talbot segment foreign exchange (losses) were (\$0.4) million compared to (\$20.2) million for the nine months ended September 30, 2008, a decrease of \$19.8 million. The decrease in Talbot segment foreign exchange (losses) was due primarily to a \$15.5 million change in the recurring revaluation of net unearned premiums and deferred acquisition costs and a \$16.6 million gain on revaluation of foreign exchange to reporting currency, offset by an (\$8.0) million (loss) related to a prior year tax adjustment. The British pound sterling to U.S. Dollar exchange rates were 1.44 and 1.59 at December 31, 2008 and September 30, 2009, respectively. Certain premiums receivable and liabilities for losses incurred in currencies other than the U.S. dollar are exposed to the risk of changes in value resulting from fluctuations in foreign exchange rates and may affect financial results in the future.

**Table of Contents**

At September 30, 2009, Talbot's balance sheet includes net unearned premiums and deferred acquisition costs denominated in foreign currencies of approximately \$89.3 million and \$19.3 million, respectively. These balances consisted of British pounds sterling and Canadian dollars of \$63.3 million and \$6.7 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. During the nine months ended September 30, 2009, this translation process resulted in foreign exchange gains that will reverse in future periods as net unearned premiums and deferred acquisition costs are earned together with gains arising from the reversal of losses incurred in previous periods. Additional foreign exchange (losses) gains may be incurred on the translation of net unearned premiums and deferred acquisition costs arising from insurance and reinsurance premiums written in future periods.

**Tax Benefit (Expense)**

Tax benefit for the nine months ended September 30, 2009 was \$3.3 million compared to an (expense) of (\$5.0) million for the nine months ended September 30, 2008, a change of \$8.3 million. The tax benefit was due primarily to an \$8.9 million adjustment to the U.K. tax basis of net unearned premiums and deferred acquisition costs and \$2.5 million of U.K. tax credits on performance bonus and share compensation offset by (\$8.2) million of U.K. tax expenses on profit commissions and managing agency fees, within the Talbot segment.

**Other Non-GAAP Financial Measures**

In presenting the Company's results, management has included and discussed certain schedules containing net operating income (loss), underwriting income, annualized return on average equity and diluted book value per common share 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. The calculation of annualized return on average equity is discussed in the section above entitled Financial Measures. A reconciliation of underwriting income to net income, the most comparable U.S. GAAP financial measure, is presented above in the section entitled Underwriting Income. A reconciliation of diluted book value per share to book value per share, the most comparable U.S. GAAP financial measure, is presented below. Operating income is calculated based on net income (loss) excluding net realized gains (losses), net unrealized gains (losses) on investments, gains (losses) arising from translation of non-US\$ denominated balances and non-recurring items. A reconciliation of operating income to net income, the most comparable U.S. GAAP financial measure, is embedded in the table presenting results of operations for the three and nine months ended September 30, 2009 and 2008 in the section above entitled Results of Operations. Realized gains (losses) from the sale of investments are driven by the timing of the disposition of investments, not by our operating performance. Gains (losses) arising from translation of non-US\$ denominated balances are unrelated to our underlying business.

The following tables present reconciliations of diluted book value per share to book value per share, the most comparable U.S. GAAP financial measure, at September 30, 2009 and December 31, 2008.

|  | <b>As at September 30, 2009</b> |               |                           | <b>Book value<br/>per<br/>share</b> |
|--|---------------------------------|---------------|---------------------------|-------------------------------------|
|  | <b>Equity<br/>amount</b>        | <b>Shares</b> | <b>Exercise<br/>price</b> | <b>share</b>                        |
| <b>Book value per common share</b>         |                                 |               |                           |                                     |
| Total shareholders' equity                 | \$ 3,966,192                    | 131,107,196   |                           | \$ 30.25                            |
| <b>Diluted book value per common share</b> |                                 |               |                           |                                     |
| Total shareholders' equity                 | 3,966,192                       | 131,107,196   |                           |                                     |
| Assumed exercise of outstanding warrants   | 139,576                         | 7,952,138     | \$ 17.55                  |                                     |
|  | 68,368                          | 3,430,816     | \$ 19.93                  |                                     |

Assumed exercise of outstanding stock  
options

Unvested restricted shares 3,383,298

**Diluted book value per common share** \$ 4,174,136 145,873,448 \$ 28.61

87

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**Table of Contents**

|   | <b>As at December 31, 2008</b> |                   |                           | <b>Book value<br/>per<br/>share</b> |
|---|--------------------------------|-------------------|---------------------------|-------------------------------------|
|   | <b>Equity<br/>amount</b>       | <b>Shares</b>     | <b>Exercise<br/>price</b> |                                     |
| <b>Book value per common share</b>            |                                |                   |                           |                                     |
| Total shareholders' equity                    | \$ 1,938,734                   | 75,624,697        |                           | \$ 25.64                            |
| <b>Diluted book value per common share</b>    |                                |                   |                           |                                     |
| Total shareholders' equity                    | 1,938,734                      | 75,624,697        |                           |                                     |
| Assumed exercise of outstanding warrants      | 152,316                        | 8,680,149         | \$ 17.55                  |                                     |
| Assumed exercise of outstanding stock options | 51,043                         | 2,799,938         | \$ 18.23                  |                                     |
| Unvested restricted shares                    |                                | 2,986,619         |                           |                                     |
| <b>Diluted book value per common share</b>    | <b>\$ 2,142,093</b>            | <b>90,091,403</b> |                           | <b>\$ 23.78</b>                     |

**Financial Condition and Liquidity**

Validus Holdings, Ltd. is a holding company and conducts no operations of its own. The Company relies primarily on cash dividends and other permitted payments from Validus Re and Talbot to pay finance expenses and other holding company expenses. There are restrictions on the payment of dividends from Validus Re and Talbot to the Company. Please refer to Part II, Item 5, "Market for Registrants, Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities" in the Company's Annual Report on Form 10-K for the year ended December 31, 2008 for further discussion of the Company's dividend policy.

Three main sources provide cash flows for the Company: operating activities, investing activities and financing activities. Cash flow from operating activities is derived primarily from the net receipt of premiums less claims and expenses related to underwriting activities. Cash flow from investing activities is derived primarily from the receipt of net proceeds on the Company's total investment portfolio. Cash flow from financing activities is derived primarily from the issuance of common shares and debentures payable. The movement in net cash provided by operating activities, net cash (used in) provided by investing activities, net cash (used in) provided by financing activities and the effect of foreign currency rate changes on cash and cash equivalents for the nine months ended September 30, 2009 and 2008 is described in the following table.

| <b>(Dollars in thousands)</b>  | <b>Nine months ended September 30,</b> |                     |                     |
|--|--|---------------------|---------------------|
|  | <b>2009</b>                            | <b>2008 (a)</b>     | <b>%<br/>Change</b> |
| Net cash provided by operating activities                            | \$ 348,384                             | \$ 397,377          | (12.3)%             |
| Net cash used in investing activities                                | (361,838)                              | (391,857)           | 7.7%                |
| Net cash provided by (used in) financing activities                  | (57,361)                               | (90,513)            | 36.6%               |
| Effect of foreign currency rate changes on cash and cash equivalents | 14,755                                 | (24,338)            | (160.6)%            |
| <b>Net (decrease) increase in cash</b>                               | <b>\$ (56,060)</b>                     | <b>\$ (109,331)</b> | <b>(48.7)%</b>      |

(a) The results of operations for

IPC are consolidated only from the September 2009 date of acquisition. Consequently, 2008 data does not include IPC financial results.

During the nine months ended September 30, 2009, net cash provided by operating activities was driven primarily by net income of \$731.6 million, offset by non-cash bargain purchase gain of \$330.7 million and net unrealized gains on investments of \$109.9 million. Cash provided by operating activities, as compared to the nine months ended September 30, 2008, was affected by the relative movement in change in reserves for losses and loss expenses for the nine months ended September 30, 2009, due primarily to the settlement 2008 loss reserves. Net cash used in investing activities was driven primarily by the proceeds on sales of investments to finance the IPC acquisition and the investment of operating surpluses. Net cash provided by (used in) financing activities was driven primarily by aggregate quarterly dividend payments of \$50.9 million. Net cash provided by (used in) financing activities, as compared to the nine months ended September 30, 2008, was affected by the absence of a debenture repurchase during the nine months ended September 30, 2009.

**Table of Contents**

During the nine months ended September 30, 2008, net cash provided by operating activities was driven primarily by a \$370.0 million increase in reserve for losses and loss expense primarily due to Hurricanes Ike and Gustav, a \$134.8 million increase in premiums receivable, and a \$147.5 million increase in unearned premiums. Net cash used in investing activities was driven primarily by the investment of operating surpluses. Net cash provided by (used in) financing activities was driven primarily by a \$36.9 million debenture repurchase and aggregate quarterly dividend payments of \$50.6 million.

As at September 30, 2009, the Company's portfolio was composed of fixed income investments including; cash, short-term investments, agency securities and sovereign securities amounting to \$3,192.2 million or 55.9% of total cash and investments. Details of the Company's debt and financing arrangements at September 30, 2009 are provided below.

| <b>(Dollars in thousands)</b>                    | <b>Maturity Date /<br/>Term</b> | <b>In Use/<br/>Outstanding</b> |
|--|---------------------------------|--------------------------------|
| 9.069% Junior Subordinated Deferrable Debentures | June 15, 2036                   | \$ 150,000                     |
| 8.480% Junior Subordinated Deferrable Debentures | June 15, 2037                   | 154,300                        |
| \$200,000 unsecured letter of credit facility    | March 12, 2010                  |                                |
| \$500,000 secured letter of credit facility      | March 12, 2012                  | 269,231                        |
| \$250,000 IPC Syndicated facility                | April 13, 2011                  | 38,602                         |
| \$350,000 IPC Bi-Lateral facility                | April 14, 2010                  | 91,071                         |
| Talbot FAL facility                              | December 31,<br>2009            | 100,000                        |
| Talbot third party FAL facility                  | December 31,<br>2009            | 121,515                        |
| <b>Total</b>                                     |                                 | <b>\$ 924,719</b>              |

The capital and credit markets have been experiencing extreme volatility and disruption for more than one year. In some cases, the markets have exerted downward pressure on the availability of liquidity and credit capacity for certain issuers. However, management believes that liquidity is not a key constraint for the Company due to its highly liquid investment portfolio and the maturity dates of debt and facilities reflected in the table above. Management's belief is based on the following considerations:

The Talbot third party FAL facility represents cash, investments and undrawn letters of credit provided by various third parties for the 2007 year of account. These third party funds have been replaced by the Company effective January 1, 2008;

The Talbot FAL facility is a facility currently secured by assets of Validus Reinsurance, Ltd. and the Company could choose to provide FAL in the form of cash should the Talbot FAL facility not be renewed;

The \$200 million unsecured letter of credit facility is not utilized by the Company currently and has been used in the past only as part of the Talbot acquisition.

On September 4, 2009, pursuant to an Agreement and Plan of Amalgamation among IPC Holdings, Ltd., the Company and Validus Ltd. (a wholly owned subsidiary of the Company), the Company acquired all of the outstanding shares of IPC from a group of institutional and other investors. Each outstanding IPC common share (including any shares held by IPC shareholders that do not vote in favor of the amalgamation, but excluding shares owned by the Company), have been cancelled and converted into the right to receive 0.9727 common shares of Validus, \$7.50 in cash (less any applicable withholding tax and without interest) and cash in lieu of fractional shares upon closing of the acquisition. The IPC Acquisition resulted in the payment of \$420.8 million in cash to IPC shareholders.



**Table of Contents****Capital Resources**

Shareholders' equity at September 30, 2009 was \$3,966.2 million.

On November 4, 2009, the Company announced a quarterly cash dividend of \$0.20 per each common share and \$0.20 per common share equivalent, for which each outstanding warrant is then exercisable, payable on December 31, 2009 to holders of record on December 15, 2009. During 2009, the Company paid quarterly cash dividends of \$0.20 per each common share and \$0.20 per common share equivalent, for which each outstanding warrant is then exercisable, on March 31, June 30 and September 30 to holders of record on March 16, June 15 and August 20, 2009, respectively. The timing and amount of any future cash dividends, however, will be 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.

The Company may from time to time repurchase its securities, including common shares and Junior Subordinated Deferrable Debentures. Share repurchases may be made pursuant to a share repurchase program authorized by the Board of Directors on November 4, 2009 authorizing the Company to repurchase up to \$400.0 million of its common shares. The Company expects the purchases 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. The repurchase program may be modified, extended or terminated by the Board at any time.

On August 7, 2008, the Company filed a shelf registration statement on Form S-3 (No. 333-152856) with the U.S. Securities Exchange Committee in which we may offer from time to time common shares, preference shares, depository shares representing common shares or preference shares, senior or subordinated debt securities, warrants to purchase common shares, preference shares and debt securities, share purchase contracts, share purchase units and units which may consist of any combination of the securities listed above. In addition, the shelf registration statement will provide for secondary sales of common shares sold by the Company's shareholders. The registration statement is intended to provide the Company with additional flexibility to access capital markets for general corporate purposes, subject to market conditions and the Company's capital needs.

The following table details the capital resources of the Company's more significant subsidiaries on an unconsolidated basis:

|   | <b>Capital at<br/>September 30,<br/>2009</b> |
|---|--|
| <b>(Dollars in thousands)</b>                                   |  |
| Validus Reinsurance, Ltd. (consolidated), excluding IPCRe, Ltd. | \$ 1,791,208                                 |
| IPCRe, Ltd  | 1,886,217                                    |
| <b>Total Validus Reinsurance, Ltd. (consolidated)</b>           | <b>3,677,425</b>                             |
| Talbot Holdings, Ltd  | 593,067                                      |
| <b>Total consolidated capitalization</b>                        | <b>4,270,492</b>                             |
| Debentures payable  | (304,300)                                    |
| <b>Total shareholders' equity</b>                               | <b>\$ 3,966,192</b>                          |

Please refer to the discussion of capital resources in Item 7, Management's Discussion and Analysis of Results of Operations and Financial Condition in the Company's Annual Report on Form 10-K for the year ended December 31, 2008. There have been no other material changes to this discussion.

**Recent accounting pronouncements**

Please refer to Note 2 to the consolidated financial statements (Part I, Item I) for further discussion of relevant recent accounting pronouncements.

### Debt and Financing Arrangements

The following table details the Company's borrowings and credit facilities as at September 30, 2009:

| <b>(Dollars in thousands)</b>                    | <b>Commitments</b>  | <b>Outstanding</b> |
|--|---------------------|--------------------|
| 9.069% Junior Subordinated Deferrable Debentures | \$ 150,000          | \$ 150,000         |
| 8.480% Junior Subordinated Deferrable Debentures | 200,000             | 154,300            |
| \$200,000 unsecured letter of credit facility    | 200,000             |                    |
| \$500,000 secured letter of credit facility      | 500,000             | 269,231            |
| \$250,000 IPC Syndicated facility                | 250,000             | 38,602             |
| \$350,000 IPC Bi-Lateral facility                | 350,000             | 91,071             |
| Talbot FAL facility                              | 100,000             | 100,000            |
| Talbot third party FAL facility                  | 121,515             | 121,515            |
| <b>Total</b>                                     | <b>\$ 1,871,515</b> | <b>\$ 924,719</b>  |

- (1) The third party FAL facility comprises \$144.0 million which supports the 2007 and prior underwriting years. These funds have now been withdrawn from Lloyd's and placed in escrow but remain available to pay losses.

**Table of Contents**

On July 24, 2009, the Company announced that it has entered into the Second Amendment to each of its \$500.0 million five-year secured letter of credit facility, \$200.0 million three-year unsecured facility and the First Amendment to its \$100.0 million Talbot FAL facility to amend a specific investment restriction clause to permit the completion of the IPC amalgamation agreement. The amendment also modifies and updates certain pricing and covenant terms.

IPCRe obtains letters of credit through a \$250 million Credit Agreement between IPC Holdings, Ltd., IPCRe Limited, the Lenders party thereto and Wachovia Bank, National Association (the IPC Syndicated Facility ) and a \$350 million Letters of Credit Master Agreement between Citibank N.A. and IPCRe Limited (the IPC Bi-Lateral Facility ). In July, 2009, certain terms of these credit facilities were amended including suspending IPCRe s ability to increase existing letters of credit or to issue new letters of credit. With respect of the IPC Syndicated Facility, IPCRe provides the banks security by depositing cash in the amount of 103% of the aggregate letters of credit outstanding. Effective September 30, 2009 and December 31, 2008, there were outstanding letters of credit of \$129.7 million and \$166.3 million, respectively, of which \$38.6 million and \$65.9 million were issued from the IPC Syndicated Facility with \$91.1 million and \$100.4 million issued from the IPC Bi-Lateral Facility.

Please refer to Note 7 to the consolidated financial statements (Part I, Item I) for further discussion of the Company s debt and financing arrangements.

**Ratings**

*A.M. Best.* On July 9, 2009, following the announcement that the Company entered into the Amalgamation Agreement with IPC Holdings, Ltd. ( IPC ), *A.M. Best* placed the Company s *bbb-* issuer credit and indicative senior debt ratings as well as the *bb+* subordinated debt and *bb* preferred stock ratings under review with negative implications. In addition, the *A-* financial strength and *a-* issuer credit ratings of subsidiary unit Validus Reinsurance, Ltd. were placed under review with negative implications. *A.M. Best* explained the rationale for the under review status which reflects uncertainties associated with the transaction including the execution risk in completing the deal as well as integrating both companies. *A.M. Best* also noted remaining concern with the heightened risk profile of the combined entity due to the significant property catastrophe business written by Validus Holdings and IPC and the timing of the transaction during the Atlantic wind storm season.

On September 9, 2009, following the IPC Acquisition, *A.M. Best* removed the under review with negative implications modifier to the ratings of Validus Holdings, Ltd., Validus Reinsurance, Ltd., IPCRe, and IPCRe Europe Limited. The outlook assigned to all ratings was returned to stable.

At the same time, *A.M. Best* affirmed Validus Holdings, Ltd. s issuer credit rating of *bbb-* and the Company s indicative ratings for securities available under the shelf registration at *bbb-* on senior debt, *bb+* on subordinated debt and *bb* on preferred stock. *A.M. Best* also affirmed the financial strength ratings at *A-* and issuer credit ratings at *a-* for Validus Reinsurance Ltd., IPCRe and IPCRe Europe Ltd. *A.M. Best* also withdrew the issuer credit rating of *bbb-* and the indicative ratings of *bb+* on preferred stock, *bbb* on senior unsecured debt and *bbb-* on subordinated debt for securities available under the former shelf registration of IPC Holdings Ltd., as they have been merged out of existence.

*A.M. Best* noted that the ratings contemplate the potential benefits that will be realized from Validus Holdings acquisition of IPC Holdings due to the larger capital base and market profile. *A.M. Best* said these strengths are partially offset by Validus Holdings susceptibility to low-frequency, high-severity events as a property catastrophe-focused reinsurer and the increased uncertainty in the short term due to the business previously underwritten by IPCRe.

**Table of Contents**

*Standard & Poor's.* On July 10, 2009, Standard & Poor's (S&P) revised its outlook on the Company to positive from stable and affirmed the counterparty credit rating of BBB-. According to S&P, the Company's ratings are based on the group's good and expanding competitive position; strong capitalization; strong risk controls around exposure management, underwriting and modeling; and very strong operating performance since its inception, partially offset by the potential integration risk related to the expected IPC transaction.

On September 8, 2009, S&P downgraded the counterparty credit rating of IPC Holdings Ltd. (IPC) to BBB- from BBB, noting that the rating was lowered to align it with the ratings on Validus Holdings, Ltd. Subsequently, S&P withdrew its ratings on IPC and subsidiaries at the company's request.

Also on September 8, 2009, S&P published a full credit analysis on Validus which confirmed the BBB- counterparty credit rating with a positive outlook.

*Moody's Investors Service.* On July 13, 2009, Moody's Investors Service (Moody's) said that it will continue the negative rating outlook on the Company and subsidiary unit Validus Reinsurance Ltd. following the Amalgamation Agreement with IPC. Moody's noted that The ratings were assigned a negative outlook on April 2, 2009 when Validus initially made an unsolicited stock for stock offer to acquire IPC.

On September 9, 2009, Moody's affirmed the Company's ratings and changed the ratings outlook to stable from negative. The Baa2 long-term issuer rating was affirmed for Validus Holdings, Ltd. and the A3 insurance financial strength rating was affirmed for Validus Reinsurance, Ltd.

**Investments**

A significant portion of contracts written provide short-tail reinsurance coverage for losses resulting mainly from natural and man-made catastrophes, which could result in a significant amount of losses on short notice. Accordingly, the Company's investment portfolio is structured to provide significant liquidity and preserve capital, which means the investment portfolio contains a significant amount of relatively short-term fixed maturity investments, such as U.S. government securities, U.S. government-sponsored enterprises securities, corporate debt securities and mortgage-backed and asset-backed securities.

Substantially all of the fixed maturity investments held at September 30, 2009 were publicly traded. At September 30, 2009, the average duration of the Company's fixed maturity portfolio was 2.2 years (December 31, 2008: 1.8 years) and the average rating of the portfolio was AA+ (December 31, 2008: AAA). At September 30, 2009, the total fixed maturity portfolio was \$4,590.1 million (December 31, 2008: \$2,454.5 million), of which \$2,831.9 million (December 31, 2008: \$1,941.3 million) were rated AAA. At September 30, 2009, fair value measurements of certain non-Agency RMBS securities, representing 1.3% of the Company's total assets, have primarily unobservable inputs (December 31, 2008: 2.6%).

On September 4, 2009, as part of the acquisition of IPCRe the Company assumed IPCRe's investment portfolio containing \$1,820.9 million of corporate bonds, \$112.9 million of agency residential mortgage-backed securities, \$234.7 million of equity mutual funds, \$114.8 million fund of hedge funds and \$11.0 million of equity mutual funds contained within a deferred compensation trust. On September 9, 2009, the Company realized a gain of \$4.5 million on the disposition of \$234.7 million of equity mutual funds. A redemption request for the fund of hedge funds has been submitted for value as at October 31, 2009. Given the fund of hedge funds' relative illiquidity, the Company anticipates receiving the majority of proceeds periodically over the three months to end December 31, 2009. As at September 30, 2009, the fund of hedge funds included a side pocket of \$28.1 million. While a redemption request has been submitted, the timing of receipt of proceeds on the side pocket is unavailable.

On August 28, 2009, the Company sold short equity index futures contracts with a goal of hedging until closing of the IPC Acquisition and liquidation of IPCRe's mutual fund equity portfolio exposure. The contracts were closed when the equity positions were fully redeemed on September 9, 2009. The Company experienced a \$3.3 million realized investment loss as a result of the futures contracts.

The Company's investment guidelines require that investments be rated A- or higher at the time of purchase. During the quarterly period ended September 30, 2009, Moody's downgraded a substantial number of non-agency mortgage backed securities issues, including several securities held by the Company. The Company reports the

**Table of Contents**

ratings of its investment portfolio securities at the lower of Moody's or Standard & Poor's rating for each investment security and, as a result, the Company's investment portfolio now has \$95.4 million of non-agency mortgage backed securities rated less than investment grade. The Company expects that Standard & Poor's may take similar actions in respect of their ratings of non-agency mortgage backed securities. The other components of less than investment grade securities held by the Company at September 30, 2009 were \$21.4 million of catastrophe bonds and \$12.1 million of corporate bonds.

Cash and cash equivalents and investments in Talbot of \$1,188.3 million at September 30, 2009 were held in trust for the benefit of cedants and policyholders, and to facilitate the accreditation as an alien insurer/reinsurer by certain regulators (December 31, 2008: \$1,032.3 million). Total cash and cash equivalents and investments in Talbot were \$1,330.5 million at September 30, 2009 (December 31, 2008: \$1,142.0 million).

As of September 30, 2009, the Company had approximately \$3.7 million of asset-backed securities with sub-prime collateral (December 31, 2008: \$6.4 million) and \$90.5 million of Alt-A RMBS (December 31, 2008: \$103.8 million).

As described more fully under the "Critical Accounting Policies and Estimates" in Item 7, *Management's Discussion and Analysis of Results of Operations and Financial Condition* in the Company's Annual Report on Form 10-K for the year ended December 31, 2008, the Company identified certain non-Agency RMBS securities trading in inactive markets. During the three months ended September 30, 2009, the change in fair value for the identified RMBS securities resulted in a \$0.6 million decrease in net unrealized loss on investments. This decrease in net unrealized losses on investments resulted in a \$0.6 million increase in shareholders' equity as at September 30, 2009.

**Cash Flows**

During the three months ended September 30, 2009 and 2008, the Company generated net cash from operating activities of \$90.0 million and \$150.0 million, respectively. During the nine months ended September 30, 2009 and 2008, the Company generated net cash from operating activities of \$299.8 million and \$397.4 million, respectively. Cash flows from operations generally represent premiums collected, investment earnings realized and investment gains realized less losses and loss expenses paid and underwriting and other expenses paid. Cash flows from operations may differ substantially, however, from net income.

Pursuant to an Amalgamation Agreement dated July 9, 2009 among IPC, Validus Holdings, Ltd. and Validus, Ltd. (the "Amalgamation Agreement"), on September 4, 2009, the Company acquired all of IPC's outstanding common shares in exchange for a combination of the Company's common shares and cash (the "IPC Acquisition"). Each outstanding IPC common share (including any shares held by IPC shareholders that did not vote in favor of the amalgamation, but excluding shares owned by the Company), have been cancelled and converted into the right to receive 0.9727 of the Company's common shares, \$7.50 in cash (less any applicable withholding tax and without interest) and cash in lieu of fractional shares. The IPC Acquisition resulted in the issuance by the Company of 54,556,762 common shares valued at \$24.10 per share and the payment of \$420.8 million in cash to IPC shareholders. IPC's operations are focused on short-tail lines of reinsurance. 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 other short-tail reinsurance on a worldwide basis. The acquisition of IPC was undertaken to gain a strategic advantage in the current reinsurance market and increase the Company's capital base. Sources of funds consist primarily of the receipt of premiums written, investment income and proceeds from sales and redemptions of investments. In addition, cash will also be received from financing activities. Cash is used to pay primarily losses and loss expenses, brokerage commissions, excise taxes, general and administrative expenses, purchase new investments, payment of premiums retroceded and payment of dividends. The Company has had sufficient resources to meet its liquidity requirements.

As of September 30, 2009 and December 31, 2008, the Company had cash and cash equivalents of \$393.8 million and \$449.9 million, respectively.

The Company has written certain business that has loss experience generally characterized as having low frequency and high severity. This results in volatility in both results and operational cash flows. The potential for large claims or a series of claims under one or more reinsurance contracts means that substantial and unpredictable

**Table of Contents**

payments may be required within relatively short periods of time. As a result, cash flows from operating activities may fluctuate, perhaps significantly, between individual quarters and years. Management believes the Company's unused credit facility amounts and highly liquid investment portfolio are sufficient to support any potential operating cash flow deficiencies. Please refer to the table detailing the Company's borrowings and credit facilities as at September 30, 2009, presented above.

In addition to relying on premiums received and investment income from the investment portfolio, the Company intends to meet these cash flow demands by carrying a substantial amount of short and medium term investments that would mature, or possibly be sold, prior to the settlement of expected liabilities. The Company cannot provide assurance, however, that it will successfully match the structure of its investments with its liabilities due to uncertainty related to the timing and severity of loss events.

**Table of Contents**

**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

The Private Securities Litigation Reform Act of 1995 ( PSLRA ) provides a safe harbor for forward-looking statements. Any prospectus, prospectus supplement, the Company's Annual Report to shareholders, any proxy statement, any other Form 10-K, Form 10-Q or Form 8-K of the Company or any other written or oral statements made by or on behalf of the Company may include forward-looking statements that reflect the Company's current views with respect to future events and financial performance. Such statements include forward-looking statements both with respect to the Company in general, and to the insurance and reinsurance sectors in particular. Statements that include the words expect , intend , plan , believe , project , anticipate , will , may , and similar statements of a forward-looking nature identify forward-looking statements for purposes of the PSLRA or otherwise. All forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause actual results to differ materially from those indicated in such statements and, therefore, you should not place undue reliance on any such statement.

We believe that these factors include, but are not limited to, the following:  
unpredictability and severity of catastrophic events;

our ability to obtain and maintain ratings, which may be affected by our ability to raise additional equity or debt financings, as well as other factors described herein;

adequacy of the Company's and IPC's risk management and loss limitation methods;

cyclicality of demand and pricing in the insurance and reinsurance markets;

the Company's limited operating history;

the Company's ability to implement its business strategy during soft as well as hard markets;

adequacy of the Company's loss reserves;

continued availability of capital and financing;

the Company's ability to identify, hire and retain, on a timely and unimpeded basis and on anticipated economic and other terms, experienced and capable senior management, as well as underwriters, claims professionals and support staff;

acceptance of our business strategy, security and financial condition by rating agencies and regulators, as well as by brokers and (re)insureds;

competition, including increased competition, on the basis of pricing, capacity, coverage terms or other factors;

potential loss of business from one or more major insurance or reinsurance brokers;

the Company's ability to implement, successfully and on a timely basis, complex infrastructure, distribution capabilities, systems, procedures and internal controls, and to develop accurate actuarial data to support the business and regulatory and reporting requirements;

general economic and market conditions (including inflation, volatility in the credit and capital markets, interest rates and foreign currency exchange rates) and conditions specific to the insurance and reinsurance markets in which we expect to operate;

the integration of IPC or other businesses we may acquire or new business ventures, including overseas offices, we may start;

accuracy of those estimates and judgments used in the preparation of our financial statements, including those related to revenue recognition, insurance and other reserves, reinsurance recoverables, investment valuations,



**Table of Contents**

intangible assets, bad debts, taxes, contingencies, litigation and any determination to use the deposit method of accounting, which, for a relatively new insurance and reinsurance company like our company, are even more difficult to make than those made in a mature company because of limited historical information;

the effect on the Company's or IPC's investment portfolio of changing financial market conditions including inflation, interest rates, liquidity and other factors;

acts of terrorism, political unrest, outbreak of war and other hostilities or other non-forecasted and unpredictable events;

availability and cost of reinsurance and retrocession coverage;

the failure of reinsurers, retrocessionaires, producers or others to meet their obligations to us;

the timing of loss payments being faster or the receipt of reinsurance recoverables being slower than anticipated by us;

changes in domestic or foreign laws or regulations, or their interpretations;

changes in accounting principles or the application of such principles by regulators;

statutory or regulatory or rating agency developments, including as to tax policy and matters and reinsurance and other regulatory matters such as the adoption of proposed legislation that would affect Bermuda-headquartered companies and/or Bermuda-based insurers or reinsurers;

failure to realize the anticipated benefits of the IPC Acquisition, including as a result of failure or delay in integrating the businesses of the Company and IPC; and

the other factors set forth herein under Part II Item 1A "Risk Factors" and under Part I Item 2 "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the other sections of this Quarterly Report on Form 10-Q and the Company's Annual Report on Form 10-K for the year ended December 31, 2008, as well as the risk and other factors set forth in the Company's other filings with the SEC as well as management's response to any of the aforementioned factors.

In addition, other general factors could affect our results, including: (a) developments in the world's financial and capital markets and our access to such markets; (b) changes in regulations or tax laws applicable to us, including, without limitation, any such changes resulting from the recent investigations relating to the insurance industry and any attendant litigation; and (c) the effects of business disruption or economic contraction due to terrorism or other hostilities.

The foregoing review of important factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included herein or elsewhere. Any forward-looking statements made in this report are qualified by these cautionary statements, and there can be no assurance that the actual results or developments anticipated by us will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, us or our business or operations. We undertake no obligation to update publicly or revise any forward-looking statement, whether as a result of new information, future developments or otherwise.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We believe we are principally exposed to five types of market risk:  
interest rate risk;

foreign currency risk;

credit risk;

96

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**Table of Contents**

liquidity risk; and

effects of inflation.

*Interest Rate Risk:* The Company's primary market risk exposure is to changes in interest rates. The Company's fixed maturity portfolio is exposed to interest rate risk. Fluctuations in interest rates have a direct impact on the market valuation of these investments. As interest rates rise, the market value of the Company's fixed maturity portfolio falls and the Company has the risk that cash outflows will have to be funded by selling assets, which will be trading at depreciated values. As interest rates decline, the market value of the Company's fixed income portfolio increases and the Company has reinvestment risk, as funds reinvested will earn less than is necessary to match anticipated liabilities. We manage interest rate risk by selecting investments with characteristics such as duration, yield, currency and liquidity tailored to the anticipated cash outflow characteristics of the insurance and reinsurance liabilities the Company assumes.

As at September 30, 2009, the impact on the Company's fixed maturity and short-term investments from an immediate 100 basis point increase in market interest rates (based on U.S. treasury yield) would have resulted in an estimated decrease in market value of 2.6%, or approximately \$138.4 million. As at September 30, 2009, the impact on the Company's fixed maturity portfolio from an immediate 100 basis point decrease in market interest rates would have resulted in an estimated increase in market value of 1.7% or approximately \$92.0 million.

As at September 30, 2008, the impact on the Company's fixed maturity and short-term investments from an immediate 100 basis point increase in market interest rates would have resulted in an estimated decrease in market value of 2.2%, or approximately \$64.3 million. As at September 30, 2008, the impact on the Company's fixed maturity portfolio from an immediate 100 basis point decrease in market interest rates would have resulted in an estimated increase in market value of 2.2% or approximately \$63.5 million.

As at September 30, 2009, the Company held \$914.4 million (December 31, 2008: \$994.1 million), or 19.9% (December 31, 2008: 40.5%), of the Company's fixed maturity portfolio in asset-backed and mortgage-backed securities. These assets are exposed to prepayment risk, which occurs when holders of underlying loans increase the frequency with which they prepay the outstanding principal before the maturity date and refinance at a lower interest rate cost. The adverse impact of prepayment is more evident in a declining interest rate environment. As a result, the Company will be exposed to reinvestment risk, as cash flows received by the Company will be accelerated and will be reinvested at the prevailing interest rates.

*Foreign Currency Risk:* Certain of the Company's reinsurance contracts provide that ultimate losses may be payable in foreign currencies depending on the country of original loss. Foreign currency exchange rate risk exists to the extent that there is an increase in the exchange rate of the foreign currency in which losses are ultimately owed. Therefore, we attempt to manage our foreign currency risk by seeking to match our liabilities under insurance and reinsurance policies that are payable in foreign currencies with cash and investments that are denominated in such currencies. As of September 30, 2009, \$407.7 million, or 5.7% of our total assets and \$389.8 million, or 1.2% of our total liabilities was held in foreign currencies. As of September 30, 2009, \$89.8 million, or 2.8% of our total net liabilities held in foreign currencies was non-monetary items which do not require revaluation at each reporting date. As of September 30, 2008, \$440.9 million, or 9.8% of our total assets and \$356.0 million, or 13.7% of our total liabilities was held in foreign currencies. As of September 30, 2008, \$81.7 million, or 3.2% of our total net liabilities held in foreign currencies was non-monetary items which do not require revaluation at each reporting date. The Company does not transact in foreign exchange markets to hedge its foreign currency exposure. To the extent foreign currency exposure is not hedged, the Company may experience exchange losses, which in turn would adversely affect the results of operations and financial condition.

*Credit Risk:* We are exposed to credit risk primarily from the possibility that counterparties may default on their obligations to us. We attempt to limit our credit exposure by purchasing high quality fixed income investments to maintain an average portfolio credit quality of AA- or higher with mortgage and commercial mortgage-backed issues having an aggregate weighted average credit quality of AAA. In addition, we have limited our exposure to any single issuer to 3.0% or less of total investments, excluding treasury and agency securities. The minimum credit rating of any security purchased is A-/A3 and where investments are downgraded below A-/A3, we permit our investment managers to hold up to 2.0% in aggregate market value, or up to 10.0% with written authorization of the



**Table of Contents**

Company. At September 30, 2009, 3.9% of the portfolio was below A-/A3 and we did not have an aggregate exposure to any single issuer of more than 1.8% of total investments, other than with respect to government securities.

The amount of the maximum exposure to credit risk is indicated by the carrying value of the Company's financial assets. The Company's primary credit risks reside in investment in U.S. corporate bonds and recoverables from reinsurers at the Talbot segment. The Company evaluates the financial condition of its reinsurers and monitors concentration of credit risk arising from its exposure to individual reinsurers. The reinsurance program is generally placed with reinsurers whose rating, at the time of placement, was A- or better rated by S & P or the equivalent with other rating agencies. Exposure to a single reinsurer is also controlled with restrictions dependent on rating. 100.0% of reinsurance recoverables (which includes loss reserves recoverable and recoverables on paid losses) at September 30, 2009 were from reinsurers rated A-, (December 31, 2008 rated A- or better) or from reinsurers posting full collateral. Validus Re does not have any reinsurance recoverable balances that are not fully collateralized.

*Liquidity risk:* Certain of the Company's investments may become illiquid. The current disruption in the credit markets may materially affect the liquidity of the Company's investments, including residential mortgage-backed securities which represent 14.2% (December 31, 2008: 20.3%) of total cash and investments. If the Company requires significant amounts of cash on short notice in excess of normal cash requirements (which could include claims on a major catastrophic event) in a period of market illiquidity, the investments may be difficult to sell in a timely manner and may have to be disposed of for less than what may otherwise have been possible under other conditions. At September 30, 2009, the Company had \$2,052.8 million of unrestricted, liquid assets, defined as unpledged cash and cash equivalents, short term investments, government and government agency securities. Details of the Company's debt and financing arrangements at September 30, 2009 are provided below.

On September 4, 2009, as part of the acquisition of IPCRe the Company assumed IPCRe's investment portfolio containing \$1,820.9 million of corporate bonds, \$112.9 million of agency residential mortgage-backed securities, \$234.7 million of equity mutual funds, \$114.8 million fund of hedge funds and \$11.0 million of equity mutual funds contained within a deferred compensation trust. On September 9, 2009, the Company realized a gain of \$4.5 million on the disposition of \$234.7 million of equity mutual funds. A redemption request for the fund of hedge funds has been submitted for value as at October 31, 2009. Given the fund of hedge funds' relative illiquidity, the Company anticipates receiving the majority of proceeds periodically over the three months to end December 31, 2009. As at September 30, 2009, the fund of hedge funds included a side pocket of \$28.1 million. While a redemption request has been submitted, the timing of receipt of proceeds on the side pocket is unavailable.

| <b>(Dollars in thousands)</b>                    | <b>Maturity<br/>Date /<br/>Term</b> | <b>In Use/<br/>Outstanding</b> |
|--|-------------------------------------|--------------------------------|
| 9.069% Junior Subordinated Deferrable Debentures | June 15, 2036                       | \$ 150,000                     |
| 8.480% Junior Subordinated Deferrable Debentures | June 15, 2037                       | 154,300                        |
| \$200,000 unsecured letter of credit facility    | March 12, 2010                      |                                |
| \$500,000 secured letter of credit facility      | March 12, 2012                      | 269,231                        |
| \$250,000 IPC Syndicated Facility                | April 13, 2011                      | 38,602                         |
| \$350,000 IPC Bi-Lateral Facility                | April 14, 2010                      | 91,071                         |
| Talbot FAL facility                              | December 31,<br>2009                | 100,000                        |
| Talbot third party FAL facility                  | December 31,<br>2009                | 121,515                        |
| <b>Total</b>                                     |                                     | <b>\$ 924,719</b>              |

*Effects of Inflation:* We do not believe that inflation has had or will have a material effect on our combined results of operations, except insofar as (a) inflation may affect interest rates, and (b) losses and loss expenses may be affected by inflation.

**ITEM 4. CONTROLS AND PROCEDURES**

**Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures**

98

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**Table of Contents**

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of disclosure controls and procedures pursuant to Rules 13a-15 and 15d-15 promulgated under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report. The Company acquired all of the outstanding shares of IPC on September 4, 2009. IPC's assets represented approximately 33.0% of the Company's total assets as at September 30, 2009. Consistent with the SEC's general guidance, IPC has been omitted from the Company's assessment scope for the effectiveness of internal control over financial reporting in the year of acquisition.

Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective to provide reasonable assurance that all material information relating to the Company required to be filed in this report has been made known to them in a timely fashion.

**Changes in Internal Control Over Financial Reporting**

There have been no changes in internal control over financial reporting identified in connection with the Company's evaluation required pursuant to Rules 13a-15 and 15d-15 promulgated under the Securities Exchange Act of 1934, as amended, that occurred during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

We anticipate that, similar to the rest of the insurance and reinsurance industry, we will be subject to litigation and arbitration in the ordinary course of business.

**ITEM 1A. RISK FACTORS**

Please refer to the discussion of Risk Factors in Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2008 and in Part II, Item 1A of the Company's Quarterly Report on Form 10-Q for the three months ended June 30, 2009.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

There were no stock repurchases for the three months ended September 30, 2009.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

**Special Meeting of Shareholders**

(a) The special meeting of shareholders (the "Special Meeting") of the Company was held on September 4, 2009.

(b) Proxies for the Special Meeting were solicited pursuant to Regulation 14 under the Securities Exchange Act of 1934. There was no solicitation in opposition to the proposals as listed in the Company's proxy statement, dated August 6, 2009 (the "Special Meeting Proxy Statement").

(c) The shareholders of the Company (1) approved the issuance of common shares, \$0.175 par value per share, in connection with the acquisition of all of the outstanding common shares of IPC and (2) approved the adjournment of the meeting. Set forth below are the voting results for these proposals:

**Table of Contents**Approval of the Issuance of Common Shares in Connection with the IPC Acquisition

|  | <b>For</b> | <b>Against</b> | <b>Abstain</b> |
|--|------------|----------------|----------------|
| Total:   | 51,066,389 | 597,956        | 13,034         |
| <u>Approved the Adjournment of the Meeting</u> |            |                |                |

|        | <b>For</b> | <b>Against</b> | <b>Abstain</b> |
|--------|------------|----------------|----------------|
| Total: | 50,597,673 | 1,068,514      | 11,192         |

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

| <b>Exhibit</b> | <b>Description</b>  |
|----------------|---|
| Exhibit 10.1   | Amendment No. 1, dated as of July 23, 2009, to the \$100 million Standby Letter of Credit Facility dated as of 28 November 2007, among Talbot Holdings Ltd., Validus Holdings, Ltd., the Lenders party thereto and Lloyds TSB Bank plc, as Agent (Incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on July 23, 2009).   |
| Exhibit 10.2   | Second Amendment, dated as of July 24, 2009, to each of the Three-Year Unsecured Letter of Credit Facility Agreement dated as of March 12, 2007, as amended by the First Amendment dated October 25, 2007, and the Five-Year Secured Letter of Credit Facility Agreement dated as of March 12, 2007, as amended by the First Amendment dated October 25, 2007, among Validus Holdings, Ltd., Validus Reinsurance, Ltd., the Lenders party thereto and JPMorgan Chase Bank, National Association, as administrative agent for the Lenders (Incorporated by reference to the Company's Current Report on Form 8-K filed with the SEC on July 23, 2009). |
| Exhibit 31.1   | Certification of Chief Executive Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002.   |
| Exhibit 31.2   | Certification of Chief Financial Officer pursuant to Section 302 of The Sarbanes-Oxley Act of 2002.   |
| Exhibit 32     | Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002.   |



**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**VALIDUS HOLDINGS, LTD.**  
(Registrant)

Date: November 6, 2009

/s/ Edward J. Noonan

Edward J. Noonan  
Chief Executive Officer

Date: November 6, 2009

/s/ Joseph E. (Jeff) Consolino

Joseph E. (Jeff) Consolino  
Chief Financial Officer and Executive Vice President

101