

WHITE MOUNTAINS INSURANCE GROUP LTD  
Form 10-K  
March 07, 2006

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-K**

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

For the fiscal year ended December 31, 2005

OR

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

For the transition period from        to

Commission file number 1-8993

**WHITE MOUNTAINS INSURANCE GROUP, LTD.**

(Exact name of Registrant as specified in its charter)

**Bermuda**

(State or other jurisdiction of  
incorporation or organization)

**94-2708455**

(I.R.S. Employer  
Identification No.)

**Harborside Financial Center, Plaza 5,**

**Jersey City, New Jersey**

(Address of principal executive offices)

**07311-1114**

(Zip Code)

Registrant's telephone number, including area code: **(201) 631-3300**

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Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Shares, par value \$1.00 per share	New York Stock Exchange Bermuda Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Act. Yes  No

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.  
Yes  No

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated Filer  Non-accelerated filer

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

The aggregate market value of voting shares (based on the closing price of those shares listed on the New York Stock Exchange and the consideration received for those shares not listed on a national or regional exchange) held by non-affiliates of the Registrant as of June 30, 2005, was \$3,785,698,416.

As of March 3, 2006, 10,780,053 common shares, par value of \$1.00 per share, were outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the Registrant's Definitive Proxy Statement to be filed with the Securities and Exchange Commission ( SEC ) pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended (the Exchange Act ), relating to the Registrant's Annual General Meeting of Members scheduled to be held May 25, 2006 are incorporated by reference into Part III of this Form 10-K. With the exception of the portions of the Proxy Statement specifically incorporated herein by reference, the Proxy Statement is not deemed to be filed as part of this Form 10-K.

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## PART I

### Item 1. Business

#### GENERAL

White Mountains Insurance Group, Ltd. (the Company or the Registrant) is an exempted Bermuda limited liability company whose principal businesses are conducted through its subsidiaries and affiliates in the businesses of property and casualty insurance and reinsurance. Within this report, the term White Mountains is used to refer to one or more entities within the consolidated organization, as the context requires. The Company's headquarters are located at Bank of Butterfield Building, 42 Reid Street, Hamilton, Bermuda HM 12, its principal executive office is located at Harborside Financial Center, Plaza 5, Jersey City, New Jersey, 07311-1114 and its registered office is located at Clarendon House, 2 Church Street, Hamilton, Bermuda HM 11. White Mountains reportable segments are OneBeacon, White Mountains Re, Esurance and Other Operations.

The OneBeacon segment consists of the OneBeacon Insurance Group LLC family of companies (collectively OneBeacon), which are U.S.-based property and casualty insurance writers, substantially all of which operate in a multi-company pool. OneBeacon offers a wide range of specialty, personal and commercial products and services sold primarily through select independent agents. OneBeacon was acquired by White Mountains from Aviva plc (Aviva, formerly CGNU) on June 1, 2001 (the OneBeacon Acquisition).

The White Mountains Re segment consists of White Mountains Re Group, Ltd. and its subsidiaries. White Mountains Re offers lead reinsurance capacity for property, casualty, accident & health, aviation and marine exposures on a worldwide basis through its reinsurance subsidiaries, Folksamerica Reinsurance Company (Folksamerica Re, together with its parent, Folksamerica Holding Company, Folksamerica), which has been a wholly-owned subsidiary of White Mountains since 1998, and Sirius International Insurance Corporation (Sirius International). On April 16, 2004, White Mountains acquired Sirius Insurance Holdings Sweden AB and its subsidiaries (Sirius) from ABB Ltd. (the Sirius Acquisition). The principal companies acquired were Sirius International, Sirius America Insurance Company (Sirius America), which provides primary insurance programs in the United States, and Scandinavian Reinsurance Company Ltd. (Scandinavian Re), a reinsurance company that has been in run-off since 2002. White Mountains Re also provides reinsurance advisory services, specializing in international property and marine excess reinsurance, through White Mountains Underwriting Limited (domiciled in Ireland and formed in 2001) and White Mountains Underwriting (Bermuda) Limited, formed in 2003 (collectively, WMU).

The Esurance segment consists of Esurance Holdings, Inc. and its subsidiaries (collectively, Esurance). Esurance, which has been a unit of White Mountains since October 2000, markets personal auto insurance directly to customers online and through select online agents.

White Mountains Other Operations segment consists of the Company and its intermediate holding companies, its wholly-owned investment management subsidiary, White Mountains Advisors LLC (WM Advisors), as well as the International American Group, Inc. (the International American Group). The International American Group, which was acquired by White Mountains in 1999, consists of American Centennial Insurance Company (American Centennial) and British Insurance Company of Cayman (British Insurance Company), both of which are in run-off. The Other Operations segment also includes White Mountains investments in warrants to purchase common shares of both Montpelier Re Holdings, Ltd. (Montpelier) and Symetra Financial Corporation (Symetra).



## White Mountains Operating Principles

White Mountains strives to operate within the spirit of four operating principles. These are:

**Underwriting Comes First.** An insurance enterprise must respect the fundamentals of insurance. There must be a realistic expectation of underwriting profit on all business written, and demonstrated fulfillment of that expectation over time, with focused attention to the loss ratio and to all the professional insurance disciplines of pricing, underwriting and claims management.

**Maintain a Disciplined Balance Sheet.** The first concern here is that insurance liabilities must always be fully recognized. Loss reserves and expense reserves must be solid before any other aspect of the business can be solid. Pricing, marketing and underwriting all depend on informed judgment of ultimate loss costs and that can be managed effectively only with a disciplined balance sheet.

**Invest for Total Return.** Historical insurance accounting has tended to hide unrealized gains and losses in the investment portfolio and over-reward reported investment income (interest and dividends). Regardless of the accounting, White Mountains must invest for the best growth in after-tax value over time. In addition to investing our bond portfolios for total after-tax return, that will also mean prudent investment in a balanced portfolio consistent with leverage and insurance risk considerations.

**Think Like Owners.** Thinking like owners has a value all its own. There are stakeholders in a business enterprise and doing good work requires more than this quarter's profit. But thinking like an owner embraces all that without losing the touchstone of a capitalist enterprise.

## ONEBEACON

OneBeacon, which is headquartered in Boston, Massachusetts, has been a part of White Mountains since June 2001. OneBeacon is one of the oldest property and casualty insurers in the United States, tracing its roots to 1831 and the Potomac Fire Insurance Company. OneBeacon's legacy includes being among the first to issue automobile policies, honoring claims arising from the great San Francisco earthquake and the sinking of the Titanic, as well as insuring several U.S. presidents.

At December 31, 2005 and 2004, OneBeacon had \$9.7 billion and \$10.0 billion of total assets, respectively, and shareholder's equity of \$2.0 billion and \$2.3 billion, respectively. OneBeacon's principal operating insurance subsidiaries are rated A (Excellent, the third highest of fifteen ratings) by A.M. Best and A (Strong, the sixth highest of twenty-one ratings) by Standard & Poor's, rating agencies that specialize in the insurance and reinsurance industry.



### **Property and Casualty Insurance Overview**

Generally, property and casualty insurance companies write insurance policies in exchange for premiums paid by its customers (the insured). An insurance policy is a contract between the insurance company and the insured where the insurance company agrees to pay for losses suffered by the insured that are covered under the contract. Such contracts often are subject to subsequent legal interpretation by courts, legislative action and arbitration. Property insurance generally covers the financial consequences of accidental losses to the insured's property, such as a home and the personal property in it, or a business building, inventory and equipment. Casualty insurance (often referred to as liability insurance) generally covers the financial consequences of a legal liability of an individual or an organization resulting from negligent acts and omissions causing bodily injury and/or property damage to a third party. Claims on property coverage generally are reported and settled in a relatively short period of time, whereas those on casualty coverage can take years, even decades, to settle.

Insurance companies derive substantially all of their revenues from earned premiums, investment income and net gains and losses from sales of investment securities. Earned premiums represent premiums received from insureds, which are recognized as revenue over the period of time that insurance coverage is provided (i.e., ratably over the life of the policy). A significant period of time normally elapses between the receipt of insurance premiums and the payment of insurance claims. During this time, investment income is generated, consisting primarily of interest earned on fixed maturity investments and dividends earned on equity securities. Net realized investment gains and losses result from sales of securities from the insurance companies' investment portfolios.

Insurance companies incur a significant amount of their total expenses from policyholder losses, which are commonly referred to as claims. In settling policyholder losses, various loss adjustment expenses (LAE) are incurred, such as insurance adjusters' fees and litigation expenses. In addition, insurance companies incur policy acquisition expenses, such as commissions paid to agents and premium taxes, and other expenses related to the underwriting process, including compensation and benefits for professional and clerical staff.

The key measure of relative underwriting performance for an insurance company is the combined ratio. An insurance company's combined ratio under accounting principles generally accepted in the United States (GAAP) is calculated by adding the ratio of incurred loss and LAE to earned premiums (the loss ratio) and the ratio of policy acquisition and other underwriting expenses to earned premiums (the expense ratio). A combined ratio under 100% indicates that an insurance company is generating an underwriting profit. However, when considering investment income and investment gains or losses, insurance companies operating at a combined ratio of greater than 100% can be profitable.

### Lines of Business

OneBeacon provides specialty lines insurance products and a variety of segmented personal lines insurance products for individuals and commercial lines insurance products for businesses.

OneBeacon has built specialty businesses by providing customized coverages to certain niche markets. These specialty businesses are not subject to extreme competitive market conditions and are distinct in their product design. Each specialty business has its own operations and distribution channels that target specific customer groups. OneBeacon's specialty lines insurance products include the following:

**Assigned risk services:** OneBeacon offers Limited Assigned Distribution (LAD) and Commercial Limited Assigned Distribution (CLAD) services to insurance companies required to accept personal and/or commercial automobile assignments through assigned risk plans in ten states. OneBeacon writes the majority of its LAD and CLAD business through the New York Automobile Insurance Plan (NYAIP) and the New Jersey Personal Automobile Insurance Plan (NJPAIP). During 2005, OneBeacon also began to write such business through other state programs, including California, Connecticut, Delaware, Maine, Pennsylvania, Texas and Vermont, as well as the District of Columbia.

**Medical errors and omissions:** provides coverage for claims arising from direct patient treatment, such as making diagnoses, rendering opinions or providing advice or referral to another physician. Medical errors and omissions also provides coverage for professional committee activities as a member of an accredited hospital staff or any professional medical association or committee. These coverages are generally offered to mid-sized hospitals and/or managed care organizations and to individual physicians, but only through selected programs.

**Ocean marine:** provides coverage for losses to an insured's vessel, cargo and/or its marine property as a result of collision, fire, piracy, windstorm or other perils. Ocean marine coverages include cargo, hull, protection and indemnity, primary and excess liability, marina package, comprehensive marina liability package and yacht products.

**Agricultural and rural marketplace products:** policies providing property and liability coverages for dairy farms, equine farms, farm equipment dealers, orchard and other commercial farms. Also provides liability and umbrella coverages for farm owners as a package and property, liability and umbrella coverages for select commercial businesses, such as feed stores, seed merchants, fruit and vegetable packers and shippers, and others actively involved

in support of farming operations. Coverage does not include multi-peril crop insurance or crop hail insurance.

Excess and surplus lines property: excess property covers the insured against certain damages over and above those covered by primary policies or a large self-insured retention. Specialized insurance coverage is available on a surplus lines basis in instances where such coverage is unavailable from insurers licensed ( admitted ) within a particular state. OneBeacon entered the excess and surplus lines property business in 2004.

Tuition reimbursement: covers tuition payments due to insured schools and colleges when a student is unable to complete a school term as a result of a covered reason for withdrawal (medical and in certain instances voluntary withdrawal and involuntary dismissal).

Community banking and lawyers professional liability: provides professional liability coverages for community banks with assets of \$3 billion or less and law firms employing fewer than 150 attorneys. OneBeacon also offers its community banking customers its commercial package product, thereby providing comprehensive insurance solutions.

OneBeacon's personal lines coverages include homeowners insurance, segmented private passenger automobile and package policies sold through select independent agents. In addition, OneBeacon provides management services for a fee to reciprocal exchanges. Since OneBeacon's acquisition of the renewal rights on Atlantic Mutual's commercial lines business in 2004 (see page 8), OneBeacon's focus on commercial lines has been to write property, liability, automobile and other related lines for small and mid-sized businesses for specific industry segments. While its personal and commercial lines are subject to more competitive pressures than its specialty lines, OneBeacon believes that it has created certain niches in its personal and commercial businesses through proper segmentation in the design and rating of its products. OneBeacon's objective is to underwrite only profitable business without regard to market share or premium growth. OneBeacon's personal and commercial lines insurance products include the following:

**Automobile:** consists of physical damage and liability coverage. Automobile physical damage insurance covers loss or damage to vehicles from collision, vandalism, fire, theft or other causes. Automobile liability insurance covers bodily injury of others, damage to their property and costs of legal defense resulting from a collision caused by the insured.

**Homeowners:** covers losses to an insured's home, including its contents, as a result of weather, fire, theft and other causes and losses resulting from liability for acts of negligence by the insured or the insured's immediate family. OneBeacon also offers identity theft resolution assistance and identity theft expense reimbursement coverage as part of its homeowners policies.

**Commercial property:** covers losses to a business' premises, inventory and equipment as a result of weather, fire, theft and other causes.

**General liability:** covers businesses for any liability resulting from bodily injury and property damage arising from its general business operations, accidents on its premises and the products it manufactures or sells.

**Umbrella:** supplements existing insurance policies by covering losses from a broad range of insurance risks in excess of coverage provided by the primary insurance policy up to a specified limit.

**Workers compensation:** covers an employer's liability for injuries, disability or death of employees, without regard to fault, as prescribed by state workers compensation law and other statutes.

**Multi-peril:** a package policy sold to small to mid-sized insureds or to members of trade associations or other groups that includes general liability insurance and commercial property insurance.

**Inland marine:** covers property that may be in transit or held by a bailee at a fixed location, movable goods that are often stored at different locations or property with an unusual antique or collector's value.

Net written premiums in OneBeacon's other lines of business are primarily from reciprocal insurance exchanges administered by OneBeacon and premiums written during 2003 under the Liberty Agreement (as defined below).

On November 1, 2001, OneBeacon transferred its regional agency business, agents and operations in 42 states and the District of Columbia to Liberty Mutual Insurance Group ( Liberty Mutual ) pursuant to a renewal rights agreement (the Liberty Agreement ). The renewal rights under the Liberty Agreement expired on October 31, 2003. As a result, OneBeacon did not write any new premiums in 2005 or 2004 under the Liberty Agreement, but recorded earned premium in 2004 from policies written under the Liberty Agreement in 2003.

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For the twelve months ended December 31, 2005, 2004 and 2003, OneBeacon's net written premiums by line of business were as follows:

Net written premiums by line of business (\$ in millions)	Year Ended December 31,		
	2005	2004	2003
Specialty	\$ 840.2	\$ 848.5	\$ 733.7
Personal	618.7	724.7	676.8
Commercial	610.9	807.1	426.7
Other lines	51.3	78.8	135.3
Total	\$ 2,121.1	\$ 2,459.1	\$ 1,972.5

*Specialty Lines*

OneBeacon's specialty businesses include AutoOne, medical errors and omissions (offered through OneBeacon Professional Partners, OBPP), ocean marine (offered through International Marine Underwriters, IMU), agricultural (Agri), excess and surplus lines property business (offered through OneBeacon Specialty Property, OBSP), tuition reimbursement (offered through A.W.G. Dewar, Inc., Dewar) and other specialty products. OneBeacon offered additional rural and farm related products through National Farmers Union Property and Casualty Company (NFU) until its sale on September 30, 2005.

For the twelve months ended December 31, 2005, 2004 and 2003, OneBeacon's specialty lines net written premiums were as follows:

Specialty lines net written premiums (\$ in millions)	Year Ended December 31,		
	2005	2004	2003
AutoOne	\$ 248.0	\$ 263.1	\$ 233.8
OBPP	149.5	119.5	68.7
IMU	133.6	136.5	125.7
NFU (sold on September 30, 2005)	132.5	178.5	169.0
Agri	84.0	83.6	84.0
Dewar	45.6	44.6	43.4
OBSP	43.6	19.2	
Other	3.4	3.5	9.1
Total specialty lines	\$ 840.2	\$ 848.5	\$ 733.7

**AutoOne.** As a condition of its license to write automobile business within most states, an insurance carrier is obligated by statute to accept future assignments from the assigned risk plan for that state. Assigned risk plans create a residual insurance market that provides personal automobile insurance for those who cannot otherwise obtain it in the voluntary market. Insurance carriers that are subject to assignments may contractually satisfy their assigned risk obligation by transferring their assignments to another insurance company or by utilizing various credits offered in New York and certain other states (i.e. take-out, territorial and youthful driver credits).

The process of transferring assigned risk obligations for personal auto is called Limited Assigned Distribution or LAD and the companies that assume these obligations are called LAD servicing carriers. The process of transferring assigned risk obligations for commercial auto is called Commercial Limited Assigned Distribution or CLAD and the companies that assume this obligation are called CLAD servicing carriers. Numerous states have similar programs for personal and commercial automobile assignments. AutoOne has launched a program to expand its

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services into an additional twelve states for 2006. With this expansion, AutoOne will provide LAD and/or CLAD services in all twenty-two states where such obligations may be assumed by a servicing carrier for a negotiated rate.

In addition to LAD and CLAD services, AutoOne also writes voluntary take-out business under NYAIP rules, whereby policies previously written through the assigned risk plan are taken out of the assigned risk pool and written voluntarily. AutoOne receives credits for taking these policies out of the pool. These credits may be utilized to reduce AutoOne's assigned risk quota obligations, or they may be sold to other carriers to reduce their quota obligations. In 2005, AutoOne wrote more take-out business than all other carriers in New York combined.

In late 2004, AutoOne introduced a multi-tiered private passenger auto product in New York. This sophisticated product utilizes underwriting tiers to move the policy premium rates higher or lower based on underwriting rules and risk characteristics. The tiered structure is a key element in the design, as it provides the flexibility needed to adjust to changing market and competitor conditions.

**OBPP.** OneBeacon entered into the professional liability markets in 2002 through OBPP, which provides insurance and excess of loss coverage to the healthcare industry, including hospital professional liability ( HPL ), managed care errors and omissions ( MCE&O ) and HMO reinsurance. Additionally, OBPP provides directors and officers liability coverage and medial liability coverage. In June 2005, OneBeacon acquired the renewal rights to the HPL and MCE&O business of Chubb Specialty. In May 2005, OBPP added smaller and middle market media liability insurance capabilities by acquiring First Media Insurance Specialists, Inc. These transactions added \$35 million of net written premium in 2005.

**IMU.** IMU offers insurance products that specialize in the ocean marine marketplace. IMU's products include coverage for cargo, hull, yacht, marina and primary and excess liability. IMU is a franchise with an extensive history of profitability and outperforming the industry. The business is operated through nine regional offices throughout the United States providing local expertise and decision making.

**NFU.** On September 30, 2005, OneBeacon sold NFU to QBE Insurance Group for approximately \$138 million, which resulted in a pre-tax gain of \$26 million. The transaction included NFU's wholly-owned subsidiary, United Security Insurance Company.

**Agri.** Agri specializes in commercial farm and ranch and commercial agricultural package policies. Agri is a leading agricultural insurer focused on twelve core states and select targeted commercial agricultural segments. Marketing is focused primarily on southern states stretching from Kentucky to Arizona, and the west coast. Agri targets commercial agricultural segments that are low-to-moderate hazardous risks, including seed merchants, feedlots, wholesale nurseries, livestock auction yards and fruit and vegetable growers, packers and shippers.

**Dewar.** Dewar, which has offered tuition reimbursement insurance since 1930, provides customized policies to a large number of the leading independent schools and colleges in North America. Dewar is the originator of the Tuition Refund Plan, a means of protecting schools and parents from the financial consequences of withdrawals and dismissals.



**OBSP.** During 2004, OneBeacon entered the excess and surplus lines property business through OBSP, which markets products through brokers in all fifty states. OBSP's products offer attachment points and policy limits tailored to specific business-class and market conditions. Target classes include habitational risks (e.g., apartments and condominiums), municipalities and school districts, real estate and related classes (e.g., offices buildings, shopping centers), retail, wholesale (e.g., warehousing), builders risks and other inland marine classes. OBSP is exposed to large catastrophes, like hurricane Katrina, that cause losses to insured property in excess of attachment points in its policies. OBSP manages its catastrophic wind, earthquake and terrorism risks within the OneBeacon catastrophe management programs (see "**Reinsurance Protection**" below), including individual risk and portfolio loss modeling and reinsurance protection.

*Personal Lines*

OneBeacon's personal lines include automobile, homeowners and package products (package products are combination policies offering home and automobile coverage with optional umbrella, boatowners and other coverages). OneBeacon's mix of personal lines products between automobile and homeowners, including package, was 64% and 28%, respectively, of personal lines' 2005 net written premium, compared to 67% and 25%, respectively, during 2004 and 63% and 30%, respectively, during 2003. OneBeacon writes the majority of its personal business in New York, Massachusetts and Maine.

In 2004, OneBeacon launched OneChoice, a multi-tiered product suite that enables OneBeacon to offer a broader range of coverages to a full spectrum of customers through more sophisticated pricing models that have a greater statistical correlation between historical loss experience and price than traditional pricing models. This product was initially launched in the Northeast. During 2005, in addition to expanding its OneChoice product within its core Northeast territory by rolling out additional products in Maine, New Jersey, Massachusetts and New York, OneBeacon also expanded its OneChoice product into Arizona. In addition, a surplus lines operation became operational in 2005, with an initial focus on high value homes.

#### *Commercial Lines*

OneBeacon's commercial lines products principally include multi-peril, commercial automobile and workers compensation, which represented 52%, 23% and 11%, respectively, of commercial lines' 2005 net written premium, compared to 54%, 23% and 14%, respectively, during 2004 and 55%, 23% and 8%, respectively, during 2003.

In late 2004, OneBeacon's commercial lines operation was separated into middle-market and small-business divisions to enable a specialized focus in each market and to recognize the difference in product needs, customers and service requirements. In 2005, OneBeacon's middle-market and small-business operations represented 87% and 13% of commercial lines net written premium, respectively.

The middle-market division offers total protection for a broad range of mid-size businesses and industries. Tailored products and customized risk control and claims services are a focus of this division. In 2005, OneBeacon continued to be segment focused through its middle-market operations with 60% of its net written premium in segmented industries. In addition, OneBeacon grew its inland marine net written premium by 37% over 2004. Inland marine now represents 5% of total middle-market net written premium as compared to only 3% in 2004.

The small-business operation offers package, auto, workers compensation and umbrella policies typically to small businesses with account premium less than \$25,000 and less than 25 employees. Target programs are in the office, service and retail classes. During 2005, OneBeacon expanded its small business offering products into eight additional states.

On March 31, 2004, OneBeacon acquired Atlantic Specialty Insurance Company (Atlantic Specialty), a subsidiary of Atlantic Mutual Insurance Company (Atlantic Mutual), and the renewal rights to Atlantic Mutual's segmented commercial insurance business, including the unearned premiums on the acquired book (the Atlantic Specialty Transaction). The overall gross written premium for this book of business totaled \$404 million. This transaction has allowed OneBeacon to sell a highly segmented product to small and mid-sized companies on an industry basis. These select industries include, but are not limited to technology, professional services, printers and wholesalers.

During the third quarter of 2004, OneBeacon entered into an agreement to sell the renewal rights to most of its non-Atlantic Mutual New York commercial business to Tower Insurance Group. As a result of this transaction, approximately \$110 million of premiums written in 2004 were subject to this renewal rights agreement in 2005.

#### *Other Lines*

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OneBeacon's other lines include the results of insurance reciprocals that are included in OneBeacon's GAAP results and also business assumed under the Liberty Agreement.

Reciprocals are policyholder-owned insurance associations. In 2002, OneBeacon formed New Jersey Skylands Management LLC to provide management services for a fee to New Jersey Skylands Insurance Association, a reciprocal, and its wholly-owned subsidiary New Jersey Skylands Insurance Company (together, New Jersey Skylands Insurance). New Jersey Skylands Insurance began writing personal automobile coverage for new customers in August 2002. During 2004, OneBeacon formed Houston General Management Company to provide management services for a fee to another reciprocal, Houston General Insurance Exchange. In November 2005, Houston General Insurance Exchange commenced writing business in Arizona using the full suite of OneChoice products (auto, home and package). OneBeacon has no ownership interest in New Jersey Skylands Insurance or Houston General Insurance Exchange. As a result of accounting literature changes, OneBeacon began consolidating the results of reciprocals on March 31, 2004 (See **Note 15 - "Variable Interest Entities"** in the accompanying Consolidated Financial Statements). Net written premiums of New Jersey Skylands Insurance and Houston General Insurance Exchange that were included in OneBeacon's results totaled \$44 million and \$75 million in 2005 and 2004, respectively.

## Geographic Concentration

OneBeacon's net written premiums are derived solely from business produced in the United States. Business from specialty, personal and commercial lines was produced in the following states:

Specialty, personal and commercial net written premiums by state	Year Ended December 31,		
	2005	2004	2003
New York	27%	30%	36%
Massachusetts	17	17	20
New Jersey	9	9	3
California	7	8	2
Maine	6	6	2
Connecticut	5	5	5
Other (1)	29	25	32
Total	100%	100%	100%

(1) No individual state is greater than 3% of specialty, personal and commercial net written premiums for the years ended December 31, 2005, 2004 and 2003.

## Marketing

OneBeacon offers its products through a combination of independent agents, regional and national brokers and wholesalers. In total, OneBeacon has approximately 2,000 agency and distribution relationships. No agent or broker produced more than 2% of OneBeacon's premiums during 2005.

OneBeacon's specialty businesses are located in separate locations, logistically appropriate to their target markets. AutoOne issues its assigned risk (LAD and CLAD) business through independent agents and brokers in its operating states. In New York, AutoOne generates takeout credits by writing policies from select insurance brokers that were previously in the NYAIP, and sells these credits to insurance companies subject to NYAIP assignments. AutoOne markets its LAD and CLAD services and NY takeout credits directly to insurance carriers seeking assigned risk solutions. OBPP distributes its products through selected national and regional brokers and agents. IMU distributes its products through a network of select agents that specialize in the ocean marine business. Agri distributes its products through independent agencies. OBSP's excess property solutions are provided primarily through surplus lines wholesalers. Dewar's affiliate, A.W.G. Dewar Agency, distributes the tuition refund products to independent schools and colleges throughout North America. Through these distribution channels, OneBeacon leverages its knowledge about specialty markets to provide products and services that are tailored to meet customer needs.

OneBeacon distributes its personal and commercial lines products through select independent insurance agents. OneBeacon believes that independent agents provide complete assessments of their clients' needs, which results in appropriate coverages and prudent risk management. OneBeacon believes that independent agents will continue to be a significant force in overall industry premium production and management intends to increase the cross-selling of specialty, commercial and personal business among its top agents and brokers.

**Underwriting and Pricing**

OneBeacon believes that there must be a realistic expectation of attaining an underwriting profit on all the business it writes as well as a demonstrated fulfillment of that expectation over time. Adequate pricing is a critical component to the achievement of an underwriting profit and requires a disciplined approach towards pricing insurance products. Inadequate pricing can be caused by pressures from: (1) insurance companies selling their products at rates less than those acceptable to OneBeacon because they either underestimate ultimate claim costs or overestimate the amount of investment income and investment gains they will earn on premiums collected before claims are paid, (2) insurance companies willing to accept a lower return on investment for their stakeholders than OneBeacon, (3) insurance companies seeking to increase revenues and market share by reducing the price of their products beneath levels acceptable to OneBeacon, (4) the emergence and continued growth of competitors that have lower cost structures, and (5) state regulation, legislation and judicial mandates.

Since 2003, OneBeacon has used tiered rating plans in both its personal and commercial lines that permit OneBeacon to offer more tailored price quotes to its customers based on underwriting criteria applicable to each tier. As a result, OneBeacon now has the flexibility to renew expiring policies into the appropriate tier rather than being forced to choose to either renew the policy at the same base rate or cancel the policy. Management believes that this significant improvement in the accuracy and precision of OneBeacon's rate plans moves it toward the pricing sophistication of the best insurance underwriters in the market.

These tiers are just one example of OneBeacon's segmented underwriting and pricing strategy. Segmentation is a key driver of OneBeacon's success in specialty lines and is being carried over into personal and commercial lines. OneBeacon develops proprietary knowledge about the industry, class and risk characteristics of its customers, which provides it with a competitive edge when offering terms and conditions on individual accounts. OneBeacon believes this will deliver superior returns versus a more generalist underwriting approach.

OneBeacon also monitors pricing activity on a weekly basis and regularly measures usage of tiers, credits, debits and limits. In addition, it regularly updates base rates to achieve targeted returns on surplus and attempts to shift writings away from lines and classes where pricing is inadequate. Lastly, OneBeacon expends considerable effort to measure and verify exposure bases and values.

## **Competition**

Property and casualty insurance is highly competitive and extensively regulated by state insurance departments. In specialty lines, OneBeacon competes with numerous regional and national insurance companies, most notably The Chubb Corporation, American International Group, The St. Paul Travelers Companies and the regional Farm Bureaus. In personal and commercial lines, OneBeacon competes with numerous regional and national insurance companies, most notably The St. Paul Travelers Companies, Zurich Insurance Group, CNA Financial, the Hartford Financial Services Group, The Hanover Insurance Group, W.R. Berkley Corporation, The Chubb Corporation, Progressive Insurance, Allstate Insurance and Liberty Mutual. The more significant competitive factors for most insurance products offered by OneBeacon are price, product terms and claims service. OneBeacon's underwriting principles and dedication to independent agency distribution are unlikely to make it the low-cost provider in most markets. However, while it is often difficult for insurance companies to differentiate their products to consumers, OneBeacon believes that its dedication to providing superior product offerings, expertise and local talent, claims service and disciplined underwriting provide a competitive advantage over typical low-cost providers.

## **Claims Management**

Effective claims management is a critical factor in achieving satisfactory underwriting results. OneBeacon maintains an experienced staff of appraisers, medical specialists, managers, attorneys and field adjusters strategically located throughout its operating territories. OneBeacon also maintains a special investigative unit designed to detect insurance fraud and abuse, and support efforts by regulatory bodies and trade associations to curtail the cost of fraud.

In 2005, OneBeacon completed several operational changes in the claims department that began in 2004. Claims are now separately organized by specialty, commercial, personal and run-off operations. This segmented approach has allowed OneBeacon to better identify and manage claims handling costs. In addition, a shared service unit was established to better manage costs related to both staff and vendors. OneBeacon has also introduced a total claims cost management program that gives equal importance to controlling claims handling costs, legal expenses and claims payments, enabling OneBeacon to lower its overall claims handling costs.

OneBeacon's claims department utilizes a modern claims workstation that records reserves, payments and adjuster activity and assists each claim handler in evaluating bodily injury claims, determining liability and identifying fraud. OneBeacon's commitment and performance in fighting insurance fraud has reduced claim costs and aided law enforcement investigations. Under OneBeacon's Staff Counsel Program, in-house attorneys defend the majority of new lawsuits, which has resulted in savings when compared to the cost of using outside counsel. In addition, OneBeacon's internal legal bill audit team has contributed to savings by reducing legal invoices submitted by outside counsel.

Calendar year reported claims in OneBeacon's run-off operations were 3,300 in 2005 compared to 5,900 in 2004, a 44% reduction. Total open claims for run-off operations were 8,800 at December 31, 2005 compared to 15,300 at December 31, 2004, a 42% reduction. These numbers included all of the claims that were previously handled by Liberty Mutual as a Third Party Administrator ( TPA ). Most of OneBeacon's claims for run-off operations are handled by in-house adjusters.

National Indemnity Company ( NICO ) is used as a TPA for asbestos and environmental claims reinsured under the NICO Cover (as defined on page 12). OneBeacon claims department personnel are consulted by NICO on major claims. As with all TPAs, claims department personnel perform claim audits on NICO to ensure their controls, processes and settlements are appropriate. For more information regarding OneBeacon's A&E exposures, see the Asbestos and Environmental Reserves discussion included in **CRITICAL ACCOUNTING ESTIMATES** in **Management's Discussion and Analysis of Financial Condition and Results of Operations** .

## **Terrorism**

Since the terrorist attacks of September 11, 2001 (the Attacks ), OneBeacon has sought to mitigate the risk associated with any future terrorist attacks by limiting the aggregate insured value of policies in geographic areas with exposure to losses from terrorist attacks. This is accomplished by either limiting the total insured values exposed, or, where applicable, through the use of terrorism exclusions.

On November 26, 2002, President Bush signed the Terrorism Risk Insurance Act (the Terrorism Act ) establishing a federal backstop for commercial property and casualty losses, including workers compensation, resulting from acts of terrorism by or on behalf of any foreign person or foreign interest. On December 22, 2005, the United States government extended the Terrorism Act, which was set to expire on December 31, 2005, for two more years. The Terrorism Act requires primary commercial insurers to make terrorism coverage available and provides Federal protection for certain losses above both individual company retention and industry retention levels. The following types of coverage are excluded from the program; commercial automobile, burglary and theft, surety, farm-owners multi-peril and all professional liability coverage except directors and officers coverage.

OneBeacon estimates its individual retention level for commercial policies subject to the Terrorism Act to be approximately \$150 million in 2006. The aggregate industry retention levels are \$25 billion in 2006 and \$27.5 billion in 2007. The Federal government will pay 90% of covered terrorism losses that exceed OneBeacon's or the industry's retention levels in 2006, and 85% of such losses in 2007, up to a total of \$100 billion in each year.

OneBeacon's current property and casualty catastrophe reinsurance programs provide coverage for non-certified events as defined under the Terrorism Act, provided such losses are not the result of a nuclear, biological or chemical attack. See the discussion in the **Reinsurance Protection** section below for a further description of OneBeacon's catastrophe program.

OneBeacon closely monitors and manages its concentration of risk by geographic area. OneBeacon's strategy is to control its exposures so that its total probable maximum loss ( PML ) from a terrorism event within any half-mile radius in a metropolitan area or target risk will not exceed \$200 million. (PML is a modeling technique that measures a company's catastrophic exposure as the maximum probable loss from a defined loss event scenario.) The financial exposure of potential new business is evaluated when it is located in an area of existing concentration or individually presents significant terrorism exposure. Additionally, formal reports are generated quarterly to help validate that OneBeacon's terrorism exposures do not exceed limits specified within its corporate standards. As a result, OneBeacon believes that it has taken appropriate actions to mitigate its exposure to losses from terrorist attacks and will continue to monitor its terrorism exposure in the future. Nonetheless, risks insured by OneBeacon, including those covered by the Terrorism Act, remain exposed to terrorist attacks and the possibility remains that losses resulting



from future terrorist attacks could prove to be material to the Company.

## Reinsurance Protection

In the ordinary course of its business, OneBeacon purchases reinsurance from high-quality, highly rated, third party reinsurers in order to provide diversification of its business and minimize loss from large risks or catastrophic events.

The timing and size of catastrophe losses are unpredictable and the level of losses experienced in any year could be material to OneBeacon's operating results and financial position. Examples of catastrophes include losses caused by earthquakes, wildfires, hurricanes and other types of storms and terrorist acts. The extent of losses caused by catastrophes is both a function of the amount and type of insured exposure in an area affected by the event and the severity of the event. OneBeacon uses PML forecasting to quantify its exposure to catastrophic losses. OneBeacon continually assesses and implements programs to manage its exposure to catastrophe losses through individual risk selection and by limiting its concentration of insurance written in catastrophe-prone areas, such as coastal regions. In addition, OneBeacon imposes wind deductibles on existing coastal windstorm exposures. OneBeacon believes that its largest natural catastrophe exposures, based on a 250-year PML single event scenario, are Northeastern United States windstorm and California earthquake.

OneBeacon seeks to further reduce its exposure to catastrophe losses through the purchase of catastrophe reinsurance. Effective July 1, 2005, OneBeacon renewed its normal property catastrophe reinsurance program to cover its full estimated PML (one-in-250 year) through June 30, 2006. Under that cover, the first \$200 million of losses resulting from any single catastrophe are retained by OneBeacon and losses from a single event in excess of \$200 million and up to \$850 million are reinsured for 100% of the loss. In the event of a catastrophe, OneBeacon's property catastrophe reinsurance program is reinstated for the remainder of the original contract term by paying a reinstatement premium that is based on the percentage of coverage reinstated and the original property catastrophe coverage premium.

OneBeacon's property catastrophe reinsurance program does not cover personal or commercial property losses resulting from nuclear, biological or chemical terrorist attacks. The program covers personal property losses resulting from other types of terrorist attacks, and commercial property losses resulting from other types of domestic terrorist attacks or events not certified under the Terrorism Act.

OneBeacon also purchases individual property reinsurance coverage for certain risks to reduce large loss volatility. The property-per-risk reinsurance program reinsures losses in excess of \$5 million up to \$75 million. Individual risk facultative reinsurance may be purchased above \$75 million where OneBeacon deems it appropriate. The property-per-risk treaty also reinsures losses in excess of \$10 million up to \$75 million on an individual risk basis for terrorism losses. However, nuclear, biological and chemical events are not covered.

OneBeacon also maintains a casualty reinsurance program that provides protection for catastrophe losses involving workers compensation, general liability, automobile liability or umbrella liability in excess of \$6 million up to \$81 million. This program provides coverage for either certified or non-certified terrorism losses but does not provide coverage for losses resulting from nuclear, biological or chemical attacks.

In connection with the OneBeacon Acquisition, Aviva caused OneBeacon to purchase reinsurance contracts with two reinsurance companies rated AAA (Extremely Strong, the highest of twenty-one ratings) by Standard & Poor's and A++ (Superior, the highest of fifteen ratings) by A.M. Best: a full risk-transfer cover from NICO for up to \$2.5 billion in old asbestos and environmental claims (the NICO Cover) and an adverse development cover from General Reinsurance Corporation (GRC) for up to \$400 million on additional losses occurring in accident years 2000 and prior (the GRC Cover).

Reinsurance contracts do not relieve OneBeacon of its obligation to its policyholders. Therefore, collectibility of balances due from its reinsurers is critical to OneBeacon's financial strength. See **Note 4 Third Party Reinsurance** in the accompanying Consolidated Financial Statements for a discussion of OneBeacon's top reinsurers.

### Loss and Loss Adjustment Expense Reserves

OneBeacon establishes loss and LAE reserves that are estimates of amounts needed to pay claims and related expenses in the future for insured events that have already occurred. The process of estimating reserves involves a considerable degree of judgment by management and, as of any given date, is inherently uncertain. See **CRITICAL ACCOUNTING ESTIMATES** in **Management's Discussion and Analysis of Financial Condition and Results of Operations** for a full discussion regarding OneBeacon's loss reserving process.

The following information presents (1) OneBeacon's reserve development over the preceding ten years and (2) a reconciliation of reserves in accordance with accounting principles and practices prescribed or permitted by insurance authorities (Statutory basis) to such reserves determined in accordance with GAAP, each as prescribed by Securities Act Industry Guide No. 6.

Section I of the ten year table shows the estimated liability that was recorded at the end of each of the indicated years for all current and prior accident year unpaid losses and LAE. The liability represents the estimated amount of losses and LAE for claims that were unpaid at the balance sheet date, including incurred but not reported (IBNR) reserves. In accordance with GAAP, the liability for unpaid losses and LAE is recorded in the balance sheet gross of the effects of reinsurance with an estimate of reinsurance recoverables arising from reinsurance contracts reported separately as an asset. The net balance represents the estimated amount of unpaid losses and LAE outstanding as of the balance sheet date, reduced by estimates of amounts recoverable under reinsurance contracts.

Section II shows the re-estimated amount of the previously recorded net liability as of the end of each succeeding year. Estimates of the liability for unpaid losses and LAE are increased or decreased as payments are made and more information regarding individual claims and trends, such as overall frequency and severity patterns, becomes known. Section III shows the cumulative net (deficiency)/redundancy representing the aggregate change in the liability from original balance sheet dates and the re-estimated liability through December 31, 2005. Section IV shows the re-estimated gross liability and re-estimated reinsurance recoverables through December 31, 2005. Section V shows the cumulative amount of net losses and LAE paid relating to recorded liabilities as of the end of each succeeding year.

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OneBeacon Loss and LAE (1), (3), (4)  
Years Ended December 31,

(\$ in millions)	1995	1996	1997	1998 (2)(5)	1999	2000	2001	2002	2003	2004	2005
I. Liability for unpaid losses and LAE:											
Gross balance	\$ 5,844.4	\$ 5,804.4	\$ 5,655.9	\$ 6,944.0	\$ 6,368.8	\$ 6,982.7	\$ 8,425.2	\$ 7,630.5	\$ 6,241.2	\$ 5,475.5	\$ 5,713.4
Less: reins. recoverables on unpaid losses and LAE	(1,307.4)	(1,260.4)	(1,159.2)	(1,651.9)	(1,285.6)	(1,276.4)	(3,609.7)	(3,560.6)	(2,984.0)	(2,714.7)	(3,382.0)
Net balance	\$ 4,537.0	\$ 4,544.0	\$ 4,496.7	\$ 5,292.1	\$ 5,083.2	\$ 5,706.3	\$ 4,815.5	\$ 4,069.9	\$ 3,257.2	\$ 2,760.8	\$ 2,331.4
II. Net liability re-estimated as of:											
1 year later	4,584.7	4,627.8	5,370.1	5,305.3	5,901.2	4,815.8	4,872.9	4,216.7	3,357.4	2,855.8	
2 years later	4,667.1	5,476.0	5,424.7	5,985.4	5,013.5	4,913.7	5,155.0	4,337.0	3,478.4		
3 years later	5,460.6	5,549.0	5,965.0	5,002.8	5,001.5	5,384.7	5,244.0	4,451.2			
4 years later	5,510.6	5,924.8	4,980.5	4,932.1	5,297.5	5,429.3	5,325.3				
5 years later	5,779.5	4,948.0	4,911.8	5,117.6	5,243.4	5,482.0					
6 years later	4,794.7	4,900.4	5,069.3	5,006.1	5,279.5						
7 years later	4,749.4	5,028.9	4,902.3	5,017.7							
8 years later	4,871.8	4,867.4	4,910.2								
9 years later	4,714.2	4,868.0									
10 years later	4,713.6										
III. Cumulative net (deficiency)/redundancy											
Percent (deficient)/redundant	(3.9)%	(7.1)%	(9.2)%	5.2%	(3.9)%	3.9%	(10.6)%	(9.4)%	(6.8)%	(3.4)%	%
IV. Reconciliation of net liability re-estimated as of the end of the latest re-estimation period (see II. above):											
Gross re-estimated liability	8,777.5	8,931.1	8,892.2	9,486.9	9,489.6	9,667.7	9,934.7	9,007.4	7,341.4	6,364.0	
Less: gross re-estimated reinsurance recoverable	(4,063.9)	(4,063.1)	(3,982.0)	(4,469.2)	(4,210.1)	(4,185.6)	(4,609.4)	(4,556.2)	(3,863.1)	(3,508.2)	
Net re-estimated liability	\$ 4,713.6	\$ 4,868.0	\$ 4,910.2	\$ 5,017.7	\$ 5,279.5	\$ 5,482.1	\$ 5,325.3	\$ 4,451.2	\$ 3,478.3	\$ 2,855.8	\$
V. Cumulative net amount of liability paid through:											
1 year later	1,476.6	1,594.8	1,684.3	1,815.2	1,966.5	2,007.9	1,892.0	1,656.9	1,463.7	1,143.8	
2 years later	2,372.6	2,621.3	2,732.5	2,954.8	3,112.6	3,213.8	3,101.3	2,834.7	2,345.0		
3 years later	3,083.3	3,331.1	3,515.0	3,702.2	3,882.3	4,057.3	4,040.5	3,579.0			
4 years later	3,571.3	3,872.2	4,028.8	4,125.9	4,394.5	4,677.2	4,622.4				
5 years later	3,961.5	4,225.0	4,282.8	4,421.0	4,736.0	5,050.4					
6 years later	4,219.2	4,398.1	4,464.4	4,627.2	4,966.0						
7 years later	4,329.4	4,516.6	4,584.6	4,780.4							
8 years later	4,416.0	4,609.4	4,694.6								
9 years later	4,485.7	4,691.3									
10 years later	4,555.6										

- (1) In 1998, OneBeacon was formed as a result of a pooling of interests between Commercial Union and General Accident. All historical balances have been restated as though the companies had been merged throughout the periods presented.
- (2) OneBeacon acquired Houston General Insurance Company in 1998 and contributed it to Houston General Insurance Exchange in 2005. All liabilities related to this entity have been shown from 1998 forward in this table as it is still consolidated by OneBeacon.
- (3) This table reflects the effects of the NICO Cover and the GRC Cover as if they had been in effect for all periods presented.
- (4) OneBeacon became a wholly-owned subsidiary of White Mountains during 2001. Reserve development for the years ended 1995 through 2000 reflects development on reserves established before White Mountains consolidated OneBeacon's results.
- (5) OneBeacon acquired NFU in 1998 and sold it during 2005. All liabilities related to this entity have been shown from 1998 through 2004.

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The cumulative net (deficiency)/redundancy in the table above reflects reinsurance recoverables recorded in connection with the OneBeacon Acquisition under the NICO Cover and the GRC Cover. See **Note 4 Third Party Reinsurance** in the accompanying Consolidated Financial Statements for a description of the NICO Cover and the GRC Cover. These covers apply to losses incurred in 2000 and prior years. As a result, they have the effect of significantly increasing OneBeacon's reinsurance recoverables in 2001 and 2002 and reducing its reserve deficiency for each of the years presented prior to the OneBeacon Acquisition by the amount of the reserves ceded at the time these covers were purchased. See **Asbestos and Environmental Reserves** under **CRITICAL ACCOUNTING ESTIMATES** in **Management's Discussion and Analysis of Financial Condition and Results of Operations** for a discussion of the impact of the NICO Cover on OneBeacon's net loss and LAE reserve position. The table presented below represents OneBeacon's cumulative net deficiency without regard to the NICO Cover and the GRC Cover.

(\$ in millions)	Years Ended December 31,										
	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Cumulative net deficiency adjusted for the NICO Cover and the GRC Cover	\$ (2,277.0)	\$ (2,447.8)	\$ (2,573.0)	\$ (1,938.0)	\$ (2,490.8)	\$ (2,194.2)	\$ (862.7)	\$ (734.4)	\$ (574.2)	\$ (448.0)	\$
Percent deficient	(50.2)%	(53.9)%	(57.2)%	(36.6)%	(49.0)%	(38.5)%	(17.9)%	(18.0)%	(17.6)%	(16.2)%	%

The following table reconciles loss and LAE reserves determined on a Statutory basis to loss and LAE reserves determined in accordance with GAAP at December 31, as follows:

(\$ in millions)	December 31,		
	2005	2004	2003
Statutory reserves	\$ 4,253.4	\$ 4,413.4	\$ 5,085.5
Reinsurance recoverable on unpaid losses and LAE (1)	1,455.2	1,046.8	1,197.5
Reserves allocated from other segments, net	41.6	44.5	
Other (2)	(36.8)	(29.2)	(41.8)
GAAP reserves	\$ 5,713.4	\$ 5,475.5	\$ 6,241.2

(1) Represents adjustments made to add back reinsurance recoverables included with the presentation of reserves under Statutory accounting.

(2) Primarily represents long-term workers compensation loss and LAE reserve discount recorded of \$36.8 million, \$36.1 million and \$38.0 million in 2005, 2004 and 2003 in excess of statutorily defined discount.

## WHITE MOUNTAINS RE

During 2004, White Mountains formed White Mountains Re, which combined Folksamerica, Fund American Reinsurance Company, Ltd. ( Fund American Re ) and WMU with the newly acquired Sirius to form a global reinsurance organization.

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White Mountains Re offers lead reinsurance capacity for property, casualty, accident & health, aviation and marine exposures on a world-wide basis and writes direct program insurance business through Sirius America. White Mountains Re also provides reinsurance advisory services through WMU, specializing in international property and marine excess reinsurance. White Mountains Re has offices in Belgium, Bermuda, Chicago, Connecticut, Dublin, Hamburg, London, Miami, New York, Singapore, Stockholm, Toronto and Zurich. At December 31, 2005 and 2004, White Mountains Re had \$8.5 billion and \$8.2 billion of total assets and \$1.9 billion and \$1.7 billion of shareholder's equity, respectively.



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Folksamerica is a multi-line property and casualty reinsurer that provides reinsurance to insurers primarily in the United States, Canada, Continental Europe, Latin America, the Caribbean and Japan. Folksamerica Re is rated A (Excellent, the third highest of fifteen ratings) by A.M. Best and A- (Strong, the seventh highest of twenty-one ratings) with a positive outlook by Standard & Poor's.

On April 16, 2004, White Mountains completed the Sirius Acquisition, through which the principal operating companies acquired were Sirius International and Sirius America. Stockholm-based Sirius International is a multi-line property and casualty reinsurer that provides reinsurance primarily in Europe, North America and Asia and is the largest reinsurance company domiciled in Scandinavia (based on gross written premiums). Sirius America is a U.S.-based insurer that specializes in primary insurance programs. Sirius International and Sirius America are both rated A (Excellent, the third highest of fifteen ratings) by A.M. Best. Sirius International is also rated A- (Strong, the seventh highest of twenty-one ratings) with a positive outlook by Standard & Poor's.

Effective October 1, 2003, White Mountains Re acquired renewal rights to the property and casualty treaty reinsurance business of CNA Reinsurance (CNA Re), a division of CNA Financial Corporation (the CNA Re Agreement). Under the terms of the CNA Re Agreement, White Mountains Re pays CNA Re a renewal commission on the premiums renewed over the two contract renewal periods subsequent to October 1, 2003.

In December 2001, White Mountains formed WMU, a reinsurance advisory company domiciled in Ireland. As part of a corporate reorganization, WMU established a sister company in Bermuda in June 2003. WMU provides reinsurance underwriting advice and reinsurance portfolio analysis services to both Folksamerica and Olympus Reinsurance Company Ltd. (Olympus). Prior to the Sirius Acquisition, WMU's Irish company, a specialist in handling non-marine property treaty excess of loss classes, expanded White Mountains Re's international profile, particularly in the United Kingdom, Continental Europe, Japan and Australia. WMU's Bermuda company specializes in excess reinsurance coverages for the marine and energy sector.

Since 1999, in addition to the transactions discussed above, White Mountains Re has made the following acquisitions:

On November 11, 2004, Sirius International acquired 100% of Denmark-based Tryg-Baltica Forsikring, internationalt forsikringsselskab A/S (Tryg-Baltica). Following the closing, White Mountains Re placed Tryg-Baltica into run-off, with select business renewed by Sirius International. White Mountains Re did not acquire any infrastructure or employees and is managing the company's run-off administration.

On March 31, 2004, Folksamerica acquired 100% of the Sierra Insurance Group companies (the Sierra Group). Subsequent to the acquisition, the Sierra Group companies, which previously wrote mainly workers compensation business, were placed into run-off and all of the acquired companies' run-off claims administration was transferred to TPAs working under White Mountains Re's direction.

In 2002, Folksamerica acquired 100% of Imperial Casualty and Indemnity Insurance Company, a company in run-off.

In 2001, Fund American Re acquired substantially all of the international reinsurance operations of Folksam International Insurance Company and Folksamerica acquired 100% of C-F Insurance Company, a company in run-off.

In 2000, Folksamerica acquired substantially all the reinsurance operations of Risk Capital Reinsurance

Company ( Risk Capital ) and 100% of PCA Property & Casualty Insurance Company ( PCA ), a company in run-off.

In 1999, Folksamerica acquired 100% of USF Re Insurance Co.

## Reinsurance Overview

Reinsurance is an arrangement in which a reinsurance company (the reinsurer) agrees to indemnify an insurance company (the ceding company) for all or a portion of the insurance risks underwritten by the ceding company under one or more insurance policies. Reinsurance can benefit a ceding company in a number of ways, including reducing exposure on individual risks, providing catastrophe protections from large or multiple losses, and assisting in maintaining acceptable capital levels as well as financial and operating leverage ratios. Reinsurance can also provide a ceding company with additional underwriting capacity by permitting it to accept larger risks and underwrite a greater number of risks without a corresponding increase in its capital or surplus. Reinsurers may also purchase reinsurance, known as retrocessional reinsurance, to cover their own risks assumed from primary ceding companies. Reinsurance companies often enter into retrocessional agreements for many of the same reasons that ceding companies enter into reinsurance agreements.

Reinsurance is generally written on a treaty or facultative basis. Treaty reinsurance is an agreement whereby the reinsurer assumes a specified portion or category of risk under all qualifying policies issued by the ceding company during the term of the agreement, usually one year. In the underwriting of treaty reinsurance, the reinsurer does not evaluate each individual risk and generally accepts the original underwriting decisions made by the ceding insurer. Treaty reinsurance is typically written on either a quota share or excess of loss basis. A quota share reinsurance treaty is an arrangement whereby a reinsurer assumes a predetermined proportional share of the premiums and losses generated on specified business. An excess of loss treaty is an arrangement whereby a reinsurer assumes losses that exceed an agreed retention of loss by the ceding company. Facultative reinsurance, on the other hand, is underwritten on a risk-by-risk basis, which allows the reinsurer to determine pricing for each exposure.

A significant period of time normally elapses between the receipt of reinsurance premiums and the payment of reinsurance claims. While premiums are generally paid to the reinsurer upon inception of coverage, the claims process is delayed and generally begins upon the occurrence of an event causing an insured loss followed by: (1) the reporting of the loss by the insured to the ceding company; (2) the reporting of the loss by the ceding company to the reinsurer; (3) the ceding company's adjustment and payment of the loss; and (4) the payment to the ceding company by the reinsurer. During this time, reinsurance companies generate investment income on premium receipts, consisting primarily of interest earned on fixed maturity investments and dividends earned on equity securities. The period of time between the receipt of premiums and the payment of claims is typically longer for a reinsurer than for a primary insurer. However, this difference is less significant for reinsurers like White Mountains Re that write large volumes of short-tailed coverage, such as property reinsurance.

## Classes of Business

White Mountains Re writes three main classes of reinsurance: property, liability and accident and health. White Mountains Re's net written premiums by class of business for the years ended December 31, 2005, 2004 and 2003 were as follows:

Business class (Millions)	Year Ended December 31,		
	2005	2004	2003
Property	\$ 567.4	\$ 432.1	\$ 314.6
Liability	403.4	524.5	450.7
Accident and Health	169.4	151.6	88.4
Other	163.9	138.1	32.0
Total	\$ 1,304.1	\$ 1,246.3	\$ 885.7

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White Mountains Re writes both treaty and facultative reinsurance, as well as direct business. The majority of White Mountains Re's premiums are derived from treaty reinsurance contracts both on a quota share and an excess of loss basis, which in 2005 amounted to 51% and 36%, respectively, of its total net written premiums, while direct business represented 13% of total net written premium.

During the years ended December 31, 2005, 2004 and 2003, White Mountains Re received no more than 10% of its gross reinsurance premiums from any individual ceding company. During the years ended December 31, 2005, 2004 and 2003, White Mountains Re received approximately 40%, 51% and 58%, respectively, of its gross reinsurance written premiums from three major, third-party reinsurance brokers as follows: (1) AON Re - 18%, 22% and 25%, respectively; (2) Benfield - 14%, 16% and 19%, respectively; and (3) Guy Carpenter - 8%, 13% and 14%, respectively.

### Geographic Concentration

White Mountains Re's net written premiums by geographic region for the years ended December 31, 2005, 2004 and 2003 were as follows:

Geographic region (Millions)	Year Ended December 31,		
	2005	2004	2003
United States	\$ 878.9	\$ 846.7	\$ 702.5
Europe	315.6	303.5	114.0
Canada, the Caribbean and Latin America	47.2	42.4	53.6
Asia and Other	62.4	53.7	15.6
Total	\$ 1,304.1	\$ 1,246.3	\$ 885.7

### Marketing

White Mountains Re, which conducts its reinsurance business through Folksamerica and Sirius International, obtains most of its reinsurance business from reinsurance brokers. Business submissions come from intermediaries that represent the ceding company or through submissions recommended by WMU. White Mountains Re considers both the intermediary and the ceding company to be its clients in any placement. White Mountains Re has developed strong business relationships over a long period of time with the management of many of its ceding companies. The process of placing an intermediary reinsurance program typically begins when a ceding company enlists the aid of a reinsurance intermediary in structuring a reinsurance program. Often the ceding company and the broker will consult with one or more lead reinsurers as to the pricing and contract terms for the reinsurance protection being sought. Once the ceding company has approved the terms quoted by the lead reinsurer, the broker will offer participation to qualified reinsurers until the program is fully subscribed.

White Mountains Re pays ceding companies a ceding commission under most quota share reinsurance treaties and some excess of loss reinsurance treaties. The ceding commission is generally based on the ceding company's cost of acquiring and administering the business being reinsured (commissions, premium taxes and certain miscellaneous expenses). Additionally, White Mountains Re pays reinsurance intermediaries commissions based on negotiated percentages of the premium they produce. The reinsurance intermediary's commissions constitute a significant portion of White Mountains Re's total acquisition costs.

As mentioned above, White Mountains Re also writes direct program business through Sirius America, which began its program insurance operations in 1999. Sirius America works with managing general agents to produce U.S. based liability, property and accident & health insurance programs for small and mid-sized commercial accounts. Sirius America establishes strict underwriting guidelines, closely monitors all exposures and performs periodic on-site audits of the managing general agents to confirm compliance with established guidelines and procedures.



## **Underwriting and Pricing**

White Mountains Re derives its business from a broad spectrum of ceding insurers including national, regional, specialty and excess and surplus lines writers, both in the United States and internationally. White Mountains Re determines which risks it accepts based on the anticipated underwriting results of the transaction, which are evaluated on a variety of factors including types of risk, the quality of the reinsured, the attractiveness of the reinsured's insurance rates and policy conditions and the adequacy of the proposed reinsurance terms.

White Mountains Re's underwriters and pricing actuaries perform reviews of the underwriting, pricing, and general underwriting controls of potential clients before quoting contract terms for its reinsurance products. White Mountains Re prices its products by assessing the desired return on the expected capital needed to write a given contract and by estimating future loss and LAE costs. White Mountains Re accepts contracts that are anticipated to generate sufficient returns on capital. White Mountains Re's pricing indications are based on a number of underwriting factors including historical results, analysis of exposure and estimates of future loss costs, a review of other programs displaying similar exposure characteristics, the primary insurer's underwriting and claims experience and the primary insurer's financial condition. Folksamerica's underwriters, actuaries and claims personnel perform regular audits to monitor ceding companies' risk selection, pricing and claim handling discipline. Sirius International's underwriters frequently communicate with ceding companies to discuss current terms and conditions. Additionally, White Mountains Re's finance staff reviews the financial stability and creditworthiness of certain ceding companies. Such reviews provide important input to support underwriting decisions.

White Mountains Re and other reinsurance companies have sought to mitigate the risk associated with future terrorist attacks in a similar manner as primary insurers. Since the Attacks, reinsurers have attained significant price increases across all lines of reinsurance in response to greater perceived policy exposures. Reinsurers do not have the stringent regulations with respect to contract terms and policy exclusions that are generally imposed on primary writers. For example, the Terrorism Act is not applicable to reinsurers. As a result, exclusions on reinsurance contracts are dictated by the marketplace. White Mountains Re evaluates terrorism exposure to its ceding company clients and applies exclusions as appropriate. For example, reinsurance written on commercial risks subsequent to the Attacks generally contain clauses that exclude acts of terrorism certified under the Terrorism Act. Reinsurance on personal risks written subsequent to the Attacks generally contains exclusions related to nuclear, biological and chemical attacks.

Following the 2004 and 2005 catastrophe activity, White Mountains Re enhanced its catastrophe underwriting process by significantly raising its provision for demand surge (i.e., the rise in costs from shortages of material and labor in regions affected by a catastrophe) and by employing a more conservative methodology to evaluate exposure than those that result from standard actuarial and modeling techniques. Reflecting the increasing capital costs associated with providing catastrophe protection, the marketplace is supporting an increase in the underwriting profit margin of catastrophe-exposed reinsurance contracts.

## **Claims Management**

White Mountains Re maintains a staff of experienced reinsurance claim specialists that work closely with reinsurance intermediaries to obtain specific claims information from its customers. Folksamerica's claims staff also regularly perform on site claim reviews to assess the reinsured's claim handling ability, including suggesting improvements, and reserving techniques. In addition, White Mountains Re's claims specialists review loss information provided by the reinsured for adequacy. The results of these claim reviews are shared with the actuaries and underwriters to ensure that they are making the correct assumptions in pricing products and that all relevant information is used in establishing loss reserves.

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White Mountains Re also uses TPAs for certain other claims, including the direct program business written by Sirius America and run-off claims related to the Sierra and PCA acquisitions. White Mountains Re's claims staff performs on-site claim audits of certain TPAs to ensure the propriety of the controls and processes over claims serviced by the TPA.



## Competition

In general, White Mountains Re competes for reinsurance business with other major global reinsurers, local reinsurers in certain markets and reinsurance divisions of direct insurance companies. Competition in the worldwide reinsurance market is influenced by a variety of factors, including financial strength ratings, prior history and relationships, as well as expertise and the speed at which the company has historically paid claims.

Through Folksamerica, White Mountains Re competes with all of the larger U.S. reinsurance companies. As reported by the Reinsurance Association of America (RAA) for the nine month period ending September 30, 2005, (the most recent data available), Folksamerica wrote approximately 5% of gross written premiums of all reinsurance companies that are viewed as direct competition. The reinsurance companies writing the largest portion of gross premiums in this period were: XL Reinsurance America (17%), Transatlantic Reinsurance Company (13%) and Everest Reinsurance Company (13%).

Through Sirius International, the largest reinsurance company domiciled in Scandinavia (based upon gross written premiums), White Mountains Re competes with many of the larger European and international reinsurance companies, including Munich Re, Swiss Re, Hannover Re, Lloyds, Partner Re and Everest Re.

White Mountains Re, through its operating subsidiaries, has a long history of close relationships with ceding companies and maintains a disciplined underwriting strategy which, among other things, focuses on writing more business when market terms and conditions are favorable and reducing business volume during soft markets when terms and conditions become less favorable. White Mountains Re also employs a multi-line approach, offering clients a wide range of reinsurance products to satisfy their risk management needs. Additionally, White Mountains Re's acquisition strategy has contributed to its growth. Since 1995, White Mountains Re has completed eleven acquisitions of other insurance and reinsurance organizations. In most cases the acquired entities were fundamentally sound, but were owned by organizations that no longer considered them core businesses.

## Catastrophe Risk Management

White Mountains Re has exposure to losses caused by hurricanes, earthquakes, winter storms, windstorms, terrorist acts and other catastrophic events. In the normal course of business, White Mountains Re regularly manages its concentration of exposures to catastrophic events, primarily by limiting concentrations of exposure to acceptable levels and, if necessary, purchasing reinsurance. In addition, White Mountains Re seeks terrorism exclusions in its reinsurance contracts, where applicable. White Mountains Re also uses a global catastrophe model that calculates its expected PML from several possible catastrophes. White Mountains Re believes that its largest natural catastrophe exposures, net of reinsurance and based on a 250-year PML single event scenario, are European winter storm, California earthquake, United States Atlantic Coast windstorm (i.e., Delaware to Florida) and United States Gulf Coast windstorm (i.e., Florida to Texas).

White Mountains Re's global catastrophe model is based on third party software models and internally developed models. White Mountains Re models and assesses each contract it writes for catastrophe exposure and uses the results in underwriting to ensure that the contracts it writes have an appropriate charge for assumed catastrophe risks.

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Catastrophe exposure modeling is inherently uncertain due to the model's reliance on a large number of data points. In particular, geographic and policy coverage data on the primary policies reinsured by White Mountains Re is essential. Accordingly, White Mountains Re's ability to accurately predict its catastrophe exposure is dependent on the quality and accuracy of data obtained from its clients.

Additionally, catastrophe modeling is dependent upon several broad economic and scientific assumptions, such as storm surge (i.e., the water that is pushed toward the shore by the force of a windstorm), demand surge and zone density (i.e., the percentage of insured perils that would be affected in a region by a catastrophe).

While catastrophe modeling is an important tool, White Mountains Re does not believe that it can be strictly relied upon to measure its catastrophe exposure. For example, the losses caused by Katrina for both the industry and White Mountains were substantially in excess of previously modeled losses, due to issues such as inadequate storm surge and demand surge assumptions in the models.

## Reinsurance Protection

During 2005, White Mountains Re's primary reinsurance protection was through quota share retrocessional arrangements with Olympus. Under these arrangements, for an override commission on premiums ceded, Folksamerica ceded up to 75% of substantially all of its short-tailed excess of loss business, mainly property and marine, and 50% of its proportional property business and Sirius International ceded 25% of its new and renewal short-tailed proportional and excess of loss business to Olympus. Additionally, White Mountains Re was to receive a profit commission with respect to the profitability of the business placed with Olympus. This profit commission arrangement is subject to a deficit carryforward whereby net underwriting losses from one underwriting year carryover to future underwriting years. As a result of the Gulf Coast hurricanes and several other significant loss events during the year, Olympus recorded substantial net underwriting losses in 2005. Accordingly, White Mountains Re did not record a profit commission from Olympus during 2005 and does not expect to record profit commissions from Olympus for the foreseeable future. During 2004, White Mountains Re recorded a profit commission of \$12.6 million.

Effective January 1, 2006, Sirius International no longer cedes any of its business to Olympus and Folksamerica renewed its quota-share reinsurance arrangements with Olympus on modified terms. Under its revised arrangements, for an override commission on premiums ceded, Folksamerica will cede up to 35% of its 2006 underwriting year short-tailed excess of loss business, mainly property and marine, to Olympus and a newly-formed reinsurer, Helicon Reinsurance Company, Ltd. ( Helicon ). Olympus and Helicon share, pro rata, in this up to 35% cession based on their relative capital bases. The 2005 and prior underwriting year business will continue to run-off with Olympus and it is expected that the majority of the risk exposures will expire by the end of the second quarter of 2006. White Mountains Re is fully collateralized for all recoverable amounts recorded as of December 31, 2005, related to the 2005 and prior underwriting year business ceded to Olympus.

These arrangements are designed to increase White Mountains Re's capacity to capitalize on improved pricing trends, where appropriate, and to reduce its potential loss exposure to any large, or series of smaller, property catastrophe events.

Under its prior ownership, Sirius' threshold for risk exposure and earnings volatility was extremely low. As a consequence, Sirius purchased many reinsurance protections at significant costs. These protections were purchased primarily to reduce the company's property catastrophe exposure on both a treaty and facultative basis. Under White Mountains Re's ownership, Sirius' reinsurance purchasing is subject to a higher retention of underlying business. Selective purchases are made primarily for property catastrophe protection and aviation exposures.

Reinsurance contracts do not relieve White Mountains Re of its obligation to its ceding companies. Therefore, collectibility of balances due from its retrocessional reinsurers is critical to White Mountains Re's financial strength. See **Note 4 - Third Party Reinsurance** to the accompanying Consolidated Financial Statements for a discussion of White Mountains Re's top reinsurers.

### Loss and Loss Adjustment Expense Reserves

White Mountains Re establishes reserves that are estimates of future amounts needed to pay claims and related expenses for insured events that have already occurred. See **CRITICAL ACCOUNTING ESTIMATES** in **Management's Discussion and Analysis of Financial Condition and Results of Operations** for a full discussion regarding White Mountains Re's loss reserving process.

The following information presents (1) White Mountains Re's reserve development over the preceding ten years and (2) a reconciliation of reserves on a regulatory basis to reserves determined in accordance with GAAP, each as prescribed by Securities Act Industry Guide No. 6.

Section I of the ten year table shows the estimated liability that was recorded at the end of each of the indicated years for all current and prior accident year unpaid losses and LAE. The liability represents the estimated amount of losses and LAE for claims that were unpaid at the balance sheet date, including IBNR reserves. In accordance with GAAP, the liability for unpaid losses and LAE is recorded in the balance sheet gross of the effects of reinsurance with an estimate of reinsurance recoverables arising from reinsurance contracts reported separately as an asset. The net balance represents the estimated amount of unpaid losses and LAE outstanding as of the balance sheet date, reduced by estimates of amounts recoverable under reinsurance contracts.

Section II shows the re-estimated amount of the previously recorded net liability as of the end of each succeeding year. Estimates of the liability for unpaid losses and LAE are increased or decreased as payments are made and more information regarding individual claims and trends, such as overall frequency and severity patterns, becomes known. Section III shows the cumulative net (deficiency)/redundancy representing the aggregate change in the liability from original balance sheet dates and the re-estimated liability through December 31, 2005. Section IV shows the re-estimated gross liability and re-estimated reinsurance recoverables through December 31, 2005. Section V shows the cumulative amount of net losses and LAE paid relating to recorded liabilities as of the end of each succeeding year.

The following table includes the complete loss development history for all periods presented for all companies acquired by White Mountains Re as if the companies had been combined from their inception.

**This table includes development on reserves reported by acquired companies before those companies were acquired by White Mountains Re**

(\$ in millions)	White Mountains Re Loss and LAE (1), (2), (3), (4)										
	Years Ended December 31,										
	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
<b>I. Liability for unpaid losses and LAE:</b>											
Gross balance	\$ 1,895.7	\$ 2,448.2	\$ 2,386.1	\$ 2,524.2	\$ 2,299.6	\$ 3,175.1	\$ 3,917.3	\$ 3,925.1	\$ 3,910.4	\$ 4,170.3	\$ 4,680.3
Less: reins. recoverables on unpaid losses and LAE	(336.6)	(524.7)	(513.3)	(592.9)	(651.0)	(1,148.5)	(1,353.7)	(1,277.6)	(1,214.6)	(1,346.6)	(1,878.5)
Net balance	\$ 1,559.1	\$ 1,923.5	\$ 1,872.8	\$ 1,931.3	\$ 1,648.6	\$ 2,026.6	\$ 2,563.6	\$ 2,647.5	\$ 2,695.8	\$ 2,823.7	\$ 2,801.8
<b>II. Net liability re-estimated as of:</b>											
1 year later	1,470.8	1,937.9	1,855.4	2,001.3	1,908.2	2,491.9	2,617.0	2,844.0	2,718.4	2,874.7	
2 years later	1,482.1	1,871.0	1,889.2	2,036.4	2,169.0	2,500.7	2,844.8	2,881.9	2,788.9		
3 years later	1,423.4	1,909.2	1,862.8	2,011.9	2,175.0	2,744.5	2,907.7	2,962.9			
4 years later	1,499.0	1,903.8	1,834.3	2,012.5	2,369.9	2,793.7	2,986.1				
5 years later	1,483.4	1,870.1	1,817.6	2,065.9	2,388.3	2,909.7					
6 years later	1,445.3	1,842.7	1,837.0	2,079.0	2,448.5						
7 years later	1,416.8	1,854.5	1,842.1	2,142.6							
8 years later	1,426.7	1,857.4	1,903.9								
9 years later	1,426.5	1,914.5									
10 years later	1,482.5										
<b>III. Cumulative net (deficiency)/redundancy</b>											
	\$ 76.6	\$ 9.0	\$ (31.1)	\$ (211.3)	\$ (799.9)	\$ (883.1)	\$ (422.5)	\$ (315.4)	\$ (93.1)	\$ (51.0)	
<b>Percent (deficient)/redundant</b>											
	4.9%	.5%	(1.7)%	(10.9)%	(48.5)%	(43.6)%	(16.5)%	(11.9)%	(3.5)%	(1.8)%	%
<b>IV. Reconciliation of net liability re-estimated as of the end of the latest re-estimation period (see II. above):</b>											
<b>Gross re-estimated liability</b>											
	1,848.5	2,492.6	2,494.1	2,837.9	3,154.0	4,302.3	4,548.1	4,413.1	4,156.6	4,332.9	
<b>Less: gross re-estimated reinsurance recoverable</b>											
	(366.0)	(578.1)	(590.2)	(695.3)	(705.5)	(1,392.6)	(1,562.0)	(1,450.2)	(1,367.7)	(1,458.2)	
<b>Net re-estimated liability</b>											
	\$ 1,482.5	\$ 1,914.5	\$ 1,903.9	\$ 2,142.6	\$ 2,448.5	\$ 2,909.7	\$ 2,986.1	\$ 2,962.9	\$ 2,788.9	\$ 2,874.7	
<b>V. Cumulative net amount of liability paid</b>											

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through:										
1 year later	463.5	504.5	498.7	542.9	420.5	689.2	729.8	994.0	720.9	965.8
2 years later	665.3	771.2	830.9	741.1	860.2	1,167.4	1,429.6	1,394.5	1,310.3	
3 years later	788.4	1,007.0	975.3	1,008.0	1,142.4	1,731.1	1,720.3	1,873.4		
4 years later	940.9	1,147.4	1,129.5	1,181.6	1,516.1	1,936.7	2,119.7			
5 years later	1,018.6	1,258.2	1,242.9	1,382.7	1,658.7	2,243.2				
6 years later	1,088.7	1,351.0	1,317.4	1,487.3	1,872.7					
7 years later	1,158.8	1,405.6	1,384.2	1,580.9						
8 years later	1,200.7	1,457.7	1,444.9							
9 years later	1,246.1	1,502.8								
10 years later	1,277.1									

- (1) The table includes the complete loss development history for all periods presented for all companies acquired by Folksamerica through an instrument of transfer and assumption approved by the appropriate insurance regulators. Under the instrument, insurance regulators require that Folksamerica report reserve development as if the companies had been combined from their inception.
- (2) Folksamerica became a wholly-owned subsidiary of White Mountains during 1998. Reserve development for the years ended 1995 through 1997 reflects development on reserves established before White Mountains consolidated Folksamerica's results.
- (3) Sirius, including Scandinavian Re, became a wholly-owned subsidiary of White Mountains during 2004. Reserve development for the years ended 1995 through 2003 reflects development on reserves established before White Mountains consolidated Sirius' results. See table, below.
- (4) White Mountains acquired \$136.8 million in net loss and lae reserves when it acquired Tryg-Baltica during 2004. For periods prior to December 31, 2004, loss and LAE reserves for Tryg-Baltica are not included due to lack of availability of loss development history on a comparable basis.

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The cumulative net (deficiency)/redundancy in the table above reflects adverse development recorded by Scandinavian Re, which was acquired by White Mountains Re in 2004 and has been in run-off since 2002. This has the effect of significantly increasing White Mountains Re's cumulative deficiency for each of the years presented in the table, including the years prior to White Mountains Re's acquisition of Sirius. The table presented below represents White Mountains Re's cumulative net (deficiency)/redundancy excluding Scandinavian Re:

(\$ in millions)	Years Ended December 31,										
	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Cumulative net (deficiency) redundancy, excluding Scandinavian Re	\$ 103.2	\$ 32.6	\$ (20.5)	\$ (128.2)	\$ (311.1)	\$ (144.5)	\$ (94.6)	\$ (107.3)	\$ (52.5)	\$ (46.6)	\$
Percent (deficient) / redundant	6.8%	1.7%	(1.1)%	(7.2)%	(22.6)%	(10.7)%	(6.8)%	(6.7)%	(2.7)%	(2.1)%	%

The following table reconciles loss and LAE reserves determined on a regulatory basis to loss and LAE reserves determined in accordance with GAAP at December 31, as follows:

(Millions)	December 31,		
	2005	2004	2003
Regulatory reserves	\$ 3,109.7	\$ 3,092.0	\$ 2,928.4
Reinsurance recoverable on unpaid losses and LAE (1)	1,513.1	948.2	746.1
Discount on loss reserves	184.5	245.2	246.0
Reserves allocated to other segments	(105.4)	(91.2)	(33.4)
Purchase accounting and other	(21.6)	(23.9)	23.3
GAAP reserves	\$ 4,680.3	\$ 4,170.3	\$ 3,910.4

(1) Represents adjustments made to add back reinsurance recoverables included with the presentation of reserves under regulatory accounting.

### ESURANCE

The Esurance group of companies, which is headquartered in San Francisco, has been part of White Mountains since October 2000. Esurance markets personal auto insurance directly to customers and through select online agents. Most customer interaction with the company takes place through Esurance's website, [www.esurance.com](http://www.esurance.com). Through the website, customers can get real-time quotes, compare quotes from other companies, purchase their policies, report claims and manage their accounts. At December 31, 2005, Esurance had over 210,000 policies in force.

Esurance's underwriting companies, Esurance Insurance Company and Esurance Property and Casualty Insurance Company, are both rated A (Excellent, the third highest of fifteen ratings) by A.M. Best. The Esurance segment includes insurance ceded by Esurance to affiliates of White Mountains. At December 31, 2005 and 2004, Esurance had \$414.2 million and \$241.7 million of total assets and \$176.7 million and \$109.0 million of shareholder's equity, respectively.





## Geographic Concentration

As of December 31, 2005, Esurance writes business in twenty-two states. These states represent approximately 77% of the premium volume for the entire U.S. personal automobile insurance market. For the years ended December 31, 2005, 2004 and 2003, Esurance had net written premiums of \$349 million, \$199 million and \$116 million, respectively, which were produced in the following states:

Net written premiums by state	Year Ended December 31,		
	2005	2004	2003
Florida	20%	24%	24%
California	20	25	32
Texas	9	11	15
New York	8	5	2
Michigan	7	7	5
Virginia	4	4	3
Colorado	4	4	2
Illinois	4	4	4
Other	24	16	13
Total	100%	100%	100%

## Marketing

Esurance targets technology-savvy consumers who rely on the internet to manage their financial services needs. Esurance distributes most of its business directly online or over the telephone. Phone sales are handled by sales teams in Esurance's Sioux Falls, Tampa, and Sacramento offices. Online agent partners also represent an important distribution channel for Esurance.

Esurance uses its media mix of offline and online advertising to reach its target customers efficiently. Esurance advertises offline on television, radio, and through direct mail. Esurance advertises online through paid search (e.g., Google and Yahoo! Search), and on a variety of insurance, finance, and automotive sites, along with major portals (e.g., MSN and AOL).

## Underwriting and Pricing

Esurance collects and verifies detailed underwriting information in real-time while customers transact with the company online. Real-time access to customer information allows Esurance to continually develop and refine its highly segmented, tiered pricing models. Esurance believes that its tiered pricing models have a greater statistical correlation with historical loss experience than traditional pricing models have shown. As a result, Esurance can quote rates to customers that most closely correspond to the individual risk characteristics of the customer, enabling Esurance to focus on keeping insurance rates competitive without compromising the company's loss ratio targets.

## Competition

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Esurance competes with national and regional personal automobile insurance companies, though Esurance's main competition comes from other direct writers like Progressive, GEICO, and 21st Century.

By leveraging web-enabled technology, Esurance can capture data real-time and respond to changing loss trends. Esurance is continually able to refine pricing, enhance its auto product and optimize dollars spent on marketing with the array of customer information that is at its disposal. Web technology also allows Esurance to provide high quality, 24/7 customer service and claims handling for a competitive price.

Esurance's paperless business process allows the company to significantly reduce operating costs typically associated with policy processing, verification and endorsement activities. As a result, the company is able to achieve efficient, low-cost acquisition and operating expense structures.

## Claims Management

Esurance takes initial notice of claims at the company's loss reporting unit in South Dakota, which is available for customers 24 hours a day, 365 days a year. The loss reporting unit then transfers claims to regional claim centers in Arizona, California, Florida, Georgia, New Jersey, New York, and Texas where claims are handled and adjusted.

Esurance's claims organization leverages technology to reduce cycle times and achieve strict claims performance metrics. Rapid response to and resolution of claims creates a stronger relationship with customers, while also decreasing ancillary claims costs, such as rental car fees. Additionally, Esurance maintains a special investigative unit designed to detect insurance fraud, and actively supports efforts by regulatory bodies and trade associations to curtail the cost of insurance fraud.

## Catastrophe Risk Management

Esurance's sole line of business is personal automobile insurance that covers liabilities and physical damage arising from the operation of automobiles. The majority of Esurance's customers elect coverage for physical damage (83%), resulting in exposure to catastrophe losses at Esurance for hurricanes, hailstorms, earthquakes and other acts of nature. Generally, catastrophe costs are low for personal auto in relation to other lines of business, such as homeowners and commercial property. Additionally, Esurance's broad geographic distribution limits its concentration of risk and the potential for losses to accumulate from a single event.

## Loss and Loss Adjustment Expense Information

The process of estimating reserves for Esurance is similar to the process described in **Loss and Loss Adjustment Expense Reserves** in the **ONEBEACON** discussion and, as of any given date, is inherently uncertain. As described previously, uncertainties in projecting estimates of ultimate loss and LAE are magnified by the time lag between when a claim actually occurs and when it is reported and settled, i.e., the claim-tail. Esurance writes primarily short-tail personal automobile insurance policies, which reduces the uncertainty inherent in its loss and LAE reserves when compared to insurance companies that write long-tail policies, such as workers compensation.

Management believes that Esurance's loss and LAE reserves as of December 31, 2005 are adequate; however, ultimate loss and LAE may deviate, perhaps materially, from the amounts currently reflected in the reserve balance. Adverse development, if any, would impact the Company's future results of operations.

The following information presents (1) Esurance's reserve development over the five years since inception and (2) a reconciliation of reserves on a Statutory basis to reserves determined in accordance with GAAP, each as prescribed by Securities Act Industry Guide No. 6.

Section I of the table shows the estimated liability that was recorded at the end of each of the indicated years for all current and prior accident year unpaid losses and LAE. The liability represents the estimated amount of losses and LAE for claims that were unpaid at the balance sheet date, including IBNR reserves. In accordance with GAAP, the liability for unpaid losses and LAE is recorded in the balance sheet gross of the

effects of reinsurance with an estimate of reinsurance recoverables arising from reinsurance contracts reported separately as an asset. The net balance represents the estimated amount of unpaid losses and LAE outstanding as of the balance sheet date, reduced by estimates of amounts recoverable under reinsurance contracts.

Section II shows the re-estimated amount of the previously recorded net liability as of the end of each succeeding year. Estimates of the liability for unpaid losses and LAE are increased or decreased as payments are made and more information regarding individual claims and trends, such as overall frequency and severity patterns, becomes known. Section III shows the cumulative net (deficiency)/redundancy representing the aggregate change in the liability from original balance sheet dates and the re-estimated liability through December 31, 2005. Section IV shows the re-estimated gross liability and re-estimated reinsurance recoverables through December 31, 2005. Section V shows the cumulative amount of net losses and LAE paid relating to recorded liabilities as of the end of each succeeding year.

(\$ in millions)	Esurance Loss and LAE (1), (2)				
	Years Ended December 31,				
	2001	2002	2003	2004	2005
<b>I. Liability for unpaid losses and LAE:</b>					
Gross balances:	\$ 4.0	\$ 15.5	\$ 39.1	\$ 63.0	\$ 93.7
Less: reinsurance recoverables on unpaid losses and LAE				0.1	
Net balance	\$ 4.0	\$ 15.5	\$ 39.1	\$ 62.9	\$ 93.7
<b>II. Net liability re-estimated as of:</b>					
1 year later	4.0	16.0	34.0	54.9	
2 years later	4.4	15.3	29.4		
3 years later	4.3	14.4			
4 years later	4.2				
III. Cumulative net (deficiency)/ redundancy	\$ (0.2)	\$ 1.1	\$ 9.7	\$ 8.0	\$
Percent (deficient)/redundant	(5.0)%	7.1%	24.8%	12.7%	%
<b>IV. Reconciliation of net liability re-estimated as of the end of the latest re-estimation period (see II. above):</b>					
Gross re-estimated liability	4.2	14.4	29.6	55.1	
Less: gross re-estimated reinsurance recoverable			0.2	0.2	
Net re-estimated liability	\$ 4.2	\$ 14.4	\$ 29.4	\$ 54.9	\$
<b>V. Cumulative net amount of liability paid through:</b>					
1 year later	2.5	9.3	18.9	35.8	
2 years later	3.3	12.2	24.5		
3 years later	3.9	13.7			
4 years later	4.1				

(1) The table consists of reserve information for Esurance Insurance Company, Esurance Property & Casualty Insurance Company, and business ceded by Esurance to Folksamerica and OneBeacon.

(2) Esurance became a subsidiary of White Mountains during 2000.

The following table reconciles loss and LAE reserves determined on a Statutory basis to loss and LAE reserves determined in accordance with GAAP at December 31, as follows:

(millions)	December 31,		
	2005	2004	2003
Statutory reserves	\$ 30.0	\$ 16.2	\$ 7.6
Reserves allocated from other segments	63.7	46.7	31.5
Reinsurance recoverable on unpaid losses and LAE (1)		.1	
GAAP reserves	\$ 93.7	\$ 63.0	\$ 39.1

(1) Represents adjustments made to add back reinsurance recoverables included with the presentation of reserves under regulatory accounting.

## OTHER OPERATIONS

**The Company and its Intermediate Holding Companies**

The Company's intermediate holding companies include Fund American Companies, Inc. ( Fund American ) and Fund American Enterprises Holdings, Inc. ( FAEH ), both U.S.-domiciled companies, as well as various intermediate holding companies domiciled in the United States, Gibraltar, Luxembourg, Sweden and Bermuda. White Mountains arranges the majority of its financing through the Company and these intermediate holding companies. In May 2003, Fund American issued \$700 million face value of senior unsecured debt through a public offering, at an issue price of 99.7% (the Senior Notes ). The Senior Notes bear an annual interest rate of 5.9% until

maturity on May 15, 2013, and are fully and unconditionally guaranteed as to the payment of principal and interest by the Company.

Fund American and the Company are both permitted borrowers under a \$400 million revolving credit facility (the Bank Facility), which matures in August 2009. As of December 31, 2005, the Bank Facility was undrawn.

As part of the financing for the OneBeacon Acquisition, Berkshire Hathaway, Inc. (Berkshire) invested a total of \$300 million in cash, of which (1) \$225 million was for the purchase of cumulative non-voting preferred stock of Fund American (the Berkshire Preferred Stock), which has a \$300 million redemption value; and (2) \$75 million was for the purchase of warrants to acquire 1,724,200 common shares of the Company. The Berkshire Preferred Stock is entitled to a dividend of no less than 2.35% per quarter and is mandatorily redeemable on May 31, 2008. During 2004, Berkshire exercised its warrants for \$294 million in cash.

Also as part of the financing of the OneBeacon Acquisition, Zenith Insurance Company (Zenith) purchased \$20 million in cumulative non-voting preferred stock of FAEH (the Zenith Preferred Stock). The Zenith Preferred Stock is entitled to a dividend of no less than a 2.5% per quarter through June 30, 2007 and a dividend of no less than 3.5% per quarter thereafter. The Zenith Preferred Stock is mandatorily redeemable on May 31, 2011. At the Company's option, the Zenith Preferred Stock may be redeemed on June 30, 2007.

### **International American Group**

In October 1999, White Mountains acquired the International American Group, which included American Centennial, British Insurance Company and Peninsula Insurance Company (Peninsula).

Delaware-domiciled American Centennial and Cayman Island-domiciled British Insurance Company are property and casualty insurance and reinsurance companies in run-off. At December 31, 2005 and 2004, American Centennial had \$76.8 million and \$61.3 million of total assets and \$16.8 million and \$21.0 million of shareholder's equity, respectively. At December 31, 2005 and 2004, British Insurance Company had \$37.7 million and \$33.4 million of total assets and \$6.3 million and \$4.5 million of shareholder's equity, respectively.

In January 2004, White Mountains sold Peninsula, a Maryland-domiciled property and casualty insurer, for \$23.3 million. For the year ended December 31, 2003, Peninsula had \$34.1 million of net written premiums.

### **INVESTMENTS**

The investment portfolios of White Mountains' insurance and reinsurance operations consist primarily of fixed maturity investments but also consist, in part, of short-term investments, common equity securities and other investments (principally investments in limited partnership interests). White Mountains' management believes that prudent levels of investments in common equity securities and other investments within its investment portfolio are likely to enhance after-tax total returns without significantly increasing the risk profile of the portfolio when considered over long periods of time and balanced with leverage and insurance risk considerations. White Mountains seeks to maximize after-tax, risk-adjusted returns over the long term.

At December 31, 2005, approximately 99% of White Mountains' fixed maturity investments received an investment grade rating from Standard & Poor's or from Moody's Investor Services (Moody's) if a given security is unrated by Standard & Poor's. Standard & Poor's and Moody's are two third party rating agencies that assess the credit quality of companies that have publicly issued debt. An investment grade rating, which is indicative of a strong credit profile of an issuer, is defined as BBB (Adequate, the ninth highest of twenty-two ratings) or better by Standard & Poor's and Baa3 (Moderate Risk, the tenth highest of twenty-one ratings) or better by Moody's. White Mountains expects to continue to invest primarily in high quality, fixed maturity investments. Nearly all the fixed maturity investments currently held by White Mountains are publicly traded, and as such are considered to be liquid.



At December 31, 2005 White Mountains' consolidated investment portfolio consisted of \$7,583 million (77%) of fixed maturity investments, \$728 million (7%) of short-term investments, \$968 million (10%) of common equity securities and \$588 million (6%) of other investments. White Mountains' fixed maturity investments at December 31, 2005 consisted principally of corporate debt securities (38%), asset-backed securities (28%), U.S. government and agency securities (23%), foreign government obligations (9%) and preferred equity securities and municipal bonds (2%).

White Mountains' investment philosophy is to maximize its after-tax total risk-adjusted return over the long term. Under this approach, each dollar of after-tax investment income and realized and unrealized gains and losses is valued equally. White Mountains' overall fixed maturity investment strategy is to purchase securities that are attractively priced in relation to credit risks. White Mountains generally manages the interest rate risk associated with holding fixed maturity investments by actively maintaining the average duration of the portfolio to achieve an adequate after-tax total return without subjecting the portfolio to an unreasonable level of interest rate risk. At December 31, 2005, the duration of White Mountains' fixed maturity investments was approximately 2.9 years and including short-term investments was approximately 2.2 years.

### *Montpelier*

In December 2001, White Mountains, the Benfield Group plc and several other private investors established Montpelier and its wholly-owned subsidiary Montpelier Reinsurance Ltd. ( Montpelier Re ). Montpelier Re is a Bermuda-domiciled insurance and reinsurance company that was formed with approximately \$1.0 billion in capital to respond to the then favorable underwriting and pricing environment in the reinsurance industry. Montpelier Re has initially focused on property reinsurance business. Montpelier Re is rated A- (Excellent, the fourth highest of fifteen ratings) by A.M. Best. On October 15, 2002, Montpelier successfully completed an initial public offering and its common shares are listed on the New York Stock Exchange. White Mountains initially invested \$180 million in Montpelier in exchange for 10.8 million common shares and warrants to acquire 4.8 million additional common shares of Montpelier.

During the first quarter of 2004, White Mountains sold 4.5 million common shares of Montpelier to third parties. As a result of this sale, as well as changes to the composition of the Board of Directors of both Montpelier and White Mountains, White Mountains changed the method of accounting for its remaining common share investment in Montpelier as of March 31, 2004 from an equity method investment in an unconsolidated affiliate to a common equity security classified as available for sale and carried at fair value. Also during the first quarter of 2004, White Mountains purchased additional warrants to acquire 2.4 million common shares of Montpelier from an existing warrant holder for \$54 million in cash, thereby raising the total number of such warrants owned by White Mountains to 7.2 million. The Montpelier warrants have an exercise price of \$16.67 per share (as adjusted for stock splits) and are exercisable until December 2011.

### **Investments in Unconsolidated Affiliates**

#### *Symetra*

On August 2, 2004, White Mountains, Berkshire and several other private investors capitalized Symetra in order to purchase the life and investment operations of Safeco Corporation for \$1.35 billion. The acquired companies, which are now operating under the Symetra brand, focus mainly on group insurance, individual life insurance, structured settlements and retirement services. Symetra had an initial capitalization of approximately \$1.4 billion, consisting of \$1,065 million of common equity and \$315 million of debt. White Mountains invested \$195 million in Symetra in exchange for 2.0 million common shares of Symetra. In addition, White Mountains and Berkshire each received warrants to acquire an additional 1.1 million common shares of Symetra at \$100 per share. White Mountains owns approximately 19% of the outstanding common shares of Symetra and approximately 24% of Symetra on a fully-converted basis including the warrants. Three White Mountains

designees serve on Symetra's eight member board of directors.

Symetra's total revenues and net income for the year ended December 31, 2005 were \$1,628.6 million and \$145.5 million, respectively, and for the five months ended December 31, 2004 were \$702.2 million and \$57.9 million, respectively. Symetra's total assets and shareholders' equity as of December 31, 2005 and 2004 were \$21.0 billion and \$1.4 billion, respectively, and \$22.2 billion and \$1.4 billion, respectively. Symetra's principal

insurance operating subsidiaries are rated **A** (Excellent, the third highest of fifteen ratings) by A.M. Best and **A-** (Strong, the seventh highest of twenty-one ratings) by Standard & Poor's.

As of December 31, 2005 and 2004, White Mountains' total investment in Symetra was \$287.5 million and \$248.4 million, respectively, excluding \$24.2 million and \$56.6 million, respectively, of equity in unrealized gains from Symetra's fixed maturity investments.

*Main Street America Holdings, Inc. (MSA)*

MSA is a subsidiary of Main Street America Group Mutual Holdings, Inc. (Main Street Group), a Florida-domiciled mutual property and casualty insurance holding company, which insures risks located primarily in New York, Massachusetts, Connecticut, Pennsylvania, New Hampshire, Virginia and Florida. White Mountains owns 50% of the outstanding common stock of MSA and accounts for this investment using the equity method. MSA's net written premiums for the years ended December 31, 2005, 2004 and 2003 totaled \$481.6 million, \$454.5 million and \$427.6 million, respectively, and its net income totaled \$16.1 million, \$30.3 million and \$29.3 million, respectively. MSA's total assets as of December 31, 2005 and 2004 were \$1,064.8 million and \$993.1 million, respectively, and its shareholders' equity was \$334.9 million and \$324.0 million, respectively. The principal insurance operating subsidiaries of Main Street Group are rated **A** (Excellent, the third highest of fifteen ratings) by A.M. Best.

As of December 31, 2005 and 2004, White Mountains' total investment in MSA was \$168.0 million and \$161.6 million, respectively.

## **REGULATION**

### **United States**

White Mountains' U.S.-based insurance and reinsurance operating subsidiaries are subject to regulation and supervision in each of the states where they are domiciled and licensed to conduct business. Generally, regulatory authorities have broad supervisory and administrative powers over such matters as licenses, standards of solvency, premium rates, policy forms, investments, security deposits, methods of accounting, form and content of financial statements, reserves for unpaid loss and LAE, reinsurance, minimum capital and surplus requirements, dividends and other distributions to shareholders, periodic examinations and annual and other report filings. In general, such regulation is for the protection of policyholders rather than shareholders. White Mountains believes that it is in compliance with all applicable laws and regulations pertaining to its business that would have a material effect on its financial position in the event of non-compliance.

Over the last several years most states have implemented laws that establish standards for current, as well as continued, state accreditation. In addition, the NAIC has adopted risk-based capital (RBC) standards for property and casualty insurers as a means of monitoring certain aspects affecting the overall financial condition of insurance companies. The current RBC ratios of White Mountains' active insurance and reinsurance operating subsidiaries are satisfactory and such ratios are not expected to result in any adverse regulatory action. White Mountains is not aware of any current recommendations by regulatory authorities that would be expected to have a material effect on its results of operations or liquidity.

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As a condition of its license to do business in certain states, White Mountains insurance operating subsidiaries are required to participate in mandatory shared market mechanisms. Each state dictates the types of insurance and the level of coverage that must be provided. The most common type of shared market mechanism in which White Mountains is required to participate is an assigned risk plan. Many states operate assigned risk plans. The NYAIP and New Jersey commercial automobile insurance plans are two such shared market mechanisms in which OneBeacon is required to participate. These plans require insurers licensed within the applicable state to accept the applications for insurance policies of individuals who are unable to obtain insurance in the voluntary market. The total number of such policies an insurer is required to accept is based on its market share of voluntary business in the state. Underwriting results related to assigned risk plans are typically adverse. Accordingly, OneBeacon may be required to underwrite policies with a higher risk of loss than it would otherwise accept.

Reinsurance facilities are another type of shared market mechanism. Reinsurance facilities require an insurance company to accept all applications submitted by certain state designated agents. The reinsurance facility then allows the insurer to cede some of its business to the reinsurance facility so that the facility will reimburse the insurer for claims paid on ceded business. Typically, however, reinsurance facilities operate at a deficit, which is funded

through assessments against the same insurers. The Massachusetts Commonwealth Automobile Reinsurers is one such reinsurance facility in which OneBeacon is compelled to participate. As a result, OneBeacon could be required to underwrite policies with a higher risk of loss than it would otherwise accept.

The insurance laws of many states generally provide that property and casualty insurers doing business in those states belong to a statutory property and casualty guaranty association. The purpose of these guaranty associations is to protect policyholders by requiring that solvent property and casualty insurers pay certain insurance claims of insolvent insurers. These guaranty associations generally pay these claims by assessing solvent insurers proportionately based on the insurer's share of voluntary written premiums in the state. While most guaranty associations provide for recovery of assessments through rate increases, surcharges or premium tax credits, there is no assurance that insurers will ultimately recover these assessments. At December 31, 2005, the reserve for such assessments at OneBeacon totaled \$18 million.

Many states have laws and regulations that limit an insurer's ability to exit a market. For example, certain states limit a private passenger automobile insurer's ability to cancel and non-renew policies. Furthermore, certain states prohibit an insurer from withdrawing from one or more lines of insurance business in the state, unless the state regulators approve the company's withdrawal plans. State regulators may refuse to approve such plans on the grounds that they could lead to market disruption. Such laws and regulations may restrict White Mountains' ability to exit unprofitable markets.

Nearly all states have insurance laws requiring personal property and casualty insurers to file price schedules, policy or coverage forms, and other information with the state's regulatory authority. In most cases, such price schedules and/or policy forms must be approved prior to use. While pricing laws vary from state to state, their objectives are generally to ensure that prices are adequate, not excessive and not discriminatory. For example, Massachusetts, a state where OneBeacon has a sizable presence, sets virtually all aspects of automobile insurance rates, including agent commissions. Such regulations often challenge an insurer's ability to adequately price its product, which often leads to unsatisfactory underwriting results.

White Mountains' U.S. insurance and reinsurance operating subsidiaries are subject to state laws and regulations that require investment portfolio diversification and that limit the amount of investment in certain categories. Non-compliance may cause non-conforming investments to be non-admitted in measuring statutory surplus and, in some instances, may require divestiture. White Mountains' investment portfolio at December 31, 2005 complied with such laws and regulations in all material respects.

One of the primary sources of cash inflows for the Company and certain of its intermediary holding companies is dividends received from its insurance and reinsurance operating subsidiaries. Under the insurance laws of the states under which White Mountains' U.S.-based insurance and reinsurance subsidiaries are domiciled, an insurer is restricted with respect to the timing or the amount of dividends it may pay without prior approval by regulatory authorities. See **Dividend Capacity** in the **LIQUIDITY AND CAPITAL RESOURCES** section of Item 7 for further discussion.

White Mountains is subject to regulation under certain state insurance holding company acts. These regulations contain reporting requirements relating to the capital structure, ownership, financial condition and general business operations of White Mountains' insurance and reinsurance operating subsidiaries. These regulations also contain special reporting and prior approval requirements with respect to certain transactions among affiliates. Since the Company is an insurance holding company, the domiciliary states of its insurance and reinsurance operating subsidiaries impose regulatory application and approval requirements on acquisitions of White Mountains' common shares which may be deemed to confer control over those subsidiaries, as that concept is defined under the applicable state laws. Acquisition of as little as 10% of White Mountains' common shares may be deemed to confer control under the insurance laws of some jurisdictions, and the application process for approval can be extensive and time consuming.

While the federal government does not directly regulate the insurance business, federal legislation and administrative policies affect the insurance industry. In addition, legislation has been introduced from time to time in recent years that, if enacted, could result in the federal government assuming a more direct role in the regulation of the insurance industry. A federal law enacted in 2002 and extended in 2005, the Terrorism Act, provides a back-stop to property and casualty insurers in the event of future terrorist acts perpetrated by foreign agents or interests. In exchange for this back-stop, primary insurers are required to make coverage available to commercial insureds for losses from acts of non-domestic terrorism as specified in the Terrorism Act. OneBeacon is actively

complying with the requirements of the Terrorism Act in order to ensure its ability to be reimbursed by the federal government for any losses it may incur as a result of future terrorist acts. (See **Terrorism** in the **ONEBEACON** section of this Item for a further discussion of the Terrorism Act). A number of additional enacted and pending legislative measures could lead to increased consolidation and increased competition for business and for capital in the financial services industry. White Mountains cannot predict whether any state or federal measures will be adopted to change the nature or scope of the regulation of the insurance business or what effect such measures may have on its insurance and reinsurance operations.

Environmental cleanup of polluted waste sites is subject to both federal and state regulation. The Comprehensive Environmental Response Compensation and Liability Act of 1980 ( Superfund ) and comparable state statutes govern the cleanup and restoration of waste sites by potentially responsible parties ( PRPs ). These laws can impose liability for the entire cost of clean-up upon any responsible party, regardless of fault. The insurance industry in general is involved in extensive litigation regarding coverage issues arising out of the cleanup of waste sites by insured PRPs and as a result has disputed many such claims. From time to time, comprehensive Superfund reform proposals are introduced in Congress, but none has yet been enacted. At this time, it remains unclear as to whether Superfund reform legislation will be enacted or that any such legislation will provide for a fair, effective and cost-efficient system for settlement of Superfund related claims. The NICO Cover includes coverage for such exposures at OneBeacon; however, there can be no assurance that the coverage provided under the NICO Cover will ultimately prove to be adequate.

#### **Sweden**

In accordance with provisions of Swedish law, Sirius International is permitted to transfer up to the full amount of its pre-tax income, subject to certain limitations, into an untaxed reserve referred to as a safety reserve. Under GAAP, an amount equal to the safety reserve, net of the related deferred tax liability established at the Swedish tax rate of 28%, is classified as shareholders' equity. Generally, this deferred tax liability is only required to be paid by Sirius International if it fails to maintain predetermined levels of premium writings in future years. As a result of the indefinite deferral of these taxes, Swedish regulatory authorities do not apply any taxes to the safety reserve when calculating solvency capital under Swedish insurance regulations. Accordingly, under local statutory requirements, an amount equal to Sirius International's safety reserve of \$920 million at December 31, 2005 is classified as surplus.

#### **RATINGS**

Insurance and reinsurance companies are evaluated by various rating agencies in order to measure each company's financial strength. Higher ratings generally indicate financial stability and a stronger ability to pay claims. White Mountains believes that strong ratings are important factors in the marketing of insurance and reinsurance products to agents and consumers and ceding companies.

Rating agencies also evaluate the general creditworthiness of debt securities issued by companies. Their ratings are then used by existing or potential investors to assess the likelihood of repayment on a particular debt issue. White Mountains believes that strong debt ratings are important factors that provide better financial flexibility when issuing new debt or restructuring existing debt.

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The following table presents the financial strength ratings assigned to White Mountains' principal insurance and reinsurance operating subsidiaries and the debt ratings for Fund American's Senior Notes as of February 28, 2006:

	OneBeacon	Folksamerica Re	Sirius International	Esurance	Fund American Senior Notes (5)
<b>A.M. Best</b>					
Rating (1)	A (Excellent)	A (Excellent)	A (Excellent)	A (Excellent)	bbb (Very Good)
Outlook	Stable	Stable	Stable	Stable	Stable
<b>Standard &amp; Poor's</b>					
Rating (2)	A (Strong)	A- (Strong)	A- (Strong)	No Rating	BBB (Adequate)
Outlook	Stable	Positive	Positive	N/A	Stable
<b>Moody's</b>					
Rating (3)	A2 (Good)	A3 (Good)	A3 (Good)	A2 (Good)	Baa2 (Medium Grade)
Outlook	Stable	Positive	Positive	Stable	Stable
<b>Fitch</b>					
Rating (4)	A (Strong)	A (Strong)	No Rating	A (Strong)	BBB (Good)
Outlook	Stable	Stable	N/A	Stable	Stable

(1) A is the third highest of fifteen financial strength ratings and bbb is the ninth highest of twenty-two creditworthiness ratings assigned by A.M. Best.

(2) A is the sixth and A- is the seventh highest of twenty-one financial strength ratings and BBB is the ninth highest of twenty-two creditworthiness ratings assigned by Standard & Poor's.

(3) A2 is the sixth and A3 is the seventh highest of twenty-one financial strength ratings and Baa2 is the ninth highest of twenty-one creditworthiness ratings assigned by Moody's.

(4) A is the sixth highest of twenty-four financial strength ratings and BBB is the ninth highest of twenty-three creditworthiness ratings assigned by Fitch.

(5) The Senior Notes issued by Fund American are fully and unconditionally guaranteed as to the payment of principal and interest by the Company.

### EMPLOYEES

As of December 31, 2005, White Mountains employed 5,020 persons (consisting of 40 persons at the Company and its intermediate holding companies, 3,459 persons at OneBeacon, 566 persons at White Mountains Re, 916 persons at Esurance, 26 persons at WM Advisors and 13 persons at the International American Group companies). Management believes that White Mountains has satisfactory relations with its employees.

### AVAILABLE INFORMATION



The Company is subject to the informational reporting requirements of the Exchange Act. In accordance therewith, the Company files reports, proxy statements and other information with the SEC. These documents are available at [www.whitemountains.com](http://www.whitemountains.com). shortly after such material is electronically filed with or furnished to the SEC. In addition, the Company's code of business conduct and ethics as well as the various charters governing the actions of certain of the Company's Committees of its Board of Directors, including its Audit Committee, Compensation Committee and its Nominating and Governance Committee, are available at [www.whitemountains.com](http://www.whitemountains.com).

The Company will provide to any shareholder, upon request and without charge, copies of these documents (excluding any applicable exhibits unless specifically requested). Written or telephone requests should be directed to the Corporate Secretary, White Mountains Insurance Group, Ltd., 80 South Main Street, Hanover, New Hampshire 03755, telephone number (603) 640-2200. Additionally, all such documents are physically available at the Company's registered office at Clarendon House, 2 Church Street, Hamilton, HM 11 Bermuda.

## Item 1A. Risk Factors

The information contained in this report may contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. See **FORWARD-LOOKING STATEMENTS** (page 77) for specific important factors that could cause actual results to differ materially from those contained in forward-looking statements. The Company's actual future results and trends may differ materially depending on a variety of factors including, but not limited to, the risks and uncertainties discussed below.

### *Unpredictable catastrophic events could adversely affect our financial condition or results of operations.*

We write insurance and reinsurance policies that cover catastrophic events. Our policies cover unpredictable natural and other disasters, such as hurricanes, windstorms, earthquakes, floods, fires and explosions. Our exposure to catastrophic windstorm damage in the Northeastern United States is the largest single natural risk to our business. We also have significant exposure to a major California earthquake and windstorm damage in Northern Europe, the United States Atlantic Coast (i.e., Delaware to Florida) and the United States Gulf Coast region (i.e., Florida to Texas). In addition, we are exposed to losses from terrorist attacks, such as the attacks on the United States on September 11, 2001.

Claims from catastrophic events could reduce our earnings and cause substantial volatility in our financial results for any fiscal quarter or year and adversely affect our financial condition. Our ability to write new insurance and reinsurance policies could also be impacted as a result of corresponding reductions in our surplus levels. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Increases in the value of insured property, the effects of inflation and changes in cyclical weather patterns may increase the severity of claims from catastrophic events in the future.

We manage our exposure to catastrophic losses by limiting the aggregate insured value of policies in geographic areas with exposure to catastrophic events and by estimating PMLs for many different catastrophe scenarios. To manage and analyze aggregate insured values and PML, we use a variety of tools and analyses, including catastrophe modeling software packages. Our estimates of PML are dependent on many variables, including the quality of data provided to us by ceding companies (in the case of our reinsurance operations), the demand surge increase utilized to model the event and the relationship of the actual wind, zone density, storm surge and flood characteristics to the modeled event. Accordingly, the losses we might incur from an actual catastrophe could be materially higher than our expectation of losses generated from modeled catastrophe scenarios. For example, in 2005, the models did not adequately predict the insured losses from hurricane Katrina for either the industry or White Mountains.

*We may not be able to successfully alleviate risk through reinsurance and retrocessional arrangements. Additionally, we may be unable to collect all amounts due from our reinsurers under our existing reinsurance and retrocessional arrangements.*

We attempt to limit our risk of loss through reinsurance and retrocessional arrangements. Retrocessional arrangements refer to reinsurance purchased by a reinsurer to cover its own risks assumed from primary ceding companies. The availability and cost of reinsurance and retrocessional protection is subject to market conditions, which are outside of our control. As a result, we may not be able to successfully alleviate risk through these arrangements.

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We are not relieved of our obligation to our policyholders or ceding companies by purchasing reinsurance. Accordingly, we are subject to credit risk with respect to our reinsurance and retrocessions in the event that a reinsurer is unable to pay amounts owed to us as a result of a deterioration in its financial condition. A number of reinsurers in the industry experienced such a deterioration in the aftermath of the 2001 terrorist attacks and the active 2005 hurricane season. It is possible that one or more of our reinsurers will be significantly adversely affected by future significant loss events, causing them to be unable to pay amounts owed to us. For example, Olympus and Helicon provide a substantial amount of reinsurance protection to us. As of January 1, 2006, Olympus and Helicon had pro-forma capital of approximately \$188 million and \$145 million, respectively. We cannot guarantee that Olympus and/or Helicon will have sufficient capital to pay amounts owed to us resulting from one or more

future catastrophes. We also may be unable to recover amounts due under our reinsurance and retrocessional arrangements if our reinsurers choose to withhold payment due to a dispute or other factors beyond our control.

*Our loss reserves may be inadequate to cover our ultimate liability for losses and as a result our financial results could be adversely affected.*

We are required to maintain adequate reserves to cover our estimated ultimate liabilities for loss and loss adjustment expenses. These reserves are estimates based on actuarial and statistical projections of what we believe the settlement and administration of claims will cost based on facts and circumstances then known to us. Because of the uncertainties that surround estimating loss reserves, we cannot be certain that our reserves are adequate and actual claims and claim expenses paid might exceed our reserves. If our reserves are insufficient to cover our actual loss and loss adjustment expenses, we would have to strengthen our reserves and incur charges to our earnings. These charges could be material.

As industry practices and legal, judicial, social and other conditions change, unexpected and unintended issues related to claims and coverage may emerge. These issues may adversely affect our financial condition and results of operations by either extending coverage beyond our underwriting intent or by increasing the number and size of claims. In some instances, these changes may not become apparent until some time after we have issued insurance contracts that are affected by the changes.

For further discussion of our loss and loss adjustment reserves, including our asbestos and environmental reserves, see **Loss and Loss Adjustment Expenses** in "CRITICAL ACCOUNTING ESTIMATES" in Item 1.

*We may not maintain favorable financial strength or creditworthiness ratings which could adversely affect our ability to conduct business.*

Third party rating agencies assess and rate the financial strength of insurers and reinsurers. Financial strength ratings are used by insurers and reinsurers and insurance and reinsurance intermediaries as an important means of assessing the financial strength and quality of insurers and reinsurers. The financial strength ratings assigned by rating agencies to insurance or reinsurance companies are based upon factors relevant to policyholders and are not directed toward the protection of investors. Financial strength ratings by rating agencies are not ratings of securities or recommendations to buy, hold, or sell any security and may be withdrawn or revised at any time at the discretion of the assigning agency. Rating agencies also evaluate the general creditworthiness of debt securities issued by companies. Creditworthiness ratings are used by existing or potential investors to assess the likelihood of repayment on a particular debt issue. Some of the criteria used by rating agencies to assign financial strength and creditworthiness ratings relate to general economic conditions and other circumstances outside the rated company's control.

Rating agencies periodically evaluate us to confirm that we continue to meet the criteria of the ratings previously assigned to us. See **RATINGS** in Item 1 for a summary of financial strength ratings on our significant subsidiaries and creditworthiness ratings on our Senior Notes. A downgrade or withdrawal of our financial strength ratings could severely limit or prevent us from writing any new insurance or reinsurance policies. A downgrade or withdrawal of our creditworthiness ratings could severely limit our ability to raise new debt or could make new debt more costly and/or have more restrictive conditions.

*Our debt, preferred stock and related service obligations could adversely affect our business.*

As of December 31, 2005, we had approximately \$781 million face value of indebtedness and \$320 million face value of mandatorily redeemable preferred stock outstanding.

Our ability to meet our debt, preferred stock and related service obligations will depend on our future performance, which will be affected by financial, business, economic and other factors. We will not be able to control many of these factors, such as economic conditions and governmental regulation. We cannot be certain that our earnings will be sufficient to allow us to pay the principal and interest on our debt, the redemption value and dividends on our preferred stock and meet our other obligations. If we do not have enough cash, we may be required to refinance all or part of our existing debt and preferred stock, sell assets, borrow more cash or sell equity. We cannot assure you that we will be able to accomplish any of these alternatives on terms acceptable to us, if at all.

We could incur additional indebtedness and issue additional preferred stock in the future. To the extent new debt, new preferred stock and other obligations are added to our and our subsidiaries' current debt and preferred stock levels, the risks described in the previous paragraph would increase.

***Our investment portfolio may suffer reduced returns or losses which could adversely affect our results.***

Investment returns are an important part of our growth in tangible book value, and fluctuations in the fixed income or equity markets could impair our results of operations, financial condition or cash flows. A significant period of time normally elapses between the receipt of insurance premiums and the disbursement of insurance claims. During this time, we generate investment income, consisting primarily of interest earned on fixed maturity investments and dividends earned on equity securities, by investing our capital as well as insurance premiums allocated to support unpaid loss and loss adjustment expense reserves. We also recognize unrealized investment gains and losses on the securities we hold in our investment portfolio and we generate investment gains and losses from sales of securities from our investment portfolio. The investment income and fair market value of our investment portfolio are affected by general economic and market conditions, including fluctuations in interest rates and volatility in the stock market. These conditions are outside of our control and could adversely affect the value of our investments and our results.

Our investment portfolio consists of fixed maturity investments, common equity securities, warrants to acquire common equity securities and other investments, principally limited partnership and private hedge fund securities. Our investment selections are designed to maximize after-tax total risk-adjusted return over the long term; however, investing entails substantial risks. There can be no assurance that we will achieve our investment objectives, and our investment performance may vary substantially over time.

***The property and casualty insurance and reinsurance industry is highly competitive and we may not be able to compete effectively in the future.***

The property and casualty insurance industry is highly competitive and has, from time to time, experienced severe price competition in the past. OneBeacon competes with numerous regional and national insurance companies, including The St. Paul Travelers Companies, Zurich Insurance Group, CNA Financial, the Hartford Financial Services Group, Hanover Insurance Group, W.R. Berkley Corporation, The Chubb Corporation, Progressive Insurance, Allstate Insurance, Liberty Mutual, The Robert Plan Corporation, American International Group and the regional Farm Bureaus. White Mountains Re competes with numerous reinsurance companies throughout the world, including Munich Re, Swiss Re, XL Re, Transatlantic Re, Hannover Re, Everest Re, Partner Re and Lloyds. Some of these competitors have greater financial resources than we do and have established long-term and continuing business relationships throughout the insurance and reinsurance industries, which can be a significant competitive advantage. In addition, substantial new capital and competitors have entered the reinsurance market in recent months, and we expect to face further competition in the future. If we are unable to maintain our competitive position, our businesses may be adversely affected and we may not be able to compete effectively in the future.

***We may suffer losses from unfavorable outcomes from litigation and other legal proceedings***

White Mountains, like the insurance and reinsurance industries in general, in the ordinary course of its business is subject to litigation and other legal proceedings, the outcomes of which are uncertain. In the event of an unfavorable outcome in one or more legal matters, our ultimate liability may be in excess of amounts we have currently reserved for and such additional amounts may be material to our results of operations and financial condition. For a description of our current non-ordinary course material legal proceedings, see "**Item 3. Legal Proceedings.**"

*Regulation may restrict our ability to operate.*

The insurance and reinsurance industries are subject to extensive regulation under U.S., state and foreign laws. Governmental agencies have broad administrative power to regulate many aspects of the insurance business, which include premium rates, marketing practices, advertising, policy forms and capital adequacy. These agencies are concerned primarily with the protection of policyholders rather than shareholders. Insurance laws and regulations impose restrictions on the amount and type of investments, prescribe solvency standards that must be met and maintained and require the maintenance of reserves. In addition, state insurance holding company statutes generally require prior approval of changes of control of an insurer or its holding company.

Recently, the insurance industry has been heavily scrutinized by various regulatory bodies, including State Attorneys General and state insurance departments, for alleged illegal conduct surrounding a number of topics, including producer compensation arrangements and the sale and use of finite reinsurance.

During 2004 and 2005, OneBeacon received subpoenas from the Attorneys General of Massachusetts, New York and Connecticut requesting documents and seeking information relating to the conduct of business between insurance brokers and OneBeacon. Some of our other subsidiaries have also received information requests from various state insurance departments regarding producer compensation arrangements. We have cooperated with all of these subpoenas and information requests. We believe these requests to be part of the industry-wide investigation regarding industry sales practices.

***In recent years we have successfully created shareholder value through acquisitions and dispositions of insurance and reinsurance entities. We may not be able to continue to create shareholder value through such transactions in the future.***

In the past several years, we have completed numerous acquisitions and dispositions of insurance and reinsurance entities, many of which have contributed significantly to our growth in tangible book value. Failure to identify and complete future acquisition and disposition opportunities could limit our ability to achieve our target returns. Even if we were to identify and complete future acquisition opportunities, there is no assurance that such acquisitions will ultimately achieve their anticipated benefits.

***Changes in tax laws may adversely affect our results of operations and financial condition.***

Changes in the tax laws in the jurisdictions that we operate could adversely affect our results. In particular, from time to time legislation has been discussed or proposed in the United States that would tax us or our shareholders differently than other foreign corporations or their shareholders. In addition, if U.S. taxing authorities determined that our non-U.S. operations were subject to taxation in the United States, our results of operations and financial condition could be adversely affected.

***We have significant foreign operations that expose us to certain additional risks, including foreign currency risks and political risk.***

White Mountains Re, in particular Sirius International, conducts a significant portion of its business outside of the United States. As a result, a substantial portion of our assets, liabilities, revenues and expenses are denominated in currencies other than the U.S. dollar and are therefore subject to foreign currency risk. Our foreign currency risk cannot be eliminated entirely and significant changes in foreign exchange rates may adversely affect our financial condition or our results of operations.

Our foreign operations are also subject to legal, political and operational risks that may be greater than those present in the United States. As a result, our operations at these foreign locations could be temporarily or permanently disrupted.

***We depend on our key personnel to manage our business effectively and they may be difficult to replace.***



Our performance substantially depends on the efforts and abilities of our management team and other executive officers and key employees. Furthermore, much of our competitive advantage is based on the expertise, experience and know-how of our key management personnel. We do not have fixed term employment agreements with any of our key employees and the loss of one or more of these key employees could have a negative effect on our business, results of operations and financial condition. Our success also depends on the ability to hire and retain additional personnel. Difficulty in hiring or retaining personnel could adversely affect our future operating performance.

### **Item 1B. Unresolved Staff Comments**

As of the date of this report, the Company had no unresolved written comments from the Commission staff regarding its periodic or current reports under the Exchange Act.

### **Item 2. Properties**

The Company maintains two professional offices in Hamilton, Bermuda which serve as its headquarters and its registered office. White Mountains Re's headquarters is in Hamilton, Bermuda with an additional office in Jersey City, New Jersey, which also serves as White Mountains' principal executive office. Folksamerica is headquartered in New York, New York with branch offices in various cities throughout the United States. Sirius International is headquartered in Stockholm, Sweden with various branch offices in Europe and Asia. WMU maintains offices in Dublin, Ireland and Hamilton, Bermuda. The home office of OneBeacon is located in Boston, Massachusetts, with branch offices in various cities throughout the United States. Esurance is headquartered in San Francisco, California with various offices throughout the United States. In addition, the Company maintains professional offices in Hanover, New Hampshire and Guilford, Connecticut, which house its investment and corporate finance functions.

The Company's headquarters, registered office, principal executive office and investment and corporate finance offices are leased. Sirius International's home office in Sweden and substantially all of its branch offices, as well as WMU's offices in Ireland and Bermuda, are leased. Folksamerica's home office and its branch offices are leased as well. The home office of OneBeacon and most of its branch offices are leased with the exception of branch offices located in New York, which are owned by OneBeacon. During 2005, OneBeacon purchased an office building in Canton, Massachusetts, which it expects to occupy as its home office in late 2006. Management considers its office facilities suitable and adequate for its current level of operations.

### **Item 3. Legal Proceedings**

White Mountains, and the insurance and reinsurance industry in general, are subject to litigation and arbitration in the normal course of business. Other than those items listed below, White Mountains was not a party to any material litigation or arbitration other than as routinely encountered in claims activity, none of which is expected by management to have a material adverse effect on its financial condition and/or cash flows.

In August 2005, OneBeacon received a civil investigative demand from the Attorney General of the Commonwealth of Massachusetts requesting documents and seeking information relating to the conduct of business between insurance brokers and OneBeacon. Previously, OneBeacon received similar demands from the Attorneys General of the State of New York and the State of Connecticut. Subsidiaries of the Company have also received information requests from various state insurance departments regarding producer compensation arrangements. White Mountains believes these requests are part of the ongoing, industry-wide investigation regarding industry sales practices.

On May 15, 2002, The Robert Plan Corporation and several of its subsidiaries filed a lawsuit against the Company, certain of its subsidiaries and several individuals employed by the subsidiaries. The suit alleges that the defendants misappropriated confidential information of the plaintiffs and used such information to enter into the New York automobile assigned risk business in direct competition with the plaintiffs. The plaintiffs

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are demanding damages of approximately \$185 million, which they allege represents two years of their lost profits in the subject business. White Mountains, its named subsidiaries and employees do not believe they engaged in any improper or actionable conduct. White Mountains and its subsidiaries have no reason to believe they have any liability to The Robert Plan Corporation and intend to vigorously defend the lawsuit. In addition, OneBeacon has brought a counterclaim against the plaintiffs that it believes to be meritorious. OneBeacon is seeking compensatory damages of \$9 million as a result of the breach by the plaintiffs of the LAD servicing contract that OneBeacon had entered into with them. The case is currently scheduled for trial July 10, 2006.

In August 2000, Aramarine Brokerage, Inc. ( Aramarine ), a former insurance broker of OneBeacon s, filed a lawsuit alleging that OneBeacon had wrongfully terminated its business relationship with Aramarine. The suit originally claimed \$410 million in compensatory damages for lost commissions, although Aramarine has reduced its demand to \$158 million. OneBeacon does not believe it has engaged in any actionable conduct. During 2004,

OneBeacon prevailed on a motion for summary judgment to dismiss the plaintiff's claim. OneBeacon expects the plaintiff to appeal the summary judgment upon resolution of OneBeacon's counterclaim for return commission.

OneBeacon is in dispute with Liberty Mutual over certain costs Liberty Mutual claims it incurred in connection with the Liberty Agreement. Liberty Mutual asserts that these costs are part of unallocated loss adjustment expenses ( ULAE ) due Liberty Mutual under the Liberty Agreement. Liberty Mutual further asserts that ULAE on charges previously billed to and settled by OneBeacon since the inception of the Liberty Agreement should be retroactively recast in addition to changing the calculation of ULAE charges for the period not yet settled. OneBeacon believes that the recast charges, which are significantly higher than prior ULAE calculations, and the calculation of ULAE charges for the period not yet settled are inconsistent with the terms of the Liberty Agreement and with standard industry definitions of ULAE. The amount of additional ULAE Liberty Mutual claims that it incurred under the Liberty Agreement totals approximately \$65 million. Liberty Mutual has since invoked the provisions of offset under the Liberty Agreement and has netted amounts billed under the ULAE dispute against amounts otherwise payable to OneBeacon. As of December 31, 2005, OneBeacon has recorded ULAE expenses due Liberty Mutual on a basis that it believes is consistent with the terms of the Liberty Agreement and with standard industry definitions of ULAE.

OneBeacon also has a claim against Liberty Mutual in the Philadelphia Court of Common Pleas in which it asserts that Liberty Mutual's claims practices under the Liberty Agreement from 2001 to 2004 were inconsistent with industry standards.

#### **Item 4. Submission of Matters to a Vote of Security Holders**

There were no matters submitted to a vote of the Company's shareholders during the fourth quarter of 2005.

**Executive Officers of the Registrant and its Subsidiaries (As of March 7, 2006)**

Name	Position	Age	Executive officer since
Steven E. Fass	President and CEO	60	2002
Charles B. Chokel	Managing Director of White Mountains Capital, Inc.	52	2002
David T. Foy	Executive Vice President and Chief Financial Officer	39	2003
G. Thompson Hutton	President and CEO of White Mountains Re	50	2006
Robert R. Lusardi	Executive Vice President and Managing Director of White Mountains Capital, Inc.	49	2005
T. Michael Miller	President and CEO of OneBeacon	47	2005
J. Brian Palmer	Chief Accounting Officer	33	2001
Robert L. Seelig	Vice President and General Counsel	37	2002
Gary C. Tolman	President and CEO of Esurance	54	2005

All executive officers of the Company and its subsidiaries are elected by the Board for a term of one year or until their successors have been elected and have duly qualified. Information with respect to the principal occupation and relevant business experience of the Executive Officers follows:

**Mr. Fass** has been a director of the Company since 2000. Mr. Fass has served as President and CEO of the Company since October 2005. Mr. Fass previously served as President and CEO of White Mountains Re from 2004 to February 2006 and as President and CEO of Folksamerica and its subsidiaries from 1984 to 2004. He joined Folksamerica as its Vice President, Treasurer and Chief Financial Officer in 1980. Mr. Fass also serves as Chairman of OneBeacon, White Mountains Re and Esurance.

**Mr. Chokel** has served as Managing Director of White Mountains Capital, Inc. since September 2003. Prior to that he served as Managing Director and Chief Administrative Officer of OneBeacon since January 2003 and as Managing Director since March 2002. Prior to joining OneBeacon, Mr. Chokel served as Executive Vice President and Chief Financial Officer of Conesco, Inc. from March 2001 to March 2002 and as Co-CEO of The Progressive Corporation from January 1999 to January 2001. Mr. Chokel was with Progressive since 1978.

**Mr. Foy** was appointed Executive Vice President and Chief Financial Officer of the Company in April 2003. Prior to joining White Mountains in 2003, Mr. Foy served as Senior Vice President and Chief Financial Officer of Hartford Life Inc. and joined that company in 1993. Prior to joining Hartford Life, Mr. Foy was with Milliman and Robertson, an actuarial consulting firm. Mr. Foy also serves as the Chairman of Symetra.

**Mr. Hutton** was appointed President and CEO of White Mountains Re in February 2006. Prior to joining White Mountains, since 2000 Mr. Hutton served as a board member and consultant to private equity investors and their portfolio companies, first as a Venture Partner with Trident Capital and then as Managing Partner of Thompson Hutton, LLC. From 1990-2000, Mr. Hutton served as President and CEO of Risk Management Solutions, Inc. and was formerly a management consultant at McKinsey and Company, Inc. Mr. Hutton is also a director of Safeco Corp.

**Mr. Lusardi** was appointed Executive Vice President and Managing Director of White Mountains Capital, Inc. in February 2005. Prior to joining White Mountains, Mr. Lusardi was an Executive Vice President of XL Capital Ltd, most recently as Chief Executive of Financial Products and Services. Prior to joining XL Capital Ltd, Mr. Lusardi was a Managing Director at Lehman Brothers, where he was employed from 1980 to 1998. Mr. Lusardi also serves as a Director of Symetra and Primus Guaranty, Ltd.

**Mr. Miller** was appointed President and CEO of OneBeacon in July 2005 and joined OneBeacon as its Chief Operating Officer in April 2005. Prior to joining White Mountains, Mr. Miller spent 10 years at St. Paul Travelers, most recently as Co-Chief Operating Officer. Prior to joining St. Paul Travelers, Mr. Miller spent 14 years with The Chubb Corporation.

**Mr. Palmer** has served as Chief Accounting Officer since 2001 and previously served as Controller of a subsidiary of White Mountains from 1999 to 2001. Prior to joining White Mountains in 1999, Mr. Palmer was with PricewaterhouseCoopers LLP.

**Mr. Seelig** is Vice President and General Counsel of the Company. Prior to joining White Mountains in September 2002, Mr. Seelig was with the law firm of Cravath, Swaine & Moore. Mr. Seelig also serves as a Director of MSA.

**Mr. Tolman** has served as President and CEO of Esurance since 2000. Prior to joining Esurance, Mr. Tolman was with Talegen Holdings for 6 years, serving most recently as its President. Prior to joining Talegen, Mr. Tolman was with Fireman's Fund Corporation for more than 15 years.

## PART II

### Item 5. Market for the Company's Common Equity, Related Shareholder Matters and Issuer Purchase of Equity Securities

As of March 3, 2006, there were 368 registered holders of White Mountains' common shares, par value \$1.00 per share.

During 2005 and 2004, the Company declared and paid cash dividends on common shares of \$8.00 and \$1.00 per common share, respectively. During 2005, the Company amended its dividend payment policy to provide for quarterly dividends payable, dependent on the Company's financial position and the regularity of its cash flows.

Common shares are listed on the New York Stock Exchange (symbol WTM) and the Bermuda Stock Exchange (symbol WTM-BH). The quarterly range of the high and low sales price for common shares during 2005 and 2004 is presented below:

Quarter ended:	2005		2004	
	High	Low	High	Low
December 31	\$ 638.99	\$ 555.00	\$ 659.00	\$ 495.00
September 30	711.99	583.60	531.00	467.00
June 30	677.50	564.50	559.50	474.01
March 31	695.00	582.00	527.00	451.50

No repurchases of common shares were made by or on behalf of the Company during the fourth quarter of 2005.

**Item 6. Selected Financial Data**

Selected consolidated income statement data and ending balance sheet data for each of the five years ended December 31, 2005, follows:

\$ in millions, except share and per share amounts	Year Ended December 31,				
	2005	2004	2003	2002	2001 (a)
<b>Income Statement Data:</b>					
Revenues	\$ 4,632	\$ 4,553	\$ 3,794	\$ 4,208	\$ 3,234
Expenses	4,339	4,305	3,422	4,089	3,662
Pre-tax earnings (loss)	293	248	372	119	(428)
Income tax (provision) benefit	(37)	(47)	(127)	(11)	179
Accretion and dividends on preferred stock of subsidiaries			(21)(c)	(41)	(23)
Equity in earnings of unconsolidated affiliates	34	37	57	14	1
Net income (loss) from continuing operations	290	238	281	81	(271)
Cumulative effect of changes in accounting principles				660(b)	
Extraordinary gains		181(d)		7	12
Net income (loss)	\$ 290	\$ 419	\$ 281	\$ 748	\$ (259)
Net income (loss) from continuing operations per share:					
Basic	\$ 26.96	\$ 24.05	\$ 26.48	\$ 7.47	\$ (86.52)
Diluted	\$ 26.56	\$ 22.67	\$ 23.63	\$ 6.80	\$ (86.52)
<b>Balance Sheet Data:</b>					
Total assets	\$ 19,418	\$ 19,015	\$ 15,882	\$ 17,267	\$ 18,410
Short-term debt				33	358
Long-term debt	779	783	743	760	767
Deferred credits				(b)	683
Convertible preference shares				219	
Mandatorily redeemable preferred stock of subsidiaries	234	212	195(c)	181	170
Common shareholders' equity	3,833	3,884	2,979	2,408	1,445
Book value per share (e)	\$ 347.00	\$ 349.60	\$ 293.15	\$ 254.52	\$ 160.36
Fully converted tangible book value per share (f)	\$ 342.51	\$ 342.52	\$ 291.27	\$ 258.82	\$ 225.81
<b>Share Data:</b>					
Cash dividends paid per common share	\$ 8.00	\$ 1.00	\$ 1.00	\$ 1.00	\$ 1.00
Ending common shares (000 s)(g)	10,779	10,773	9,007	8,351	8,245
Ending equivalent common shares (000 s)(h)	34	47	1,775	2,455	1,803
Ending common and equivalent common shares (000 s)	10,813	10,819	10,782	10,806	10,048

(a) Includes the acquisition of OneBeacon on June 1, 2001 and its results of operations from that date through December 31, 2001. In connection with the OneBeacon Acquisition, White Mountains issued \$1,085 million in debt. White Mountains also issued preferred stock of subsidiaries, warrants to acquire common shares and Convertible Preference Shares for total proceeds of \$758 million. For a description of the historical factors affecting OneBeacon's loss and LAE reserves prior to the OneBeacon Acquisition, see Non-Asbestos and Environmental Reserves under the caption Loss and Loss Adjustment Expense Reserves in the OneBeacon section of the business description contained within the Company's Amendment No. 6 to Form S-3 dated July 17, 2003 (the Form S-3). Such portion of the Form S-3 is incorporated by reference into this Form 10-K.

(b) In accordance with its adoption of Statement of Financial Accounting Standard (SFAS) No. 141, Business Combinations, the Company recognized all of its outstanding deferred credits on January 1, 2002.



- (c) In accordance with its adoption of SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity ( SFAS 150 ), on July 1, 2003, the Company reclassified its outstanding mandatorily redeemable preferred stock from mezzanine equity to liabilities on its balance sheet and, beginning in the third quarter of 2003, White Mountains began presenting all accretion and dividends on its mandatorily redeemable preferred stock as interest expense. See Note 1.
- (d) Extraordinary gains in 2004 resulted from the excess of the fair value over the cost of net assets acquired in the Sirius, Symetra, Tryg-Baltica and Sierra transactions.
- (e) Includes the dilutive effects of outstanding incentive options to acquire common shares ( Options ) and, for years prior to 2004, warrants to acquire common shares.
- (f) Book value per share plus unamortized deferred credits less goodwill and the equity in net unrealized gains from Symetra's fixed income portfolio per common and equivalent common share. The 2002 fully converted tangible book value per share assumes outstanding convertible preference shares to be equivalent common shares.
- (g) During 2003, 677,966 common shares were issued in satisfaction of Convertible Preference Shares. During 2004, 1,724,200 common shares were issued in satisfaction of warrants exercised.
- (h) Includes outstanding Convertible Preference Shares, Options and warrants to acquire common shares, when applicable.

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

The following discussion contains forward-looking statements. White Mountains intends statements that are not historical in nature, which are hereby identified as forward-looking statements, to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. White Mountains cannot promise that its expectations in such forward-looking statements will turn out to be correct. White Mountains actual results could be materially different from and worse than its expectations. See **FORWARD-LOOKING STATEMENTS** for specific important factors that could cause actual results to differ materially from those contained in forward-looking statements.

The following discussion also includes three non-GAAP financial measures, adjusted comprehensive net income (loss), fully converted tangible book value per common and equivalent share and tangible capital, that have been reconciled to their most comparable GAAP financial measures (see page 56). White Mountains believes these measures to be more relevant than comparable GAAP measures in evaluating White Mountains financial performance and condition.

**RESULTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2005, 2004 and 2003****Overview**

White Mountains ended 2005 with a fully converted tangible book value per common share of \$343, which represents an increase of 2% (including dividends) over the fully converted tangible book value per common share of \$343 as of December 31, 2004. During 2004, fully converted tangible book value per common share increased by 18% (including dividends) from \$291 as of December 31, 2003.

During 2005, White Mountains experienced \$288 million in after-tax losses from hurricanes Katrina, Rita and Wilma, a \$104 million after-tax losses (net of dividends received) from the Company's investment in Montpelier and \$70 million of after-tax unrealized foreign currency losses that adversely impacted fully converted tangible book value per common share. These losses offset solid underwriting results produced by OneBeacon. Esurance also had a good year in 2005 while growing its premiums 75%.

**Fully Converted Tangible Book Value Per Share**

The following table presents the Company's tangible book value per share for the years ended December 31, 2005, 2004, and 2003 and reconciles this non-GAAP measure to the most comparable GAAP measure:

	2005	December 31, 2004	2003
<b>Book value per share numerators (in millions):</b>			
Common shareholders' equity	\$ 3,833.2	\$ 3,883.9	\$ 2,979.2

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Proceeds from assumed exercise of outstanding warrants			300.0
Benefits to be received from share obligations under employee benefit plans	5.1	6.7	7.0
Remaining accretion of subsidiary preferred stock to face value	(86.0)	(108.1)	(125.5)
Book value per share numerator	3,752.3	3,782.5	3,160.7
Equity in net unrealized gains from Symetra's fixed maturity portfolio	(24.2)	(56.6)	
Goodwill	(24.4)	(20.0)	(20.3)
Fully converted tangible book value per common and equivalent share numerator	\$ 3,703.7	\$ 3,705.9	\$ 3,140.4

**Book value per share denominators (in thousands of shares):**

Common shares outstanding	10,779.2	10,772.8	9,007.2
Common shares issuable upon exercise of outstanding warrants			1,724.2
Share obligations under employee benefit plans	34.3	46.5	50.6
Fully converted tangible book value per common and equivalent share	10,813.5	10,819.3	10,782.0
Book value per share	\$ 347.00	\$ 349.60	\$ 293.15
Fully converted tangible book value per common and equivalent share	342.51	342.52	291.27

**Review of Consolidated Results**

A summary of White Mountains' consolidated financial results for the years ended December 31, 2005, 2004 and 2003 follows:

Millions	2005	Year Ended December 31, 2004	2003
Gross written premiums	\$ 4,601.6	\$ 4,792.1	\$ 3,823.4
Net written premiums	\$ 3,776.1	\$ 3,904.8	\$ 3,007.7
<b>Revenues</b>			
Earned insurance and reinsurance premiums	\$ 3,798.6	\$ 3,820.5	\$ 3,137.7
Net investment income	491.5	360.9	290.9
Net realized investment gains	112.6	181.1	162.6
Other revenue	229.2	190.5	202.6
Total revenues	4,631.9	4,553.0	3,793.8
<b>Expenses</b>			
Losses and LAE	2,858.2	2,591.1	2,138.1
Insurance and reinsurance acquisition expenses	761.2	744.4	615.0
Other underwriting expenses	428.9	520.4	347.1
General and administrative expenses	156.8	309.3	201.8
Accretion of fair value adjustment to loss and LAE reserves	36.9	43.3	48.6
Interest expense - debt	44.5	49.1	48.6
Interest expense - dividends and accretion on preferred stock	52.4	47.6	22.3
Total expenses	4,338.9	4,305.2	3,421.5
<b>Pre-tax income</b>	\$ 293.0	\$ 247.8	\$ 372.3
Income tax expense	(36.5)	(47.0)	(127.6)
Accretion and dividends on mandatorily redeemable preferred stock of subsidiaries			(21.5)
Equity in earnings of unconsolidated affiliates	33.6	37.4	57.4
<b>Net income before accounting changes and extraordinary items</b>	\$ 290.1	\$ 238.2	\$ 280.6
Excess of fair value of acquired net assets over cost		180.5	
<b>Net income</b>	\$ 290.1	\$ 418.7	\$ 280.6
Other comprehensive income (loss)	(254.1)	176.5	79.0
<b>Comprehensive net income</b>	\$ 36.0	\$ 595.2	\$ 359.6
Less: Change in net unrealized gains from Symetra's fixed maturity portfolio	32.4	(56.6)	
<b>Adjusted comprehensive net income</b>	\$ 68.4	\$ 538.6	\$ 359.6

**Consolidated Results - Year Ended December 31, 2005 versus Year Ended December 31, 2004**

White Mountains reported adjusted comprehensive net income of \$68 million for 2005, compared to \$539 million in 2004 and \$360 million in 2003. Net income was \$290 million in 2005, compared to \$419 million in 2004 and \$281 million in 2003. The reduction in 2005 adjusted comprehensive net income resulted primarily from the aforementioned hurricane losses and Montpelier investment decline, as well as the impact of \$181 million in transaction gains reported in 2004, primarily from the Sirius Acquisition.

White Mountains' total revenues increased by 2% in 2005 compared to 2004, mainly from a \$131 million increase in net investment income, primarily due to a \$74 million special dividend from Montpelier in 2005. Earned premiums decreased by 1% in 2005, primarily due to a decrease at OneBeacon, which was partially offset by increases at White Mountains Re and Esurance, and net realized investment gains

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decreased by \$69 million in 2005, primarily due to losses in the value of the Company's investment in Montpelier warrants during 2005.

White Mountains' total expenses also increased by 1% for 2005 as a \$267 million increase in loss and LAE, primarily due to the Gulf Coast hurricanes, was partially offset by a \$153 million decrease in general and

administrative expenses, primarily due to decreased incentive compensation expense resulting from a 14% decline in White Mountains' share price during the year.

***Consolidated Results - Year Ended December 31, 2004 versus Year Ended December 31, 2003***

White Mountains' total revenues increased by 20% in 2004 compared to 2003. Growth in revenues was driven by the 22% increase in earned premiums due to the Sirius Acquisition and Atlantic Specialty transactions. Net investment income grew 24% in 2004 primarily due to the income earned on the additional invested assets acquired in the Sirius Acquisition offset by decreased net invested assets at OneBeacon.

White Mountains' total expenses grew 26% for 2004 as loss and LAE, insurance acquisition and underwriting expenses were all up due to the Sirius Acquisition and Atlantic Specialty transactions. General and administrative costs were up 53% in 2004, primarily due to an increase in incentive compensation accruals, which were driven by a 41% rise in White Mountains' share price during the year.

White Mountains' net income in 2004 also benefitted from \$181 million in transaction gains: \$111 million from the Sirius Acquisition, \$41 million for the Symetra investment, \$20 million from the Tryg-Baltica acquisition and \$9 million from the Sierra Group acquisition.

***Income Taxes***

The Company is domiciled in Bermuda and has subsidiaries domiciled in several countries. The majority of the Company's worldwide operations are taxed in the United States. Income earned or losses incurred by non-U.S. companies will generally be subject to an overall effective tax rate lower than that imposed by the United States.

The income tax provision related to pretax earnings for 2005, 2004 and 2003 represents an effective tax rate of 12.5%, 19.0% and 34.3%, respectively. White Mountains' effective tax rate for 2005 was lower than the U.S. statutory rate of 35% primarily due to income generated in jurisdictions other than the United States. White Mountains' effective tax rate for 2004 was lower than the U.S. statutory rate of 35% primarily due to income generated in jurisdictions other than the United States and the recognition of foreign tax credits, offset by taxes incurred from an internal restructuring of the company. White Mountains' effective tax rate for 2003 was lower than the U.S. statutory rate of 35% primarily due to income generated in jurisdictions other than the United States.

During 2005, White Mountains was advised that the Joint Committee on Taxation approved the United States Internal Revenue Service audit of White Mountains' 1997-2000 tax years, which contained no significant adjustments to the tax returns filed by White Mountains. This audit included the redomestication of White Mountains to Bermuda in 1999.

**I. Summary of Operations By Segment**

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White Mountains conducts its operations through four segments: (1) OneBeacon, (2) White Mountains Re, (3) Esurance and (4) Other Operations. White Mountains manages all of its investments through its wholly-owned subsidiary, WM Advisors, therefore, a discussion of White Mountains consolidated investment operations is included after the discussion of operations by segment. White Mountains segment information is presented in **Note 13 "Segment Information"** to the Consolidated Financial Statements.

**OneBeacon**

Financial results for OneBeacon for the years ended December 31, 2005, 2004 and 2003 follows:

Millions	Year Ended December 31,		
	2005	2004	2003
Gross written premiums	\$ 2,266.5	\$ 2,657.5	\$ 2,250.9
Net written premiums	\$ 2,121.1	\$ 2,459.1	\$ 1,972.5
Earned insurance and reinsurance premiums	\$ 2,118.4	\$ 2,378.5	\$ 2,160.3
Net investment income	238.1	221.4	223.7
Net realized investment gains	123.8	129.6	127.0
Other revenue	134.0	141.8	90.5
Total revenues	2,614.3	2,871.3	2,601.5
Losses and LAE	1,401.5	1,545.2	1,475.6
Insurance and reinsurance acquisition expenses	390.7	442.3	394.2
Other underwriting expenses	283.1	369.2	258.7
General and administrative expenses	88.4	122.2	67.6
Interest expense on debt	1.4	1.0	.3
Total expenses	2,165.1	2,479.9	2,196.4
<b>Pre-tax earnings</b>	<b>\$ 449.2</b>	<b>\$ 391.4</b>	<b>\$ 405.1</b>

The following tables provide GAAP ratios, net written premiums and earned insurance premiums for OneBeacon's ongoing businesses and in total for the years ended December 31, 2005, 2004, and 2003:

**Twelve Months Ended December 31, 2005**

	Specialty	Personal	Commercial	Total (1)
<i>GAAP Ratios:</i>				
Loss and LAE	64%	56%	55%	66%
Expense	31%	29%	38%	32%
Total Combined	95%	85%	93%	98%

**Dollars in millions**

Net written premiums	\$ 840.2	\$ 618.7	\$ 610.9	\$ 2,121.1
Earned insurance premiums	\$ 789.6	\$ 655.9	\$ 622.5	\$ 2,118.4

**Twelve Months Ended December 31, 2004**

	Specialty	Personal	Commercial	Total (1)
<i>GAAP Ratios:</i>				
Loss and LAE	59%	62%	56%	65%
Expense	31%	32%	41%	34%
Total Combined	90%	94%	97%	99%

**Dollars in millions**

Net written premiums	\$ 848.5	\$ 724.7	\$ 807.1	\$ 2,459.1
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Earned insurance premiums \$ 812.0 \$ 723.8 \$ 703.3 \$ 2,378.5

Twelve Months Ended December 31, 2003

	Specialty	Personal	Commercial	Total (1)
<i>GAAP Ratios:</i>				
Loss and LAE	54%	61%	61%	68%
Expense	32%	30%	34%	30%
Total Combined	86%	91%	95%	98%

**Dollars in millions**

Net written premiums	\$ 733.7	\$ 676.8	\$ 426.7	\$ 1,972.5
Earned insurance premiums	\$ 694.9	\$ 744.7	\$ 432.0	\$ 2,160.3

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(1) Includes results from reciprocals (consolidated beginning April 1, 2004) and run-off operations. Results from reciprocals are net of business assumed by OneBeacon, which is contained in Personal Lines.

*OneBeacon Results - Year Ended December 31, 2005 versus Year Ended December 31, 2004*

**Overview**

OneBeacon's pre-tax income for 2005 was \$449 million, compared to pre-tax income of \$391 million for 2004 and its combined ratio was 98% for 2005, compared to 99% for 2004. OneBeacon's 2005 results included \$69 million in losses related to hurricanes Katrina, Rita and Wilma, which impacted the combined ratio by 3 points, and \$95 million in adverse development, primarily relating to 2002 and prior accident years, which impacted the combined ratio by 5 points. Offsetting these items was a \$54 million gain from the settlement of OneBeacon's retiree medical plan, which reduced the combined ratio by a total of 3 points. The retiree medical plan, which had been frozen in 2002, was terminated and an independent trust was established and funded to provide benefits to covered participants. These actions relieved OneBeacon of its future retiree medical obligations and triggered recognition of the gain.

OneBeacon's 2004 results included \$31 million of hurricane losses, primarily from four hurricanes in the southeastern United States, and \$100 million in adverse development, primarily relating to 2002 and prior accident years, which impacted the loss ratio by a total of 6 points. The 2004 adverse development was partially offset by a release of approximately \$20 million of the New York assigned risk liability due to the shrinking of the New York assigned risk pool.

OneBeacon's total revenues decreased 9% in 2005 to \$2,614 million, compared to \$2,871 million in 2004, due principally to an 11% decline in earned premiums in 2005. The decrease in earned premiums was partially due to lower commercial lines premiums resulting from the sale of the renewal rights on most of OneBeacon's non-Atlantic Mutual New York commercial lines business to Tower Insurance Group late in 2004. As a result of this transaction, approximately \$110 million of premiums written in 2004 were subject to this renewal rights agreement and were not written by OneBeacon during 2005. OneBeacon's commercial lines also had a one-time premium increase of approximately \$135 million in 2004 from the assumption of unearned premium from the Atlantic Specialty transaction. In addition, personal lines premium decreased in 2005 due to lower volumes in Massachusetts and New York. New Jersey Skylands Insurance also had lower premiums in 2005 as compared to 2004.

Net realized investment gains for 2005 included a realized loss of \$55 million due to an other-than-temporary impairment with respect to OneBeacon's investment in Montpelier common shares. During 2005, the market value of Montpelier common shares decreased from \$38.45 per share to \$18.90 per share. OneBeacon's original cost of this investment in 2001 was \$106 million, which was subsequently increased by \$65 million in equity in earnings recorded from 2001 to March 2004, the period in which OneBeacon accounted for the investment under the equity method of accounting. The impairment charge represented the difference between OneBeacon's GAAP cost of \$171 million and the investment's fair value of \$116 million at December 31, 2005.

Other revenue for 2005 included \$34 million in gains recorded from the sales of two subsidiaries, NFU and Traders and Pacific Insurance Company. During 2004, OneBeacon sold two of its subsidiaries, Potomac Insurance Company of Illinois (Potomac) and Western States Insurance Company (Western States), as well as its boiler inspection service business, for a total gain of \$22 million that was recognized in other revenue.

As a result of an actuarial review completed in the fourth quarter of 2005, OneBeacon reallocated some of its IBNR reserves from some of the ongoing lines of business to run-off operations. This shifted \$34 million of IBNR reserves from specialty lines (\$22 million) and personal lines (\$12 million) to run-off operations. This adjustment had no impact on OneBeacon's total combined ratio.

*Specialty Lines.* The specialty lines combined ratio for 2005 was 95%, compared to 90% for 2004. The increase in the combined ratio was mainly due to \$56 million of losses related to hurricanes Katrina, Rita and Wilma, which impacted the combined ratio by 7 points. These losses were incurred at OBSP (\$43 million), IMU (\$9 million) and Agri (\$4 million). Partially offsetting the hurricane losses was the reallocation of IBNR reserves to run-off operations and the settlement of the retiree medical plan, which reduced the combined ratio by a total of 4 points. In 2004, the combined ratio for specialty lines was adversely impacted by 1 point (\$11 million) from the four hurricanes in the southeastern United States. Net written premiums for 2005 were essentially flat at \$840 million, compared to \$849 million in 2004, as increases at OBPP, which included \$28 million of net written premium from a renewal rights agreement with Chubb Specialty Insurance that took effect during the third quarter of 2005, and OBSP were offset

by decreases at AutoOne, due to changes in the fee structure of LAD and takeout business in New York, and the sale of NFU in the third quarter.

**Personal Lines.** The personal lines combined ratio for 2005 was 85%, compared to 94% for 2004. The decrease in the combined ratio is primarily due to strong homeowners results, aided by favorable catastrophe experience resulting from a relatively mild winter and lack of northeast wind events, as well as lower frequencies in OneBeacon's legacy auto business. The settlement of the retiree medical plan favorably impacted the 2005 combined ratio by 4 points. In addition, the personal lines combined ratio was favorably impacted by 2 points from the reallocation of IBNR reserves to run-off operations.

**Commercial Lines.** The commercial lines combined ratio for 2005 was 93%, compared to 97% for 2004. The decrease in the combined ratio was primarily due to the settlement of the retiree medical plan, which reduced the combined ratio by 3 points. Commercial lines results in both 2005 and 2004 included storm losses of \$13 million, which impacted the combined ratio by 2 points in each period.

**Other Lines.** Other lines for 2005 included approximately \$107 million in adverse development, mainly from 2002 and prior accident years, which was primarily due to higher than anticipated defense costs and higher damages from liability assessments in general liability and multiple peril lines. In addition, during 2005, OneBeacon reallocated \$34 million of IBNR reserves from some of its ongoing lines of business to run-off lines.

#### ***OneBeacon Results - Year Ended December 31, 2004 versus Year Ended December 31, 2003***

##### **Overview**

OneBeacon's pre-tax income for 2004 was \$391 million, compared to pre-tax income of \$405 million for 2003 and its GAAP combined ratio was 99% for 2004, compared to 98% for 2003. The earnings and combined ratios for each period were relatively consistent as each period had solid performance for the current underwriting year, partially offset by some adverse development in prior year's reserves. In total, adverse development was \$100 million in 2004 (relating primarily to 2002 and prior accident years) and \$147 million in 2003 (relating primarily to 2000 and prior accident years). The 2004 development related primarily to personal auto liability, general liability and multiple peril reserves due in part to emerging trends in claims experienced in OneBeacon's run-off operations, as well as national account and program claims administered by third parties. These claim trends principally included higher defense costs and higher damages from liability assessments. The 2003 development was primarily related to construction defect claims. Adverse development in 2004 and 2003, respectively, was partially offset by the release of approximately \$20 million and \$30 million of the New York assigned risk liability due to the shrinking New York assigned risk pool.

OneBeacon's total revenues for 2004 increased by 10% compared to 2003, due principally to an increase in earned premiums resulting primarily from the Atlantic Specialty Transaction. Total revenues for 2004 were also impacted by an increase in other revenues due mainly to the commencement of two new private equity funds that are consolidated as a result of OneBeacon's significant investment in the funds.

OneBeacon's total expenses for 2004 increased 13% compared to 2003, primarily as a result of increased incentive compensation accruals driven by the 41% rise in White Mountains' share price in 2004, partially offset by the release of \$20 million of the New York assigned risk liability. The release of this liability resulted from the continued effects of favorable revisions to the structure of credit programs. General and administrative expenses were higher in 2004 primarily due to increased expenses resulting from the aforementioned commencement of two new private equity funds.

During the fourth quarter of 2004, OneBeacon sold two of its subsidiaries, Potomac and Western States, as well as its boiler inspection service business, and recognized gains on the sales of \$22 million through other revenues.

*Specialty Lines.* The specialty lines combined ratio was 90% for 2004, compared to 86% for 2003. The 2004 combined ratio was higher than 2003 primarily due to losses relating to the four storms in the southeastern United States that impacted IMU and better than expected weather losses in 2003. Written premiums for specialty lines were up 16% in 2004, driven by growth in writings at OBPP and AutoOne Insurance, as well as the introduction of OBSP in 2004, a new division offering coverages to the excess and surplus property market.

**Personal Lines.** The combined ratio for personal lines for 2004 was 94%, compared to 91% for 2003. The 2004 personal lines combined ratio was adversely impacted by 7 points as a result of increased incentive compensation accruals, partially offset by 3 points due to the reduction of the New York assigned risk liability. The 2003 combined ratio benefitted by 4 points due to a reduction of the New York assigned risk liability. Premiums in this line grew 7% due in part to improved production of new business and increased retention levels and also \$47 million in premiums assumed from New Jersey Skylands Insurance through a quota-share reinsurance agreement.

**Commercial Lines.** The combined ratio for commercial lines for 2004 was 97%, compared to 95% for 2003. The 2004 combined ratio was higher as a result of transition and integration costs related to the Atlantic Specialty Transaction and adverse results from its non-Atlantic Mutual New York commercial lines book. The 2004 loss ratio includes 2 points relating to the four storms in the southeastern United States, which primarily related to Atlantic Specialty business in that area. Excluding these losses, the commercial lines loss ratio significantly improved. Premiums in this line grew by 89% primarily due to the Atlantic Specialty Transaction.

#### White Mountains Re

Financial results and GAAP combined ratios for White Mountains Re for the years ended December 31, 2005, 2004 and 2003 follows:

Millions	Year Ended December 31,		
	2005	2004	2003
Gross written premiums	\$ 1,981.3	\$ 1,933.3	\$ 1,414.9
Net written premiums	\$ 1,304.1	\$ 1,246.3	\$ 885.7
Earned insurance and reinsurance premiums	\$ 1,371.6	\$ 1,265.5	\$ 845.8
Net investment income	148.9	98.5	50.4
Net realized investment gains	76.8	29.6	7.7
Other revenue	33.5	36.1	75.5
Total revenues	1,630.8	1,429.7	979.4
Losses and LAE	1,237.9	918.9	557.6
Insurance and reinsurance acquisition expenses	279.6	271.8	198.0
Other underwriting expenses	107.0	122.9	57.8
General and administrative expenses	12.4	15.1	19.6
Accretion of fair value adjustment to loss and LAE reserves	10.9	10.1	
Interest expense on debt	.4	3.8	2.0
Total expenses	1,648.2	1,342.6	835.0
<b>Pre-tax earnings (loss)</b>	\$ (17.4)	\$ 87.1	\$ 144.4
	Years Ended December 31,		
	2005	2004	2003
GAAP ratios:			
Loss and LAE	90%	73%	66%
Expense	28%	31%	30%
Total Combined	118%	104%	96%



*White Mountains Re Results - Year Ended December 31, 2005 versus Year Ended December 31, 2004*

White Mountains Re's pre-tax loss for 2005 was \$17 million, compared to pre-tax income of \$87 million for 2004, and its GAAP combined ratio was 118% for 2005, compared to 104% for 2004. White Mountains Re's 2005 results included pre-tax losses, net of reinstatements and reinsurance, of \$351 million from hurricanes Katrina, Rita and Wilma and \$33 million from European storm Erwin, which added a total of 28 points to the combined ratio. In addition, White Mountains Re recorded \$51 million of net unfavorable loss reserve development in 2005 (discussed below), which contributed 4 points to the loss ratio. During 2005, earnings from business segments not impacted by the property catastrophe events and increased net investment income partially offset these losses. Additionally, White Mountains Re's expense ratio decreased to 28% in 2005, from 31% in 2004, due mainly to a decrease in incentive compensation accruals. White Mountains Re's 2004 results included \$135 million of pre-tax losses, net of reinstatements and reinsurance, from the four hurricanes that affected the southeastern United States and the tsunami that impacted South Asia, which added a total of 11 points to the combined ratio.

White Mountains Re's gross written premiums increased in 2005 by \$48 million, or 2.5%, and net written premiums increased by \$58 million, or 4.7%, over the prior year. The increase was due primarily to Sirius, which was acquired in the second quarter of 2004 and contributed nine months of premiums in 2004 versus twelve months in 2005, partially offset by decreased premium volume at both Sirius International and Folksamerica as a result of the general softness in the reinsurance market prior to the Gulf Coast hurricanes.

White Mountains Re recorded \$51 million of net unfavorable loss reserve development in 2005, the majority of which resulted from a detailed, ground-up asbestos study completed by White Mountains Re in 2005. The study analyzed all insureds that have reported over \$250,000 of asbestos claims to Folksamerica and a significant sample of all other insureds with reported asbestos claims of less than \$250,000. Comparing estimates generated by the study to Folksamerica exposed limits by underwriting year led to an increase of approximately \$50 million in IBNR during the third quarter of 2005. This unfavorable development was partially offset by favorable development in the Sirius International reserve portfolio of approximately \$12 million, mainly from the three most recent underwriting years. Included in the net unfavorable loss development in 2005 was \$23 million from workers compensation reserves acquired in 2004 as part of the Sierra acquisition. However, this amount was offset dollar-for-dollar by a decrease in the balance due under the adjustable note issued in conjunction with this acquisition.

White Mountains Re receives fee income on reinsurance placements referred to Olympus and is entitled to a profit commission based on net underwriting profits on referred business. During 2005 and 2004, White Mountains Re earned \$61 million and \$69 million, respectively, of fee income from Olympus. The decrease in fee income from the prior period is primarily due to the significant loss events in 2005, including the Gulf Coast hurricanes, which resulted in White Mountains Re not earning any profit commission in 2005 compared to earning \$12 million of profit commission in 2004. The profit commission arrangement with Olympus is subject to a deficit carryforward whereby net underwriting losses from one underwriting year carryover to future underwriting years. As a result of the significant loss events in 2005, Olympus recorded a substantial net underwriting loss for the year. Accordingly, White Mountains Re does not expect to record profit commissions from Olympus for the foreseeable future.

Effective January 1, 2006, Folksamerica renewed its quota-share reinsurance arrangements with Olympus on modified terms and Sirius terminated its agreement with Olympus. The 2005 and prior underwriting year business will continue to run-off with Olympus. For a further discussion, see "**Reinsurance Protection**", under "**WHITE MOUNTAINS RE**" in Item 1.



*White Mountains Re Results - Year Ended December 31, 2004 versus Year Ended December 31, 2003*

White Mountains Re's pre-tax income for 2004 was \$87 million, compared to \$144 million for 2003, and its combined ratio was 104% for 2004, compared to 96% for 2003. The decrease in pre-tax income was due primarily to \$135 million of claims incurred related to significant property catastrophe events in the second half of 2004. These catastrophes, which are discussed further below, increased the combined ratio in 2004 by 11 points. In general, White Mountains Re has experienced favorable underwriting conditions for the past three underwriting years. Earnings from business segments not impacted by the property catastrophe events, and earnings from the recently completed Sirius Acquisition, have partially offset the impact of these natural disasters. Net written premiums, total revenues, and total expenses were all up substantially in 2004 due to the Sirius Acquisition.

Gross written premiums increased \$518 million, or 37% from 2003 to 2004, and net written premiums increased \$361 million, or 41% for the same period. This increase is due primarily to the Sirius Acquisition, which contributed \$612 million of gross written premiums and \$418 million of net written premiums during 2004. Included in these amounts is the U.S. program business written by Sirius America totaling \$216 million of gross written premiums and \$85 million of net written premiums. Additionally, in late 2003, White Mountains Re, through Folksamerica, entered into the CNA Re agreement and established a Chicago underwriting office. Annual gross written premiums for the 2004 underwriting year resulting from this transaction and the related opening of the Chicago underwriting office were approximately \$177 million, of which \$129 million was recorded as gross written premium and \$91 million as net written premium for the year ended December 31, 2004. Partially offsetting the increases resulting from these transactions was the cancellation of several large casualty treaties at Folksamerica whose pricing or terms did not meet White Mountains Re's underwriting guidelines.

There were significant levels of property catastrophe activity during the last half of 2004, including the four hurricanes which affected the Southeast United States and the Caribbean, where White Mountains Re has historically been a significant participant in the property reinsurance market. Additionally, Sirius International was exposed to losses from the tsunami that impacted South Asia in December 2004. White Mountains Re believes its underwriting discipline and risk management approach helped to contain these losses to manageable levels. This significant property catastrophe activity during the last half of 2004 resulted in \$135 million of pre-tax losses, including \$16 million related to the tsunami. There was no significant property catastrophe activity in 2003.

During 2004, White Mountains Re recorded \$11 million of net unfavorable loss reserve development, which contributed 1 point to the loss ratio in 2004, as compared to \$46 million, or 5 points in 2003. The majority of the unfavorable development recorded in 2004 resulted from certain discontinued lines at Folksamerica as well as run-off operations acquired as part of the Sirius Acquisition. This unfavorable development was partially offset by favorable development in the Sirius International reserve portfolio, stemming mainly from the three most recent underwriting years, and is indicative of the favorable terms and conditions that have existed in the global reinsurance marketplace during that time. Additionally, White Mountains Re recorded \$10 million of unfavorable loss development on its workers compensation reserves acquired as part of the Sierra acquisition in 2004. This adverse development was offset dollar-for-dollar by the adjustable note discussed above.

White Mountains Re recognized net fee income of \$69 million from Olympus in 2004 as compared to \$98 in 2003. The decline in the fee income earned is due primarily to the negative impact of the four hurricanes on the profit commission arrangement between White Mountains Re and Olympus.

**Esurance**

Esurance's financial results and GAAP combined ratios for the years ended December 31, 2005, 2004 and 2003 follows:

Millions	Year Ended December 31,		
	2005	2004	2003
Gross written premiums	\$ 351.9	\$ 201.3	\$ 116.4
Net written premiums	\$ 349.1	\$ 199.4	\$ 116.4
Earned insurance and reinsurance premiums	\$ 306.8	\$ 176.5	\$ 99.9
Net investment income	9.8	3.5	1.3
Net realized investment gains	2.1	1.1	.2
Other revenue	3.0	2.2	.3
Total revenues	321.7	183.3	101.7
Losses and LAE	206.2	122.4	81.0
Insurance and reinsurance acquisition expenses	90.8	30.3	18.8
Other underwriting expenses	37.2	26.8	20.4
Total expenses	334.2	179.5	120.2
Pre-tax earnings (loss)	\$ (12.5)	\$ 3.8	\$ (18.5)
	Years Ended December 31,		
	2005	2004	2003
GAAP ratios:			
Loss and LAE	67%	69%	81%
Expense	42%	33%	39%
Total Combined	109%	102%	120%

**Esurance Results - Year Ended December 31, 2005 versus Year Ended December 31, 2004**

Esurance reported a pre-tax loss of \$13 million for the year ended December 31, 2005, compared with pretax income of \$4 million for the prior year. Esurance's GAAP combined ratio was 109% for 2005 compared to 102% in 2004. Esurance's loss ratio decreased to 67% in 2005, from 69% in the prior year, despite \$2 million in losses sustained from hurricane Wilma during 2005. The decrease in the loss ratio resulted primarily from improved claims performance and increased pricing sophistication. The expense ratio increased to 42% in 2005, from 33% in the prior year, mainly due to higher acquisition expenses from Esurance's marketing programs, driven by increased competition for new customers. The combined ratio was also adversely impacted by approximately 3 points from the adoption of a new long-term incentive compensation plan in 2005.

Direct written premium increased to \$352 million in 2005, a 75% increase from the prior year. As of December 31, 2005, Esurance's in-force policy count totaled 211,851, a 79% increase over the prior year, and it wrote business in twenty-two states. For the year ended December 31, 2005, Esurance's largest states were Florida (with 20% of direct premium written), California (20%), Texas (9%), New York (8%) and Michigan (7%).

**Esurance Results - Year Ended December 31, 2004 versus Year Ended December 31, 2003**

Esurance's pre-tax income of \$4 million for 2004 represented an improvement over the pre-tax loss of \$19 million in 2003. Esurance's 2004 combined ratio improved to 102% from 120% in 2003 due to improvements in both loss and expense ratios. Esurance's loss ratio improvement resulted from the continued rollout and refinement of Esurance's proprietary auto insurance program. Loss ratio improvement also resulted from better claims performance, driven by the transition from a third party administrator to an in-house claims operation in 2003, as well as 3 points of favorable development on loss reserves.

The auto program, combined with Esurance's self-service, web-enabled operating platform, allowed Esurance to increase premium volume and in-force policy count while reducing the expense ratio from 39% to 33%. As of December 31, 2004, Esurance's in-force count was 118,513 policies, a 60% increase over December 31, 2003. Increased advertising, particularly in radio and TV, drove policy count growth.

**Other Operations**

Other Operations consists of the operations of the Company and the Company's intermediate subsidiary holding companies, WM Advisors and the International American Group, as well as White Mountains' investments in Montpelier and Symetra warrants. A summary of White Mountains' financial results from its Other Operations segment for the years ended December 31, 2005, 2004 and 2003 follows:

Millions	Year Ended December 31,		
	2005	2004	2003
Gross written premiums	\$ 1.9	\$	\$ 41.2
Net written premiums	\$ 1.8	\$	\$ 33.1
Earned insurance and reinsurance premiums	\$ 1.8	\$	\$ 31.7
Net investment income	94.7	37.5	15.5
Net realized investment gains (loss)	(90.1)	20.8	27.7
Other revenue	58.7	10.4	36.3
Total revenues	65.1	68.7	111.2
Losses and LAE	12.6	4.6	23.9
Insurance and reinsurance acquisition expenses	.1		4.0
Other underwriting expenses	1.6	1.5	10.2
General and administrative expenses	56.0	172.0	114.6
Accretion of fair value adjustment to loss and LAE reserves	26.0	33.2	48.6
Interest expense on debt	42.7	44.3	46.3
Interest expense - dividends and accretion on preferred stock	52.4	47.6	22.3
Total expenses	191.4	303.2	269.9
<b>Pre-tax loss</b>	\$ (126.3)	\$ (234.5)	\$ (158.7)

White Mountains' capital raising and capital allocation activities are principally conducted through its holding companies. In this regard, the results of its Other Operations segment primarily relate to financing activities, purchase accounting adjustments relating to the OneBeacon Acquisition, gains and losses recognized from the change in fair value of the Company's investments in Montpelier and Symetra warrants, gains and losses recognized from the purchase and sale of certain of the Company's subsidiaries and other assets and general and administrative expenses incurred at the holding company level.

***Other Operations Results - Year Ended December 31, 2005 versus Year Ended December 31, 2004***

White Mountains' Other Operations segment reported a pre-tax loss of \$126 million for 2005, compared to \$235 million for 2004. The following items contributed to the reduced pre-tax loss in 2005: (1) a \$134 million decrease in incentive compensation expense in 2005; (2) the special dividend from Montpelier in the 2005 first quarter, \$39 million of which was reported in this segment; (3) \$26 million of gains recorded in other revenues in 2005 from the settlement of two lawsuits in which White Mountains was a plaintiff; and (4) a \$16 million increase in other net investment income. Additionally, the 2004 results included a \$20 million realized loss from the impact that currency fluctuations had on hedging the cost of funding for the Sirius Acquisition. These loss-reducing factors were somewhat offset by a \$126 million decrease in net realized investment gains from the valuation of the Montpelier warrants (a \$110 million loss in 2005 versus a \$16 million gain in 2004).



***Other Operations Results - Year Ended December 31, 2004 versus Year Ended December 31, 2003***

White Mountains' Other Operations segment reported a pre-tax loss of \$235 million for 2004, compared to \$159 million for 2003. The increased loss for the year was primarily due to a \$20 million increase in incentive compensation accruals, which were driven by a 41% rise in White Mountains' stock price during 2004, and higher gains from the sale of real estate in 2003 (\$13 million in 2004 and \$43 million in 2003). In addition, interest expense on preferred stock was up \$25 million in 2004 due to the inclusion of a full year of expense in pre-tax income in 2004 as opposed to six months included in 2003 as a result of the Company's adoption of SFAS 150, effective July 1, 2003. Prior to the adoption of SFAS 150, the interest expense on preferred stock was classified below the pre-tax loss line on the income statement as preferred stock dividends.

During 2003, Peninsula was the only operating company in the segment, and therefore it accounts for all of the premiums reported in the table above. During January 2004, White Mountains sold Peninsula for \$23 million. The operations of American Centennial and British Insurance Company are not significant to White Mountains, as those companies have been in run-off since they were acquired in 1999.

**II. Summary of Investment Results**

**Investment Philosophy**

White Mountains manages substantially all of its consolidated investments through its wholly-owned subsidiary, WM Advisors. White Mountains' investment philosophy is to maximize its after-tax total risk-adjusted return over the long term. Under this approach, each dollar of after-tax investment income and realized and unrealized gains and losses is valued equally. White Mountains' overall fixed maturity investment strategy is to purchase securities that are attractively priced in relation to credit risks. White Mountains generally manages the interest rate risk associated with holding fixed maturity investments by actively maintaining the average duration of the portfolio to achieve an adequate after-tax total return without subjecting the portfolio to an unreasonable level of interest rate risk. White Mountains' investment portfolio mix as of December 31, 2005 consisted in large part of high-quality, fixed maturity investments and short-term investments, as well as some equity investments and limited partnerships. White Mountains' management believes that prudent levels of investments in common equity securities and other investments within its investment portfolio are likely to enhance long term after-tax total returns without significantly increasing the risk profile of the portfolio.

***Investment Returns -Year Ended December 31, 2005 versus Year Ended December 31, 2004***

White Mountains' GAAP pre-tax total return on invested assets was 2% for the year ended December 31, 2005 versus 7% for 2004. White Mountains' equity portfolio returned 8% in 2005, which was 3 percentage points better than the S&P 500, despite its largest equity position, Montpelier, having a significant decline (as noted below). On the fixed income side, White Mountains maintained a relatively short duration (about 2 years, including short-term investments), high-quality portfolio, which performed consistent with its characteristics, while its exposure to the Swedish krona through Sirius detracted from its fixed income returns due to the strengthening of the U.S. dollar.

Net investment income for 2005 of \$492 million was up 36% from \$361 million for 2004, due mainly to the Montpelier special dividend, higher short-term interest rates and the inclusion of a full year of Sirius' results.

*Investment Returns -Year Ended December 31, 2004 versus Year Ended December 31, 2003*

White Mountains' GAAP total return on invested assets was 7% for both 2004 and 2003. White Mountains' equity portfolio returned 20% in 2004, which was 9 percentage points better than the S&P 500, while the bond portfolio performed in line with its duration and credit characteristics. Net investment income in 2004 was up 24% from 2003, mainly due to the Sirius Acquisition.

**Montpelier investment**

Millions	Year Ended December 31,		
	2005	2004	2003
Net investment income, pre-tax	\$ 89.7	\$ 18.3	\$
Net realized investment gains (losses), pre-tax	(165.1)	51.5	32.5
Total revenues (losses), pre-tax	(75.4)	69.8	32.5
Tax benefit (expense) on total revenues	13.5	(17.9)	
Total revenues (losses), after-tax	(61.9)	51.9	32.5
Change in net unrealized investment gains (losses), after-tax	(42.3)	36.0	2.0
Equity in earnings of Montpelier, after-tax		11.0	45.2
Net after-tax change in White Mountains' book value from Montpelier investment	\$ (104.2)	\$ 98.9	\$ 79.7

During 2005, White Mountains recognized \$104 million of after-tax losses, net of dividends received, on its investment in Montpelier. Montpelier's common share price decreased from \$38.45 at December 31, 2004 to \$18.90 at December 31, 2005, resulting in a \$110 million pre-tax realized investment loss on White Mountains' Montpelier warrant investment. In addition, White Mountains recorded a \$55 million pre-tax other-than-temporary impairment charge (reported as a realized investment loss) and a \$42 million after-tax unrealized investment loss on its Montpelier common share investment during 2005. White Mountains' original cost of its Montpelier common share investment was \$106 million, which was subsequently increased by \$65 million in equity in earnings recorded by White Mountains from 2001 to 2004, the period in which it accounted for the investment under the equity method of accounting. The impairment charge represented the difference between White Mountains' GAAP cost of \$171 million and the investment's fair value of \$116 million at December 31, 2005.

During 2005, White Mountains recorded \$90 million in pre-tax dividends from Montpelier in net investment income. During the first quarter of 2005, Montpelier declared a special dividend of \$5.50 per share, payable to holders of both its common shares and warrants to acquire its common shares. White Mountains recorded pre-tax dividend income of \$74 million in 2005 for this special dividend, in addition to \$16 million in dividend income from Montpelier's normal quarterly dividends.

White Mountains sold a portion of its investment in Montpelier common shares during the first quarter of 2004 resulting in a \$35 million pre-tax realized gain and, as a result, changed the method of accounting for its remaining Montpelier common shares to the fair value method, resulting in a \$33 million increase in after-tax unrealized gains in the first quarter of 2004.

**Impairment**

See **Note 5 - "Investments"** of the accompanying consolidated financial statements for White Mountains' analysis of impairment losses on investment securities.



## **NON-GAAP FINANCIAL MEASURES**

This report includes three non-GAAP financial measures that have been reconciled to their most comparable GAAP financial measures. White Mountains believes these measures to be more relevant than comparable GAAP measures in evaluating White Mountains' financial performance and capital position.

Adjusted comprehensive net income is a non-GAAP measure that excludes the change in net unrealized gains from Symetra's fixed maturity portfolio from comprehensive net income. GAAP requires these assets to be marked-to-market, which results in gains during periods when interest rates fall and losses in periods when interest rates rise. Because the liabilities related to the life insurance and structured settlement products that these assets support are not marked-to-market, it is likely that the economic impact on Symetra would be the opposite of that shown under GAAP (i.e., in general, Symetra's intrinsic value increases when interest rates rise and decreases when interest rates fall). The reconciliation of adjusted comprehensive net income to comprehensive net income is included on page 44.

Book value per share is derived by dividing the Company's total GAAP shareholders' equity as of a given date by the number of common shares outstanding as of that date, including the dilutive effects of outstanding Options and warrants to acquire common shares, as well as the unamortized accretion of preferred stock. Fully converted tangible book value per common and equivalent share is a non-GAAP measure which is derived by expanding the GAAP book value per share calculation to include the effects of assumed conversion of all convertible securities and to exclude any unamortized goodwill and net unrealized gains from Symetra's fixed maturity portfolio. The reconciliation of fully converted tangible book value per common and equivalent share to book value per share is included on page 43.

Total capital at White Mountains is comprised of common shareholders' equity, debt and preferred stock subject to mandatory redemption. Tangible capital excludes from total capital the unamortized goodwill and the equity in net unrealized gains from Symetra's fixed maturity portfolio. The reconciliation of total capital to total tangible capital is included on page 60.

## **LIQUIDITY AND CAPITAL RESOURCES**

### **Operating cash and short-term investments**

*Holding company level.* The primary sources of cash for the Company and certain of its intermediate holding companies are dividends and tax sharing payments received from its insurance and reinsurance operating subsidiaries, financing activities and net investment income and proceeds from sales and maturities of holding company investments. The primary uses of cash are interest payments on its debt obligations, dividend payments on the Company's common shares and the Berkshire Preferred Stock and Zenith Preferred Stock, purchases of investments and holding company operating expenses.

*Operating subsidiary level.* The primary sources of cash for White Mountains' insurance and reinsurance operating subsidiaries are premium collections, net investment income and proceeds from sales and maturities of investments.

The primary uses of cash are claim payments, policy acquisition costs, operating expenses, the purchase of investments and dividend and tax sharing payments made to parent holding companies.

Both internal and external forces influence White Mountains' financial condition, results of operations and cash flows. Claim settlements, premium levels and investment returns may be impacted by changing rates of inflation and other economic conditions. In many cases, significant periods of time, ranging up to several years or more, may lapse between the occurrence of an insured loss, the reporting of the loss to White Mountains and the settlement of the liability for that loss. The exact timing of the payment of claims and benefits cannot be predicted with certainty. White Mountains' insurance and reinsurance operating subsidiaries maintain portfolios of invested assets with varying maturities and a substantial amount of short-term investments to provide adequate liquidity for the payment of claims.

Management believes that White Mountains' cash balances, cash flows from operations, routine sales of investments and the liquidity provided by its undrawn Bank Facility are adequate to meet expected cash requirements for the foreseeable future on both a holding company and insurance and reinsurance operating subsidiary level.

## Dividend Capacity

Under the insurance laws of the states and jurisdictions under which White Mountains' insurance and reinsurance operating subsidiaries are domiciled, an insurer is restricted with respect to the timing or the amount of dividends it may pay without prior approval by regulatory authorities. Accordingly, there can be no assurance regarding the amount of such dividends that may be paid by such subsidiaries in the future. Following is a description of the ability of White Mountains' insurance and reinsurance operating subsidiaries to pay dividends to the Company and certain of its intermediate holding companies:

### *OneBeacon:*

Generally, OneBeacon's regulated insurance operating subsidiaries have the ability to pay dividends during any 12-month period without the prior approval of regulatory authorities in an amount equal to the greater of prior year statutory net income or 10% of prior year end statutory surplus, subject to the availability of unassigned funds. As a result, based on 2005 statutory net income, OneBeacon's top tier regulated insurance operating subsidiaries have the ability to pay approximately \$197 million of dividends during 2006 without prior approval of regulatory authorities, subject to the availability of unassigned funds. As of December 31, 2005, OneBeacon's top tier regulated insurance operating subsidiaries had \$1.3 billion of unassigned funds available for dividend distribution.

In addition, as of December 31, 2005, OneBeacon had approximately \$20 million of cash and investments outside of its regulated insurance operating subsidiaries available for distribution during 2006. During 2005, OneBeacon paid \$340 million of dividends to Fund American.

### *White Mountains Re:*

Folksamerica Re has the ability to pay dividends during any 12-month period without the prior approval of regulatory authorities in an amount equal to the lesser of net investment income, as defined by statute, or 10% of statutory surplus, in both cases as most recently reported to regulatory authorities, subject to the availability of earned surplus. Based upon December 31, 2005 statutory surplus of \$1.1 billion, Folksamerica Re would have the ability to pay approximately \$107 million of dividends during 2006 without prior approval of regulatory authorities, subject to the availability of earned surplus. However, as a result of the hurricane-related losses it sustained during 2005, Folksamerica Re had \$59 million of negative earned surplus as of December 31, 2005. Consequently, Folksamerica Re cannot pay any dividends without regulatory approval until it has earned surplus and, therefore, does not expect to pay any dividends without regulatory approval until late 2006 or early 2007. During 2005, Folksamerica Re paid \$15 million of dividends to its immediate parent.

Sirius International has the ability to pay dividends subject to the availability of unrestricted statutory surplus. Historically, Sirius International had allocated the majority of its earnings to the Safety Reserve (see **Safety Reserve** below). As a result, Sirius International currently has no unrestricted statutory surplus.

In accordance with the provisions of Swedish law, Sirius International can voluntarily transfer its pre-tax income, or a portion thereof, subject to certain limitations, to its parent company to minimize taxes. In early 2006, Sirius International contributed approximately \$49 million of its 2005 pre-tax income to its parent company.

As of December 31, 2005, WMU had \$6 million of cash and investments available for distribution during 2006. In addition, WMU has the ability to distribute its 2006 earnings without restriction. During 2005, WMU paid \$33 million of dividends to its immediate parent.

In addition, as of December 31, 2005, White Mountains Re had approximately \$39 million of cash and investments outside of its regulated insurance and reinsurance operating subsidiaries available for distribution during 2006. During 2005, White Mountains Re distributed \$98 million of cash and investments from various holding companies to its immediate parent.

*Esurance:*

Generally, Esurance's regulated insurance operating subsidiaries have the ability to pay dividends during any 12-month period without the prior approval of regulatory authorities in an amount equal to the greater of prior year statutory net income or 10% of prior year end statutory surplus, subject to the availability of unassigned funds. As a result, based on 2005 year-end statutory surplus, Esurance's top tier regulated insurance operating subsidiary has the ability to pay \$5 million of dividends during 2006 without prior approval of regulatory authorities, subject to the

availability of unassigned funds. As of December 31, 2005, Esurance's top tier regulated insurance operating subsidiary had \$15 million of unassigned funds available for dividend distribution.

In addition, as of December 31, 2005, Esurance had \$9 million of cash and short term investments outside of its regulated insurance operating subsidiaries available for distribution during 2006. During 2005, Esurance did not pay any cash dividends.

### **Safety Reserve**

In accordance with provisions of Swedish law, Sirius International is permitted to transfer up to the full amount of its pre-tax income, subject to certain limitations, into an untaxed reserve referred to as a safety reserve. Under GAAP, an amount equal to the safety reserve, net of the related deferred tax liability established at the Swedish tax rate of 28%, is classified as shareholders' equity. Generally, this deferred tax liability is only required to be paid by Sirius International if it fails to maintain predetermined levels of premium writings in future years. As a result of the indefinite deferral of these taxes, Swedish regulatory authorities do not apply any taxes to the safety reserve when calculating solvency capital under Swedish insurance regulations. Accordingly, under local statutory requirements, an amount equal to Sirius International's safety reserve of \$920 million at December 31, 2005 is classified as surplus.

### **Keep-Well**

On November 30, 2004, White Mountains completed a significant corporate reorganization, through which ownership of Folksamerica was transferred to White Mountains Re from Fund American. In order to effect the reorganization, White Mountains and Fund American entered into or amended certain agreements with respect to the Berkshire Preferred Stock. Under the terms of a Keep-Well Agreement dated November 30, 2004 between White Mountains and Fund American (the "Keep-Well"), White Mountains has agreed to return to Fund American up to approximately \$1.1 billion, which equals the amount of net assets transferred out of Fund American as a result of the reorganization, if some or all of that amount is required by Fund American to meet its obligations to Berkshire under the Berkshire Preferred Stock. Additionally, the Keep-Well limits the aggregate amount of distributions that White Mountains may make to its shareholders to approximately \$1.3 billion plus White Mountains' aggregate consolidated net income after September 30, 2004 (\$435 million at December 31, 2005). Since the inception of the Keep-Well agreement, White Mountains has distributed \$86 million in cash dividends to its shareholders. The Keep-Well will expire when all obligations of the Berkshire Preferred Stock, which is redeemable in May 2008, have been satisfied, or when approximately \$1.1 billion has been returned to Fund American.

### **Insurance Float**

Insurance float is an important dynamic of White Mountains' operations that must be managed effectively. Float is money that an insurance company holds for a limited time. In an insurance operation, float arises because premiums are collected before losses are paid. This interval can extend over many years. During that time, the insurer invests the money. When the premiums that an insurer collects do not cover the losses and expenses it eventually must pay, the result is an underwriting loss, which is considered to be the cost of float. The amount and cost of float for White Mountains is affected by underlying market conditions, as well as acquisitions or dispositions of insurance and reinsurance businesses. Although insurance float can be calculated using numbers determined under GAAP, insurance float is not a GAAP concept and, therefore, there is no comparable GAAP measure.



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One of the means by which White Mountains calculates its insurance float is by taking its net investment assets and subtracting its total tangible capital. The following table illustrates White Mountains' consolidated insurance float position as of the past five year-ends:

(\$ in millions)	December 31,				
	2005	2004	2003	2002	2001
Total investments	\$ 9,866.4	\$ 10,529.5	\$ 8,547.5	\$ 8,899.4	\$ 9,005.7
Cash	187.7	243.1	89.9	121.5	67.4
Investment in unconsolidated insurance affiliate(s)	479.7	466.6	515.9	399.9	311.1
Equity in net unrealized gains from Symetra's fixed maturity portfolio	(24.2)	(56.6)			
Accounts receivable on unsettled investment sales	21.7	19.9	9.1	160.8	75.2
Accounts payable on unsettled investment purchases	(43.4)	(30.9)	(371.6)	(495.2)	(311.2)
Interest-bearing funds held by ceding companies (1)	293.9	516.9	70.4	50.1	42.9
Interest-bearing funds held under reinsurance treaties (2)	(100.6)	(105.1)	(152.5)	(236.2)	(311.0)
Net investment assets	\$ 10,681.2	\$ 11,583.4	\$ 8,708.7	\$ 8,900.3	\$ 8,880.1
Total common shareholders' equity	\$ 3,833.2	\$ 3,883.9	\$ 2,979.2	\$ 2,407.9	\$ 1,444.6
Debt	779.1	783.3	743.0	793.2	1,125.4
Preferred stock subject to mandatory redemption	234.0	211.9	194.5	180.9	170.3
Convertible preference shares				219.0	
Total capital	\$ 4,846.3	\$ 4,879.1	\$ 3,916.7	\$ 3,601.0	\$ 2,740.3
Unamortized deferred credits and goodwill	(24.4)	(20.0)	(20.3)		660.2
Equity in net unrealized gains from Symetra's fixed maturity portfolio	(24.2)	(56.6)			
Total tangible capital	\$ 4,797.7	\$ 4,802.5	\$ 3,896.4	\$ 3,601.0	\$ 3,400.5
Insurance float	\$ 5,883.5	\$ 6,780.9	\$ 4,812.3	\$ 5,299.3	\$ 5,479.6
Insurance float as a multiple of total tangible capital	1.2x	1.4x	1.2x	1.5x	1.6x
Net investment assets as a multiple of total tangible capital	2.2x	2.4x	2.2x	2.5x	2.6x
Insurance float as a multiple of common shareholders' equity	1.5x	1.7x	1.6x	2.2x	3.8x
Net investment assets as a multiple of common shareholders' equity	2.8x	3.0x	2.9x	3.7x	6.1x

(1) Excludes funds held by ceding companies from which White Mountains does not receive interest credits.

(2) Excludes funds held by White Mountains under reinsurance treaties for which White Mountains does not provide interest credits.

White Mountains has historically obtained its float primarily through acquisitions, as opposed to organic growth. In recent years, White Mountains has had negative cash flows from operations but has grown float from its insurance and reinsurance operations. This is due to the fact

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that White Mountains' cash flow from operations does not reflect cash and investments generated by the acquisition of insurance and reinsurance businesses in recent years. Post-acquisition, such companies are often placed into partial or complete run-off, thereby resulting in negative cash flows from operations as the investments acquired are liquidated over time to pay claims.

It is White Mountains' intention to generate low-cost float over time through a combination of acquisitions and/or by organic growth in its existing insurance and reinsurance operations. However, White Mountains will seek to increase its float organically only when market conditions allow for an expectation of generating underwriting profits.



**Financing**

The following table summarizes White Mountains' capital structure as of December 31, 2005 and 2004:

\$ in millions	December 31,	
	2005	2004
Senior Notes, carrying value	\$ 698.5	\$ 698.3
Bank Facility		
Other debt of operating subsidiaries (1)	80.6	85.0
Total debt	779.1	783.3
Preferred stock subject to mandatory redemption	234.0	211.9
Total common shareholders' equity	3,833.2	3,883.9
Total capital	\$ 4,846.3	\$ 4,879.1
Unamortized goodwill	(24.4)	(20.0)
Equity in net unrealized gains from Symetra's fixed maturity portfolio	(24.2)	(56.6)
Total tangible capital	\$ 4,797.7	\$ 4,802.5
Senior Notes to total tangible capital	15%	15%
Total debt to total tangible capital	16%	16%
Total debt and preferred stock to total tangible capital	21%	21%

(1) See **Note 6 - "Debt"** of the accompanying Consolidated Financial Statements for a discussion of operating subsidiary debt.

Management believes that White Mountains' strong financial position provides it with the flexibility and capacity to obtain funds externally as needed through debt or equity financing on both a short-term and long-term basis.

Fund American and the Company are both permitted borrowers under the Bank Facility, which matures in August 2009. Under the Bank Facility, the Company guarantees all obligations of Fund American, and Fund American guarantees all borrowings of the Company, subject to certain limitations imposed by the terms of the Berkshire Preferred Stock. As of December 31, 2005, the \$400 million available under the Bank Facility was undrawn.

In connection with its acquisition of the Sierra Group on March 31, 2004, Folksamerica entered into a \$62 million purchase note (the Sierra Note), \$58 million of which will be adjusted over its approximate six-year term to reflect favorable or adverse loss reserve development on the acquired reserve portfolio and run-off of remaining policies in force (mainly workers compensation business) as well as certain other balance sheet protections. Since inception, the principal of the Sierra Note has been reduced by \$35 million, to an outstanding balance of \$27 million as of December 31, 2005, as a result of adverse development on the acquired reserves and run-off of unearned premiums.

In connection with its purchase of an office building in Canton, Massachusetts, OneBeacon entered into a \$40 million construction facility to fund renovations to the new space that will ultimately house its corporate offices. As of December 31, 2005, OneBeacon had drawn \$18 million under the facility.

Fund American's Senior Notes are currently rated Baa2 (Moderate Risk, the ninth highest of twenty-one ratings) with a stable outlook by Moody's, BBB (Adequate, the ninth highest of twenty-two ratings) with a stable outlook by Standard & Poor's, bbb (Adequate, the ninth highest of twenty-two ratings) with a stable outlook by A.M. Best and BBB (Good, the ninth highest of twenty-three ratings) with a stable outlook by Fitch Ratings. It is possible that, in the future, one or more of the rating agencies may lower White Mountains' existing ratings. If one or more of its ratings were downgraded, White Mountains could incur higher borrowing costs and its ability to access the capital markets could be impacted. In addition, White Mountains' insurance and reinsurance operating subsidiaries could be adversely impacted by a downgrade in their financial strength ratings, including a possible reduction in demand for their products in certain markets.

The Senior Notes were issued under an indenture which contains restrictive covenants that, among other things, limit the ability of the Company, Fund American and their respective subsidiaries to create liens and enter into sale and leaseback transactions and substantially limits the ability of Fund American and its respective subsidiaries to consolidate, merge or transfer their properties and assets. The indenture does not contain any financial ratios or specified levels of net worth or liquidity to which the Company or Fund American must adhere. At

December 31, 2005, White Mountains was in compliance with all of the covenants under the Senior Notes, and anticipates it will continue to remain in compliance with these covenants for the foreseeable future.

The Bank Facility contains various affirmative, negative and financial covenants which White Mountains considers to be customary for such borrowings and include maintaining certain minimum net worth and maximum debt to capitalization standards for White Mountains. Failure to meet one or more of these covenants could result in an event of default, which ultimately could eliminate availability under the facility and result in acceleration of principal repayment on any amounts outstanding. At December 31, 2005, White Mountains was in compliance with all of the covenants under the Bank Facility, and anticipates it will continue to remain in compliance with these covenants for the foreseeable future.

### Contractual Obligations and Commitments

Below is a schedule of White Mountains' material contractual obligations and commitments as of December 31, 2005:

Millions	Due in One Year or Less	Due in Two to Three Years	Due in Four to Five Years	Due After Five Years	Total
Debt	\$	\$ 19.0	\$ 31.2	\$ 730.4	\$ 780.6
Mandatorily redeemable preferred stock		300.0		20.0	320.0
Loss and LAE reserves (1)	3,575.8	2,672.3	1,438.0	3,116.4	10,802.5
Reserves for structured contracts	71.5	71.0	71.0	11.1	224.6
Interest on debt and dividends on preferred stock subject to mandatory redemption	73.0	124.8	94.3	105.2	397.3
Long-term incentive compensation	170.5	212.6	26.6	26.5	436.2
Operating leases	41.9	74.2	31.2	22.1	169.4
Total contractual obligations	\$ 3,932.7	\$ 3,473.9	\$ 1,692.3	\$ 4,031.7	\$ 13,130.6

(1) Represents expected future cash outflows resulting from loss and LAE payments. Accordingly, these balances add back the discount on OneBeacon's workers compensation loss and LAE reserves of \$214 million and the remaining purchase accounting fair value adjustment of \$357 million related to the OneBeacon and Sirius acquisitions as they are non-cash items. Further, the amounts presented are gross of reinsurance recoverables on unpaid losses of \$5,026 million as of December 31, 2005.

White Mountains' loss reserves do not have contractual maturity dates. However, based on historical payment patterns, the preceding table includes an estimate of when management expects White Mountains' loss reserves to be paid. The timing of claim payments is subject to significant uncertainty. White Mountains maintains a portfolio of marketable investments with varying maturities and a substantial amount of short-term investments to provide adequate cash flows for the payment of claims.

The balances included in the table above regarding White Mountains' long-term incentive compensation plans include amounts payable for performance shares and units, as well as deferred compensation balances. Exact amounts to be paid cannot be predicted, for performance shares, with certainty, as the ultimate amounts of these liabilities are based on future performance of the Company and the market price of the Company's common shares at the time the payments are made. The estimated payments reflected in the table are based on current accrual factors

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(common share price and pay-out percentage) and assume that all outstanding balances were 100% vested as of December 31, 2005.

There are no provisions within White Mountains leasing agreements that would trigger acceleration of future lease payments. White Mountains does not finance its operations through the securitization of its trade receivables, through special purpose entities or through synthetic leases. Further, except as noted in the following paragraph, White Mountains has not entered into any material arrangement requiring it to guarantee payment of third party debt, lease payments or to fund losses of an unconsolidated special purpose entity.

Through Sirius International, White Mountains has a long-term investment as a stockholder in LUC Holdings, an entity that has entered into a head lease to rent the London Underwriting Center ( LUC ) through 2016. LUC Holdings in turn subleases space in the LUC. In the LUC Holdings stockholders agreement, the stockholders have guaranteed any shortfall between the head lease and the sub-leases on a joint and several basis. As a consequence, in recent years the stockholders have funded an operating shortfall of LUC. At December 31, 2005,

White Mountains has recorded a liability of \$8 million for its share of the expected future shortfall between LUC Holdings' head lease payments and sub-lease receipts. White Mountains does not believe that future shortfalls, if any, will have a material impact on its results of operations.

White Mountains also has future binding commitments to fund certain limited partnership investments. These commitments, which total approximately \$35 million, do not have fixed funding dates and are therefore excluded from the table above.

Detailed information concerning White Mountains' liquidity and capital resource activities during 2005, 2004 and 2003 follows:

***For the year ended December 31, 2005***

*Financing and Other Capital Activities*

During 2005, White Mountains declared and paid cash dividends of \$86 million, \$28 million and \$2 million to holders of White Mountains common shares, the Berkshire Preferred Stock and the Zenith Preferred Stock, respectively.

During 2005, OneBeacon declared and paid dividends of \$340 million to Fund American and White Mountains Re declared and paid \$98 million of dividends to its immediate parent.

During 2005, White Mountains contributed \$250 million to White Mountains Re (which, in turn, contributed \$250 million to Folksamerica) and \$10 million to Esurance.

During 2005, White Mountains paid a total of \$41 million in interest under the Senior Notes.

During 2005, OneBeacon drew down \$18 million on an 18-year mortgage note that it entered into in connection with its purchase of land and a future home office building. As OneBeacon incurs construction costs associated with the renovation of the building, it will draw down additional principal up to the \$41 million limit on the mortgage note.

*Acquisitions and Dispositions*

During 2005, OneBeacon sold two of its insurance subsidiaries, NFU and Traders and Pacific Insurance Company, to third parties for a total of \$162 million in cash.

During 2005, White Mountains Re sold one of its subsidiaries, California Indemnity Insurance Company, to a third party for a total of \$20 million, \$19 million of which was paid in cash.

On April 29, 2005, OneBeacon purchased a 284,000 square foot office facility located in Canton, MA for \$23 million.

*Other Liquidity and Capital Resource Activities*

During 2005, White Mountains received a total of \$60 million in tax refunds and interest from the Internal Revenue Service related to the completion of an audit of White Mountains' 1997-2000 tax years, the period during which the Company redomesticated to Bermuda.

During 2005, the Company issued a total of 7,750 common shares to its employees through the exercise of Options during the period and received cash proceeds of \$1 million in connection with these Option exercises.

During the first quarter of 2005, White Mountains made payments totaling \$235 million, in cash or by deferral into certain non-qualified compensation plans of the Company or its subsidiaries, to participants in its long-term incentive compensation plans. These payments were made with respect to 212,611 performance shares at payout levels ranging from 113% to 200% of target.

During the first quarter of 2005, White Mountains received a \$74 million special dividend related to its common stock and warrant investment in Montpelier. This dividend represented \$5.50 per share and was in addition to Montpelier's normal quarterly dividend of \$.36 per share.

*For the year ended December 31, 2004*

*Financing and Other Capital Activities*

On June 29, 2004, Berkshire exercised all of its warrants to purchase 1,724,200 common shares of White Mountains for \$294 million. Berkshire acquired the warrants in connection with the financing of White Mountains' acquisition of OneBeacon in 2001. The warrants were exercisable at any time until May 2008 and callable by the Company on or after May 31, 2005. In consideration for the early exercise of the warrants, Berkshire and the Company agreed to reduce the exercise price by approximately 2%.

During 2004, White Mountains declared and paid dividends of \$9 million, \$28 million and \$2 million to holders of White Mountains' common shares, the Berkshire Preferred Stock and the Zenith Preferred Stock, respectively.

During 2004, White Mountains restructured and re-syndicated the Bank Facility to extend its maturity and to increase the availability of the revolving credit facility to \$400 million.

During 2004, White Mountains paid a total of \$41 million in interest under the Senior Notes.

During 2004, OneBeacon declared and paid a total of \$305 million in dividends to Fund American. Also during 2004, WMU paid a total of \$60 million of dividends to its immediate parent. On March 31, 2004, OneBeacon distributed Folksamerica to Fund American.

During 2004, the Company issued a net total of 3,938 common shares to its employees through the exercise of Options during the year and the Company received cash proceeds of \$.5 million in connection with these Option exercises. In addition, during the first quarter of 2004, White Mountains issued 27,772 common shares to employees of OneBeacon in connection with OneBeacon's employee stock ownership plan. OneBeacon paid \$13 million to the Company in consideration for these common shares.

On August 27, 2004, White Mountains repaid the \$25 million note that was issued as part of the financing of its 2001 acquisition of C-F Insurance Company.

*Acquisitions and Dispositions*

During 2004, White Mountains acquired Sirius for \$428 million, 19% of Symetra for \$195 million, Tryg-Baltica for \$58 million, the Sierra Group for \$14 million in cash and a \$62 million note and Atlantic Specialty for \$30 million in cash and a \$20 million note.

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During 2004, White Mountains sold Potomac for \$22 million, Western States, as well as its boiler inspection service business, for \$15 million (both subsidiaries of OneBeacon) and Peninsula for \$23 million.

See **Note 2 - "Significant Transactions"** of the accompanying Consolidated Financial Statements for further discussion of these transactions.

### *Other Liquidity and Capital Resource Activities*

During the first quarter of 2004, White Mountains sold 4.5 million common shares of Montpelier to third parties for net proceeds of \$155.3 million. Also during the first quarter of 2004, White Mountains purchased additional warrants to acquire 2.4 million common shares of Montpelier from an existing warrant holder for \$54.1 million in cash.

During the first quarter of 2004, White Mountains made payments amounting to \$127 million, in cash or by deferral into certain non-qualified compensation plans of the Company or its subsidiaries, to participants in its long-term incentive compensation plans. These payments were made with respect to 167,782 performance shares at payout levels ranging from 93% to 200% of target.



*For the year ended December 31, 2003*

*Financing and Other Capital Activities*

In May 2003, Fund American issued the Senior Notes for net proceeds of \$693 million. Using proceeds from the Senior Notes, Fund American repaid the entire \$615 million of term loans outstanding under its previous bank facility. In addition, on May 27, 2003, using the remaining \$78 million in proceeds from the Senior Notes and cash on hand, Fund American repaid the entire \$125 million of revolving loans outstanding under its previous bank facility. In connection with the repayment of its previous bank facility, Fund American paid an aggregate \$56 million to unwind all of its existing interest rate swap agreements.

In September 2003, White Mountains established its \$300 million revolving Bank Facility. As discussed earlier, this Bank Facility was restructured and re-syndicated in August 2004.

During 2003, White Mountains paid a total of \$20 million in interest under the Senior Notes.

During 2003, White Mountains made scheduled principal amortization payments of \$7 million and paid a total of \$23 million in interest under its previous bank facility, including \$11 million paid under the interest rate swap agreements, prior to its repayment.

During 2003, White Mountains declared and paid dividends of \$8 million, \$28 million and \$2 million to holders of White Mountains common shares, the Berkshire Preferred Stock and the Zenith Preferred Stock, respectively.

During 2003, White Mountains filed a shelf registration statement, which was declared effective by the SEC in July 2003, for offerings of up to \$2.0 billion in debt and/or equity securities.

During 2003, OneBeacon declared and paid a total of \$235 million in dividends to Fund American. Also during 2003, WMU paid a total of \$35 million in dividends to its immediate parent and WM Advisors paid a total of \$10 million in dividends to Fund American.

During 2003, the Company issued a total of 11,116 common shares to its employees through the exercise of Options and, as a result, the Company received cash proceeds of \$1.5 million in connection with these Option exercises.

*Acquisitions and Dispositions*

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During 2003, OneBeacon sold one of its subsidiaries, National Farmers Union Standard Insurance Company, for \$22 million.

### *Other Liquidity and Capital Resource Activities*

During the first quarter of 2003, White Mountains paid a total of 45,000 performance shares (relating to the 2000-2002 performance period) at 200%, amounting to \$29 million, to its participants in cash, common shares or by deferral into certain non-qualified compensation plans of the Company or its subsidiaries. In the second quarter of 2003, White Mountains made performance share payments amounting to \$13 million in cash or by deferral into certain non-qualified compensation plans of the Company. The payments on these additional performance shares in the second quarter represented accelerated payments to certain non-employee directors of the Company for performance periods originally scheduled to end on December 31, 2003, 2004 and 2005.

### **RELATED PARTY TRANSACTIONS**

See **Note 17 - Related Party Transactions** in the accompanying Consolidated Financial Statements.

## CRITICAL ACCOUNTING ESTIMATES

Management's Discussion and Analysis of Financial Condition and Results of Operations discusses the Company's consolidated financial statements, which have been prepared in accordance with GAAP. The financial statements presented herein include all adjustments considered necessary by management to fairly present the financial position, results of operations and cash flows of White Mountains. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

In the current year presentation of financial information, certain amounts in the prior period financial statements have been reclassified to conform with the current presentation. White Mountains has completed numerous significant transactions during the periods presented that have affected the comparability of the financial statement information presented herein.

On an ongoing basis, management evaluates its estimates, including those related to loss and LAE reserves, purchase accounting, reinsurance estimates and its pension benefit obligations. Management bases its estimates on historical experience and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgements about the carrying values of assets and liabilities that are not readily apparent from other sources.

Management believes that its critical accounting policies affect its more significant estimates used in the preparation of its consolidated financial statements. The descriptions below are summarized and have been simplified for clarity.

### 1. Loss and Loss Adjustment Expenses

#### *OneBeacon*

#### **Non-Asbestos and Environmental Reserves**

OneBeacon establishes loss and LAE reserves that are estimates of amounts needed to pay claims and related expenses in the future for insured events that have already occurred. The process of estimating reserves involves a considerable degree of judgment by management and, as of any given date, is inherently uncertain.

Reserves are typically comprised of (1) case reserves for claims reported and (2) reserves for losses that have occurred but for which claims have not yet been reported, referred to as incurred but not reported ( IBNR ) reserves, which include a provision for expected future development on case reserves. Case reserves are estimated based on the experience and knowledge of claims staff regarding the nature and potential cost of each claim and are adjusted as additional information becomes known or payments are made. IBNR reserves are derived by subtracting paid loss and LAE and case reserves from estimates of ultimate loss and LAE. Actuaries estimate ultimate loss and LAE using various generally accepted actuarial methods applied to known losses and other relevant information. Like case reserves, IBNR reserves are adjusted as additional information becomes known or payments are made.

Ultimate loss and LAE are generally determined by extrapolation of claim emergence and settlement patterns observed in the past that can reasonably be expected to persist into the future. In forecasting ultimate loss and LAE with respect to any line of business, past experience with respect to that line of business is the primary resource, but cannot be relied upon in isolation. OneBeacon's own experience, particularly claims development experience, such as trends in case reserves, payments on and closings of claims, as well as changes in business mix and coverage limits, is the most important information for estimating its reserves. External data, available from organizations such as statistical bureaus, consulting firms and reinsurance companies, is sometimes used to supplement or corroborate OneBeacon's own experience, and can be especially useful for estimating costs of new business. For some lines of business, such as "long-tail" coverages discussed below, claims data reported in the most recent accident year is often too limited to provide a meaningful basis for analysis due to the typical delay in reporting of claims. For this type of business, OneBeacon uses a selected loss ratio method for the initial accident year or years. This is a standard and accepted actuarial reserve estimation method in these circumstances in which the loss ratio is selected based upon information used in pricing policies for that line of business, as well as any publicly available industry data, such as industry pricing, experience and trends, for that line of business.

Uncertainties in estimating ultimate loss and LAE are magnified by the time lag between when a claim actually occurs and when it is reported and settled. This time lag is sometimes referred to as the claim-tail. The claim-tail for most property coverages is typically short (usually a few days up to a few months). The claim-tail for liability/casualty coverages, such as automobile liability, general liability, products liability, multiple peril coverage, and workers compensation, can be especially long as claims are often reported and ultimately paid or settled years, even decades, after the related loss events occur. During the long claims reporting and settlement period, additional facts regarding coverages written in prior accident years, as well as about actual claims and trends may become known and, as a result, OneBeacon may adjust its reserves. If management determines that an adjustment is appropriate, the adjustment is booked in the accounting period in which such determination is made in accordance with GAAP. Accordingly, should reserves need to be increased or decreased in the future from amounts currently established, future results of operations would be negatively or positively impacted, respectively.

In determining ultimate loss and LAE, the cost to indemnify claimants, provide needed legal defense and other services for insureds and administer the investigation and adjustment of claims are considered. These claim costs are influenced by many factors that change over time, such as expanded coverage definitions as a result of new court decisions, inflation in costs to repair or replace damaged property, inflation in the cost of medical services and legislated changes in statutory benefits, as well as by the particular, unique facts that pertain to each claim. As a result, the rate at which claims arose in the past and the costs to settle them may not always be representative of what will occur in the future. The factors influencing changes in claim costs are often difficult to isolate or quantify and developments in paid and incurred losses from historical trends are frequently subject to multiple and conflicting interpretations. Changes in coverage terms or claims handling practices may also cause future experience and/or development patterns to vary from the past. A key objective of actuaries in developing estimates of ultimate loss and LAE, and resulting IBNR reserves, is to identify aberrations and systemic changes occurring within historical experience and accurately adjust for them so that the future can be projected reliably. Because of the factors previously discussed, this process requires the use of informed judgment and is inherently uncertain.

OneBeacon's actuaries use several generally accepted actuarial methods to evaluate its loss reserves, each of which has its own strengths and weaknesses. OneBeacon places more or less reliance on a particular method based on the facts and circumstances at the time the reserve estimates are made. These methods generally fall into one of the following categories or are hybrids of one or more of the following categories:

**Historical paid loss development methods:** These methods use historical loss payments over discrete periods of time to estimate future losses. Historical paid loss development methods assume that the ratio of losses paid in one period to losses paid in an earlier period will remain constant. These methods necessarily assume that factors that have affected paid losses in the past, such as inflation or the effects of litigation, will remain constant in the future. Because historical paid loss development methods do not use case reserves to estimate ultimate losses, they can be more reliable than the other methods discussed below that look to case reserves (such as actuarial methods that use incurred losses) in situations where there are significant changes in how case reserves are established by a company's claims adjusters. However, historical paid loss development methods are more leveraged (meaning that small changes in payments have a larger impact on estimates of ultimate losses) than actuarial methods that use incurred losses because cumulative loss payments take much longer to equal the expected ultimate losses than cumulative incurred amounts. In addition, and for similar reasons, historical paid loss development methods are often slow to react to situations when new or different factors arise than those that have affected paid losses in the past.

**Historical incurred loss development methods:** These methods, like historical paid loss development methods, assume that the ratio of losses in one period to losses in an earlier period will remain constant in the future. However, instead of using paid losses, these methods use incurred losses (i.e., the sum of cumulative historical loss payments plus outstanding case reserves) over discrete periods of time to estimate future losses. Historical incurred loss development methods can be preferable to historical paid loss development methods because they explicitly take into account open cases and the claims adjusters' evaluations of the cost to settle all known claims. However, historical incurred loss development methods necessarily assume that case reserving practices are consistently applied over time. Therefore, when there have been significant changes in how case reserves are established, using incurred

loss data to project ultimate losses can be less reliable than other methods.

Expected loss ratio methods: These methods are based on the assumption that ultimate losses vary proportionately with premiums. Expected loss ratios are typically developed based upon the information used in pricing, and are multiplied by the total amount of premiums written to calculate ultimate losses. Expected loss ratio methods are useful for estimating ultimate losses in the early years of long-tailed lines of business, when little or no paid or incurred loss information is available.

Adjusted historical paid and incurred loss development methods: These methods take traditional historical paid and incurred loss development methods and adjust them for the estimated impact of changes from the past in factors such as inflation, the speed of claim payments or the adequacy of case reserves. Adjusted historical paid and incurred loss development methods are often more reliable methods of predicting ultimate losses in periods of significant change, provided the actuaries can develop methods to reasonably quantify the impact of changes.

### **Construction Defect Claims**

OneBeacon's general liability and multiple peril lines of business have been significantly impacted by a large number of construction defect claims. Construction defect is a liability allegation relating to defective work performed in the construction of structures such as apartments, condominiums, single family dwellings or other housing, as well as the sale of defective building materials. Such claims seek recovery due to damage caused by alleged deficient construction techniques or workmanship. Much of the recent claims activity has been generated by plaintiffs' lawyers who approach new homeowners, and in many cases homeowner associations with large numbers of homeowners in multi-residential complexes, about defects or other flaws in their homes. Claims for construction defects began with claims relating to exposures in California. Then, as plaintiffs' lawyers organized suits in other states with high levels of multi-residential construction, construction defect claims were reported in nearby western states, such as Colorado and Nevada, and eventually throughout the country. The reporting of such claims can be quite delayed as the statute of limitations can be up to ten years. Court decisions have expanded insurers' exposure to construction defect claims as well. For example, in 1995 California courts adopted a "continuous trigger" theory in which all companies that had ever insured a property that was alleged to have been damaged by defective construction must respond to the claimant, even if evidence of the alleged damage did not appear until after the insurance period had expired. As a result, claims may be reported more than ten years after a project has been completed as litigation can proceed for several years before an insurance company is identified as a potential contributor. Claims have also emerged from parties claiming additional insured status on policies issued to other parties (e.g., such as contractors seeking coverage on a sub-contractor's policy). Further, in reserving for these claims, there is additional uncertainty due to the potential for further unfavorable judicial rulings and regulatory actions.

A large number of construction defect claims have been identified relating to coverages that OneBeacon had written in the past through Commercial Union and General Accident and their subsidiaries in California, Colorado, Nevada, Washington and Oregon. Management has sought to mitigate future construction defect risks in all states by no longer providing insurance to certain residential general contractors and sub-contractors involved in multi-habitational projects. Mitigating actions also included initiating the withdrawal from problematic sub-segments within OneBeacon's construction book of business, such as street and road construction, water, sewer and pipeline construction. As a result of these actions, management believes that the number of reported construction defect claims relating to coverages written in the past peaked in 2004 and will continue to decline.

### **Asbestos and Environmental ( A&E ) Reserves**

OneBeacon's reserves include provisions made for claims that assert damages from A&E related exposures. Asbestos claims relate primarily to injuries asserted by those who came in contact with asbestos or products containing asbestos. Environmental claims relate primarily to pollution and related clean-up cost obligations, particularly as mandated by federal and state environmental protection agencies. In addition to the factors described above under **Non-Asbestos and Environmental Reserves** regarding the reserving process, OneBeacon estimates its A&E reserves based upon, among other factors, facts surrounding reported cases and exposures to claims, such as policy limits and deductibles, current law, past and projected claim activity and past settlement values for similar claims, as well as analysis of industry studies and events, such as recent settlements and asbestos-related bankruptcies. The cost of administering A&E claims, which is an important factor in estimating loss reserves, tends to be higher than in the case of non-A&E claims due to the higher legal costs typically associated with A&E claims.

A large portion of OneBeacon's A&E losses resulted from the operations of the Employers Group, an entity acquired by one of the legacy companies in 1971. These operations, including business of Employers Surplus Lines Insurance Company and Employers Liability Assurance Corporation, provided primary and excess liability insurance for commercial insureds, including Fortune 500-sized accounts, some of whom subsequently experienced claims for A&E losses. OneBeacon stopped writing such coverage in 1984.

OneBeacon's liabilities for A&E losses from business underwritten in the recent past are substantially limited by the application of exclusionary clauses in the policy language that eliminated coverage for such claims. After 1987 for pollution and 1992 for asbestos, most liability policies contained industry-standard absolute exclusions of such claims. In earlier years, various exclusions were also applied, but the wording of those exclusions was less strict and subsequent court rulings have reduced their effectiveness.

OneBeacon also incurred A&E losses via its participation in industry pools and associations. The most significant of these pools was Excess Casualty Reinsurance Association ( ECRA ), which provided excess liability reinsurance to U.S. insurers from 1950 until the early 1980s. ECRA incurred significant liabilities for A&E, of which OneBeacon bears approximately a 4.7% share, or \$65 million at both December 31, 2005 and 2004, which is fully reflected in OneBeacon's loss and LAE reserves.

More recently, since the 1990s, OneBeacon has experienced an influx of claims from commercial insureds, including many non-Fortune 500-sized accounts written during the 1970s and 1980s, who are named as defendants in asbestos lawsuits. As a number of large well-known manufacturers of asbestos and asbestos-containing products have gone into bankruptcy, plaintiffs have sought recoveries from peripheral defendants, such as installers, transporters or sellers of such products, or from owners of premises on which the plaintiffs' exposure to asbestos allegedly occurred. At December 31, 2005, 592 policyholders had asbestos-related claims against OneBeacon. In 2005, 128 new insureds with such peripheral involvement presented asbestos claims under prior OneBeacon policies.

Historically, most asbestos claims have been asserted as product liability claims. Recently, insureds who have exhausted the available products liability limits of their insurance policies have sought payment for asbestos claims under the premises and operations coverage of their liability policies. It is more difficult for plaintiffs to establish losses as stemming from premises and operations exposures, which requires proof of the defendant's negligence, rather than products liability under which strict legal liability applies. Hence, there are fewer of such claims and there is a great deal of variation in damages awarded for the actual injuries. Additionally, several accounts that seek such coverage find that previously paid losses exhausted the aggregate limits under their policies. In these situations there is no coverage for these claims. There are currently 243 active claims against OneBeacon without product liability coverage asserting operations or premises coverage.



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Immediately prior to White Mountains' acquisition of OneBeacon, OneBeacon purchased a reinsurance contract with NICO under which OneBeacon is entitled to recover from NICO up to \$2.5 billion in the future for asbestos claims arising from business written by OneBeacon in 1992 and prior, environmental claims arising from business written by OneBeacon in 1987 and prior, and certain other exposures. Under the terms of the NICO Cover, NICO receives the economic benefit of reinsurance recoverables from certain of OneBeacon's third party reinsurers in existence at the time the NICO Cover was executed ( Third Party Recoverables ). As a result, the Third Party Recoverables serve to protect the \$2.5 billion limit of NICO coverage for the benefit of OneBeacon. Any amounts uncollectible from third party reinsurers due to dispute or the reinsurers' financial inability to pay are covered by

NICO under its agreement with OneBeacon. Third Party Recoverables are typically for the amount of loss in excess of a stated level each year. Of claim payments in the past 11 years, approximately 51% of asbestos and environmental losses have been recovered under the historical third party reinsurance.

In June 2005, OneBeacon completed an internal study of its A&E exposures. This study considered, among other items, (1) facts, such as policy limits, deductibles and available third party reinsurance, related to reported claims; (2) current law; (3) past and projected claim activity and past settlement values for similar claims; (4) industry studies and events, such as recent settlements and asbestos-related bankruptcies; and (5) collectibility of third-party reinsurance. Based on the study, OneBeacon increased its best estimate of its incurred losses ceded to NICO, net of underlying reinsurance, by \$353 million (\$841 million gross) to \$2.1 billion, which is within the \$2.5 billion coverage provided by the NICO Cover. OneBeacon estimates that the range of reasonable outcomes around its best estimate is \$1.7 billion to \$2.4 billion, versus a range of \$1.5 billion to \$2.4 billion from its previous study that was conducted in 2003. Due to the NICO Cover, there was no impact to income or equity from the change in estimate.

The increase in the estimate of incurred A&E losses was principally driven by raised projections for claims related to asbestos (particularly from assumed reinsurance business), and for mass torts other than asbestos and environmental, particularly lead and sexual molestation. The increase was partially offset by reduced projections of ultimate hazardous waste losses.

As noted above, OneBeacon estimates that on an incurred basis it has used approximately \$2.1 billion of the coverage provided by NICO at December 31, 2005. Since entering into the NICO Cover, \$26 million of the \$2.1 billion of utilized coverage relates to uncollected amounts from third party reinsurers through December 31, 2005. Net losses paid totaled approximately \$701 million as of December 31, 2005, with \$94 million paid in 2005. Asbestos payments during 2005 reflect payments resulting from intensified efforts by claimants to resolve asbestos claims prior to the potential enactment of Federal asbestos legislation. To the extent that OneBeacon's estimate of ultimate A&E losses as well as the estimate and collectibility of Third Party Recoverables differs from actual experience, the remaining protection under the NICO Cover may be more or less than the approximate \$404 million that OneBeacon estimates remained at December 31, 2005.

OneBeacon's reserves for A&E losses, net of Third Party Recoverables but prior to NICO recoveries, are \$1.3 billion at December 31, 2005. An industry benchmark of reserve adequacy is the survival ratio, computed as a company's reserves divided by its historical average yearly loss payments. This ratio indicates approximately how many more years of payments the reserves can support, assuming future yearly payments are equal to historical levels. OneBeacon's survival ratio was approximately 18.6 at December 31, 2005, which was computed as the ratio of A&E reserves, net of Third Party Recoverables, of \$1.3 billion plus the remaining unused portion of the NICO Cover of \$404 million, to the average loss payments, net of Third Party Recoverables, in the past three years. The average loss payments used to calculate OneBeacon's survival ratio were net of a large commutation (\$64 million) in 2003 with a third party reinsurer. White Mountains believes that as a result of the NICO Cover and its historical third party reinsurance programs, OneBeacon should not experience material financial loss from old A&E exposures under current coverage interpretations and that its survival ratio compares favorably to industry survival ratios.

OneBeacon's reserves for A&E losses at December 31, 2005 represent management's best estimate of its ultimate liability based on information currently available. OneBeacon believes the NICO Cover will be adequate to cover all of its A&E obligations. However, as case law expands, medical and clean-up costs increase and industry settlement practices change, OneBeacon may be subject to asbestos and environmental losses beyond currently estimated amounts. Therefore, OneBeacon cannot guarantee that its A&E loss reserves, plus the remaining coverage under the NICO Cover, will be sufficient to cover additional liability arising from any such unfavorable developments. See Note 3 to the financial statements for more information regarding White Mountains' A&E reserves.

**OneBeacon A&E Claims Activity**

OneBeacon's A&E claim activity for the last two years is illustrated in the table below.

A&E Claims Activity	Year Ended December 31,	
	2005	2004
<b>Asbestos</b>		
Accounts with asbestos claims at the beginning of the year	664	642
Accounts reporting asbestos claims during the year	128	112
Accounts on which asbestos claims were closed during the year	(200)	(90)
Accounts with asbestos claims at the end of the year	592	664
<b>Environmental</b>		
Accounts with environmental claims at the beginning of the year	644	674
Accounts reporting environmental claims during the year	180	110
Accounts on which environmental claims were closed during the year	(329)	(140)
Accounts with environmental claims at the end of the year	495	644
<b>Total</b>		
Total accounts with A&E claims at the beginning of the year	1,308	1,316
Accounts reporting A&E claims during the year	308	222
Accounts on which A&E claims were closed during the year	(529)	(230)
Total accounts with A&E claims at the end of the year	1,087	1,308

**OneBeacon's Loss and LAE Reserves by Line of Business**

OneBeacon's net loss and LAE reserves by line of business at December 31, 2005 and 2004 were as follows:

**Net loss and LAE reserves by class of business**

(\$ in millions)	December 31, 2005			December 31, 2004		
	Case	IBNR	Total	Case	IBNR	Total
Workers compensation	\$ 195.2	\$ 132.6	\$ 327.8	\$ 362.1	\$ 135.5	\$ 497.6
Personal automobile liability	445.5	174.7	620.2	530.7	244.1	774.8
Multiple peril	310.4	236.0	546.4	359.3	264.3	623.6
Commercial automobile liability	140.2	65.6	205.8	203.8	82.8	286.6
General liability	106.1	227.2	333.3	121.6	151.1	272.7
Homeowners/Farmowners	81.1	41.4	122.5	82.2	41.8	124.0
Other	115.5	59.9	175.4	97.5	84.0	181.5
Total	\$ 1,394.0	\$ 937.4	\$ 2,331.4	\$ 1,757.2	\$ 1,003.6	\$ 2,760.8

For OneBeacon, the range of reserve estimates at December 31, 2005 was evaluated to consider the strengths and weaknesses of the actuarial methods applied against OneBeacon's historical claims experience data. The following table shows the recorded reserves and the high and low ends of OneBeacon's range of reasonable loss reserve estimates at December 31, 2005. The high and low ends of OneBeacon's range of reserve estimates in the table below are based on the results of various actuarial methods described above. The recorded reserve for each line is the result of the actuarial method that management believes to be most appropriate based on known facts and trends.



**OneBeacon net loss and LAE reserves by line of business****Range and recorded reserves**

(\$ in millions)	December 31, 2005		
	Low	Recorded	High
Workers compensation	\$ 291	\$ 327.8	\$ 385
Personal automobile liability	560	620.2	659
Multiple peril	499	546.4	658
Commercial automobile liability	191	205.8	231
General liability	282	333.3	372
Homeowners/Farmowners	110	122.5	125
Other	159	175.4	180
Total	\$ 2,092	\$ 2,331.4	\$ 2,610

The recorded reserves represent management's best estimate of unpaid loss and LAE by line of business. In its selection of recorded reserves, management has generally given greater weight to adjusted paid loss development methods, which are not dependent on the consistency of case reserving practices, rather than methods that rely on incurred losses, because of the increased adequacy of case reserving by OneBeacon's claim staff in the recent past. For multiple peril this resulted in OneBeacon recording reserves nearer the low end of the range. For some types of claims, such as workers compensation and construction defect, management also considered special purpose forecasting models that its claims and actuarial staff have created that consider the unique loss development characteristics of these types of claims. For personal automobile liability, homeowners and other (principally shorter tailed lines of business such as ocean and inland marine insurance) recorded reserves remain rather high in the respective ranges, as management's selections reflect a conservative approach to recognition of recent favorable development experienced in our ongoing businesses.

While variability is reflected in part in the size of the range of reserves developed by OneBeacon, that range may still not be indicative of the potential variance between the ultimate outcome and recorded reserve. This is because ranges are developed based on known events as of the valuation date, whereas the ultimate disposition of losses is subject to the outcome of events and circumstances that may be unknown as of the valuation date. The probability that ultimate losses will fall outside of the ranges of estimates by line of business is higher for each line of business individually than it is for the sum of the estimates for all lines taken together due to the effects of diversification. The diversification effects result from the fact that losses across OneBeacon's different lines of business are not completely correlated. Although management believes OneBeacon's reserves are reasonably stated, ultimate losses may deviate, perhaps materially, from the recorded reserve amounts and could be above the high end of the range of actuarial projections.

**White Mountains Re****White Mountains Re A&E Reserves**

White Mountains Re's A&E exposure is primarily from reinsurance contracts written between 1974 through 1985 by Folksamerica predecessor companies (MONY Reinsurance and Christiania General). The exposures are mostly higher layer excess of loss treaty and facultative coverages with relatively low limits exposed for each claim. Folksamerica has a specialized unit that handles claims relating to A&E exposures. The issues presented by these types of claims require specialization, expertise and an awareness of the various trends and jurisdictional developments. Net incurred loss activity for asbestos and environmental in the last two years was as follows:

Net incurred loss and LAE activity (\$ in millions)	December 31,	
	2005	2004
Asbestos	\$ 62.0	\$ 2.6
Environmental	(3.4)	.1
Total	\$ 58.6	\$ 2.7



During 2005, White Mountains Re completed a detailed, ground up asbestos study on all reported Folksamerica insureds that had over \$250,000 of asbestos claims as well as a significant sample of all other insureds with reported asbestos claims of less than \$250,000. Comparing estimates generated by the study to Folksamerica exposed limits by underwriting year led to an increase of approximately \$50 million in IBNR during the third quarter of 2005.

Folksamerica sets up claim files for each reported claim by each cedent for each individual insured. In many instances, a single claim notification from a cedent could involve several years and layers of coverage resulting in a file being set up for each involvement. Precautionary claim notices are submitted by the ceding companies in order to preserve their right to pursue coverage under the reinsurance contract. Such notices do not contain an incurred loss amount to Folksamerica, accordingly, an open claim file is not established. As of December 31, 2005, White Mountains Re had approximately 1,339 open claim files for asbestos and 750 open claim files for environmental exposures.

The costs associated with administering the underlying A&E claims by White Mountains Re's clients tend to be higher than non A&E claims due to generally higher legal costs incurred by ceding companies in connection with A&E claims ceded to White Mountains Re under the reinsurance contracts.

#### White Mountains Re A&E Claims Activity

White Mountains Re's A&E claim activity for the last two years is illustrated in the table below.

A&E Claims Activity	2005	Year ended December 31,	2004
<b>Asbestos</b>			
Total asbestos claims at the beginning of the year	1,401		1,185
Incoming asbestos claims due to Sirius Acquisition			232
Asbestos claims reported during the year	223		292
Asbestos claims closed during the year	(285)		(308)
Total asbestos claims at the end of the year	1,339		1,401
<b>Environmental</b>			
Total environmental claims at the beginning of the year	900		743
Incoming environmental claims due to Sirius Acquisition			220
Environmental claims reported during the year	65		138
Environmental claims closed during the year	(215)		(201)
Total environmental claims at the end of the year	750		900
<b>Total</b>			
Total A&E claims at the beginning of the year	2,301		1,928
Incoming A&E claims due to Sirius Acquisition			452
A&E claims reported during the year	288		430
A&E claims closed during the year	(500)		(509)
Total A&E claims at the end of the year	2,089		2,301

### Loss and LAE Reserves by Class of Business

White Mountains Re establishes loss and LAE reserves that are estimates of amounts needed to pay claims and related expenses in the future for reinsured events that have already occurred. The estimation of net reinsurance loss and LAE reserves is subject to the same risk as the estimation of insurance loss and LAE reserves. In addition to those risk factors which give rise to inherent uncertainties in establishing insurance loss and LAE reserves, the inherent uncertainties of estimating such reserves are even greater for the reinsurer, due primarily to: (1) the claim-tail for reinsurers being further extended because claims are first reported to the ceding company and then through one or more intermediary insurers or reinsurers, (2) the diversity of loss development patterns among different types of reinsurance treaties or facultative contracts, (3) the necessary reliance on the ceding companies for information regarding reported claims and (4) the differing reserving practices among ceding companies.

As with insurance reserves, the process of estimating reinsurance reserves involves a considerable degree of judgment by management and, as of any given date, is inherently uncertain. Based on the above, such uncertainty may be larger relative to the reserve for a reinsurer compared to an insurance company, and may take a longer time to emerge.

In order to reduce the potential uncertainty of loss reserve estimation, White Mountains Re obtains information from numerous sources to assist in the process. White Mountains Re's pricing actuaries devote considerable effort to understanding and analyzing a ceding company's operations and loss history during the underwriting of the business, using a combination of ceding company and industry statistics. Such statistics normally include historical premium and loss data by class of business, individual claim information for larger claims, distributions of insurance limits provided, loss reporting and payment patterns, and rate change history. This analysis is used to project expected loss ratios for each treaty during the upcoming contract period. These expected ultimate loss ratios are aggregated across all treaties and are input directly into the loss reserving process to generate the expected loss ratios that are used to estimate IBNR.

Upon notification of a loss from a ceding company, White Mountains Re establishes case reserves, including LAE reserves, based upon White Mountains Re's share of the amount of reserves established by the ceding company and our independent evaluation of the loss. In cases where available information indicates that reserves established by the ceding company are inadequate, White Mountains Re establishes case reserves or IBNR in excess of its share of the reserves established by the ceding company. In addition, specific claim information reported by ceding companies or obtained through claim audits can alert us to emerging trends such as changing legal interpretations of coverage and liability, claims from unexpected sources or classes of business, and significant changes in the frequency or severity of individual claims. Such information is often used to supplement estimates of IBNR.

As mentioned above, there can be a considerable time lag from the time a claim is reported to a ceding company to the time it is reported to the reinsurer. The lag can be several years in some cases. This lag can be due to a number of reasons, including the time it takes to investigate a claim, delays associated with the litigation process, the deterioration in a claimant's physical condition many years after an accident occurs, etc. In its loss reserving process, White Mountains Re assumes that such lags are predictable, on average, over time and therefore the lags are contemplated in the loss reporting patterns used in its actuarial methods. This means that, as a reinsurer, White Mountains Re must rely on such actuarial estimates for a longer period of time after reserves are first estimated than does a primary insurance company.

Backlogs in the recording of assumed reinsurance can also complicate the accuracy of loss reserve estimation. As of December 31, 2005, there were no significant backlogs related to the processing of assumed reinsurance information at White Mountains Re.



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White Mountains Re relies heavily on information reported by ceding companies, as discussed above. In order to determine the accuracy and completeness of such information, White Mountains Re's U.S. underwriters, actuaries, and claims personnel perform regular audits of Folksamerica's ceding companies. While regular ceding company audits are not customary outside the United States, Sirius International's staff regularly reviews information from ceding companies for unusual or unexpected results. Any material findings are discussed with the ceding companies. White Mountains Re sometimes encounters situations where we determine that a claim presentation from a ceding company is not in accordance with contract terms. In these situations, White Mountains Re attempts to resolve the dispute directly with the ceding company. Most situations are resolved amicably and without the need

for litigation or arbitration. However, in the infrequent situations where a resolution is not possible, White Mountains Re will vigorously defend our position in such disputes.

Although loss and LAE reserves are initially determined based on underwriting and pricing analysis, White Mountains Re constantly tests the accuracy of reserves using a variety of generally accepted actuarial methods, including historical incurred and paid loss development methods. If actual loss activity differs substantially from expectations based on historical information, an adjustment to loss reserves may be warranted. As time passes, loss reserve estimates for a given accident year will rely more on actual loss activity and historical patterns than on initial assumptions based on pricing indications.

White Mountains Re also obtain reinsurance whereby another reinsurer contractually agrees to indemnify White Mountains Re for all or a portion of the reinsurance risks underwritten by White Mountains Re. Such arrangements, where one reinsurer provides reinsurance to another reinsurer, are usually referred to as retrocessional reinsurance arrangements. White Mountains Re establishes estimates of amounts recoverable from retrocessional reinsurance in a manner consistent with the loss and LAE liability associated with reinsurance contracts offered to its customers (the ceding companies), net of an allowance for uncollectible amounts, if any. Net reinsurance loss reserves represent loss and LAE reserves reduced by retrocessional reinsurance recoverable on unpaid losses.

White Mountains Re's net loss and LAE reserves by class of business at December 31, 2005 and 2004 were as follows:

Net loss and LAE reserves by class of business (\$ in millions)	December 31, 2005			December 31, 2004		
	Case	IBNR	Total	Case	IBNR	Total
Liability (excluding A&E)	\$ 829.3	\$ 782.9	\$ 1,612.2	\$ 920.4	\$ 900.0	\$ 1,820.4
Property	357.7	342.2	699.9	143.3	318.0	461.3
Accident & Health and Other	233.9	138.4	372.3	279.5	187.5	467.0
A&E	42.0	75.4	117.4	50.2	24.8	75.0
Total	\$ 1,462.9	\$ 1,338.9	\$ 2,801.8	\$ 1,393.4	\$ 1,430.3	\$ 2,823.7

White Mountains Re establishes loss reserves based on a single point estimate, which is management's best estimate of ultimate losses and loss expenses. This best estimate is derived from a combination of methods as described above. Once a point estimate is established, White Mountains Re's actuaries estimate loss reserve ranges to measure the sensitivity of the actuarial assumptions used to set the point estimates. These ranges are calculated using similar methods to the point estimate calculation, but with different expected loss ratio and loss reporting pattern assumptions. For the low estimate, more optimistic loss ratios and faster reporting patterns are assumed, while the high estimate uses more conservative loss ratios and slower reporting patterns. These variable assumptions are derived from historical variations in loss ratios and reporting patterns by class and type of business. Due to the inherent difficulties in estimating ultimate A&E exposures, White Mountains Re does not estimate ranges for these reserves.

The following table illustrates White Mountains Re's recorded net loss and LAE reserves and high and low estimates for those classes of business for which a range is calculated, at December 31, 2005.

Net loss and LAE reserves by class of business (\$ in millions)	December 31, 2005		
	Low	Recorded	High
Liability (excluding A&E)	\$ 1,490	\$ 1,612.2	\$ 1,760
Property	670	699.9	730
Accident & Health and Other	320	372.3	440

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Sub-total	\$	2,480	\$	<b>2,684.4</b>	\$	2,930
A&E				<b>117.4</b>		
Total			\$	<b>2,801.8</b>		

The probability that ultimate losses will fall outside of the ranges of estimates by class of business is higher for each class of business individually than it is for the sum of the estimates for all classes taken together due to the effects of diversification. Although management believes reserves for White Mountains Re are reasonably stated, ultimate losses may deviate, perhaps materially, from the recorded reserve amounts and could be above the high end of the range of actuarial projections.

## 2. White Mountains Re Reinsurance Estimates

There is a time lag from the point when premium and related commission and expense activity is recorded by a ceding company to the point when such information is reported by the ceding company, through its reinsurance intermediary, to White Mountains Re. This time lag can vary from one to several contractual reporting periods (i.e. quarterly/monthly). This lag is common in the broker market reinsurance business.

As a result of this time lag in reporting, White Mountains Re estimates a portion of its written premium and related commissions and expenses. Given the nature of White Mountains Re's business, estimated premium balances, net of related commissions and expenses, comprise a large portion of total premium balances receivable. The estimation process begins by identifying which major accounts have not reported activity at the most recent period end. In general, premium estimates for excess of loss business are based on minimum deposit information included in the contractual terms. For proportional business, White Mountains Re's estimates are derived based on a variety of factors and assumptions, including: prior reporting from the broker or ceding company, historical reporting patterns, expected premium volume based on contractual terms or ceding company reports and other correspondence and communication with underwriters, brokers, intermediaries and ceding companies. Once premium estimates are determined, related commission and expense estimates are derived using contractual terms.

White Mountains Re closely monitors its estimation process on a quarterly basis and adjusts its estimates as more information and actual amounts become known. There is no assurance that the amounts estimated by White Mountains Re will not deviate from the amounts reported by the ceding company or reinsurance broker. Any such deviations are reflected in the results of operations when they become known.

The following table summarizes White Mountains Re's premium estimates and related commissions and expenses:

Millions	December 31, 2005					Total
	Liability	Property	Accident & Health	Other		
Gross premium estimates	\$ 123.1	\$ 245.0	\$ 34.2	\$ 67.1	\$ 469.4	
Net premium estimates	\$ 111.2	\$ 123.0	\$ 25.5	\$ 52.0	\$ 311.7	
Net commission and expense estimates	38.3	26.0	9.0	16.5	89.8	
Net amount included in reinsurance balances receivable	\$ 72.9	\$ 97.0	\$ 16.5	\$ 35.5	\$ 221.9	

Millions	December 31, 2004					Total
	Liability	Property	Accident & Health	Other		
Gross premium estimates	\$ 150.7	\$ 234.8	\$ 41.9	\$ 72.9	\$ 500.3	
Net premium estimates	\$ 148.5	\$ 129.1	\$ 33.6	\$ 65.5	\$ 376.7	

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Net commission and expense estimates		43.3		12.9		8.4		15.9		80.5
Net amount included in reinsurance balances receivable	\$	105.2	\$	116.2	\$	25.2	\$	49.6	\$	296.2

The net amounts recorded in reinsurance balances receivable may not yet be due from the ceding company at the time of the estimate since actual reporting from the ceding company has not yet occurred. Therefore, based on the process described above, White Mountains Re believes all of its estimated balances are collectible, and as such no allowance has been recorded.

### 3. Reinsurance Transactions

White Mountains insurance and reinsurance subsidiaries purchase reinsurance from time to time to protect their businesses from losses due to exposure aggregation, to manage their operating leverage ratios and to limit ultimate losses arising from catastrophic events. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policies. Amounts related to reinsurance contracts are recorded in accordance with SFAS No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts ( SFAS 113 ).

The collectibility of reinsurance recoverables is subject to the solvency and willingness to pay of the reinsurer. The Company is selective in choosing its reinsurers, placing reinsurance principally with those reinsurers with a strong financial condition, industry ratings and underwriting ability. Management monitors the financial condition and ratings of its reinsurers on an ongoing basis. See **Note 4 - "Third Party Reinsurance"** in the accompanying Consolidated Financial Statements for additional information on White Mountains reinsurance programs.

### 4. Purchase Accounting

When White Mountains acquires another company, management must estimate the fair values of the assets and liabilities acquired, as prescribed by SFAS No. 141, Business Combinations. Certain assets and liabilities require little judgment to estimate their fair values, particularly those that are quoted on a market exchange, such as publicly-traded investment securities. Other assets and liabilities, however, require a substantial amount of judgment to estimate their fair values. The most significant of these is the estimation required to fair value loss and LAE reserves. White Mountains estimates the fair value of loss and LAE reserves obtained in an acquisition following the principles contained within FASB Statement of Financial Accounting Concepts No. 7: Using Cash Flow Information and Present Value in Accounting Measurements ( CON 7 ). Under CON 7, the fair value of a particular asset or liability essentially contains five elements: (1) an estimate of the future cash flows, (2) expectations about possible variations in the amount or timing of those cash flows; (3) the time value of money, represented by the risk-free rate of interest; (4) the price for bearing the uncertainty inherent in the asset or liability; and (5) other, sometimes unidentifiable, factors including illiquidity and market imperfections.

White Mountains actuaries estimate the fair value of loss and LAE reserves obtained in an acquisition by taking the acquired company's recorded reserves and discounting them based on expected reserve payout patterns using the current risk-free rate of interest. Then, White Mountains actuaries develop additional cash flow scenarios that use different payout and ultimate reserve assumptions deemed to be reasonably possible based upon the inherent uncertainties present in determining the amount and timing of payment of such reserves. In each scenario, the risk-free rate of interest is used to discount future cash flows. These scenarios are put in a statistical model that assigns a probability to each cash flow scenario. White Mountains actuaries then choose the scenario that best represents the price for bearing the uncertainty inherent within the acquired company's recorded reserves. The price for bearing the uncertainty inherent within the acquired company's reserves is measured as the difference between the selected cash flow scenario and the expected cash flow scenario. The scenario selected has typically been between 1.5 and 2 standard deviations from the expected cash flow outcome. The fair value of the acquired company's loss and LAE reserves is determined to be the sum of the expected cash flow scenario (i.e., the acquired company's discounted loss and LAE reserves) and the uncertainty price.

The difference between an acquired company's loss and LAE reserves and White Mountains' best estimate of the fair value of such reserves at the acquisition date is amortized ratably over the payout period of the acquired loss and LAE reserves. Historically, the fair value of an acquired company's loss and LAE reserves has been less than its nominal reserves at acquisition. Accordingly, the amortization has been and will continue to be recorded as an expense on White Mountains' income statement until fully amortized.



## FORWARD-LOOKING STATEMENTS

The information contained in this report may contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements, other than statements of historical facts, included or referenced in this report which address activities, events or developments which White Mountains expects or anticipates will or may occur in the future are forward-looking statements. The words will, believe, intend, expect, anticipate, project, estimate, predict and similar expressions are intended to identify forward-looking statements. These forward-looking statements include, among others, statements with respect to White Mountains :

growth in book value per share or return on equity;

business strategy;

financial and operating targets or plans;

incurred losses and the adequacy of its losses and LAE reserves and related reinsurance;

projections of revenues, income (or loss), earnings (or loss) per share, dividends, market share or other financial forecasts;

expansion and growth of its business and operations; and

future capital expenditures.

These statements are based on certain assumptions and analyses made by White Mountains in light of its experience and perception of historical trends, current conditions and expected future developments, as well as other factors believed to be appropriate in the circumstances. However, whether actual results and developments will conform with its expectations and predictions is subject to a number of risks and uncertainties that could cause actual results to differ materially from expectations, including:

the risks discussed in Item 1A of this Form 10-K;

claims arising from catastrophic events, such as hurricanes, earthquakes, floods or terrorist attacks;

the continued availability of capital and financing;

general economic, market or business conditions;

business opportunities (or lack thereof) that may be presented to it and pursued;

competitive forces, including the conduct of other property and casualty insurers and reinsurers;



changes in domestic or foreign laws or regulations, or their interpretation, applicable to White Mountains, its competitors or its clients;

an economic downturn or other economic conditions adversely affecting its financial position;

recorded loss reserves subsequently proving to have been inadequate; and

other factors, most of which are beyond White Mountains' control.

Consequently, all of the 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 White Mountains will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, White Mountains or its business or operations. White Mountains assumes no obligation to update publicly any such forward-looking statements, whether as a result of new information, future events or otherwise.

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

White Mountains' consolidated balance sheet includes a substantial amount of assets and liabilities whose fair values are subject to market risk. The term market risk refers to the risk of loss arising from adverse changes in interest rates and other relevant market rates and prices. Due to White Mountains' sizable balances of interest rate sensitive instruments, market risk can have a significant effect on White Mountains' consolidated financial position.

**Interest Rate Risk**

**Fixed Maturity Portfolio.** In connection with the Company's consolidated insurance and reinsurance subsidiaries, White Mountains invests in interest rate sensitive securities, primarily debt securities. White Mountains' strategy is to purchase fixed maturity investments that are attractively priced in relation to perceived credit risks. White Mountains' fixed maturity investments are held as available for sale in accordance with SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities (SFAS 115), whereby these investments are carried at fair value on the balance sheet with net unrealized gains or losses reported net of tax in a separate component of common shareholders equity. White Mountains generally manages its interest rate risk associated with its portfolio of fixed maturity investments by monitoring the average duration of the portfolio, which allows White Mountains to achieve an adequate yield without subjecting the portfolio to an unreasonable level of interest rate risk. White Mountains' fixed maturity portfolio is comprised of primarily investment grade corporate securities, U.S. government and agency securities, municipal obligations and mortgage-backed securities (e.g., those receiving an investment grade rating from Standard & Poor's or Moody's).

Increases and decreases in prevailing interest rates generally translate into decreases and increases in fair values of fixed maturity investments, respectively. Additionally, fair values of interest rate sensitive instruments may be affected by the creditworthiness of the issuer, prepayment options, relative values of alternative investments, the liquidity of the instrument and other general market conditions.

The table below summarizes the estimated effects of hypothetical increases and decreases in market interest rates on White Mountains' fixed maturity portfolio and pension plan.

\$ in millions	Fair Value at December 31, 2005	Assumed Change in Relevant Interest Rate	Estimated Fair Value After Change in Interest Rate	After-Tax Increase (Decrease) in Carrying Value
Fixed maturity investments	\$ 7,582.7	100 bp decrease	\$ 7,750.2	\$ 110.5
		50 bp decrease	7,667.4	55.9
		50 bp increase	7,496.9	(56.6)
		100 bp increase	7,409.5	(114.2)
Pension fixed maturity investments	\$ 277.9	100 bp decrease	\$ 284.1	\$ 4.0
		50 bp decrease	281.0	2.0
		50 bp increase	274.8	(2.0)
		100 bp increase	271.8	(3.9)

**Long-term obligations.** As of December 31, 2005, White Mountains' interest and dividend bearing long-term obligations consisted primarily of the Senior Notes, the Berkshire Preferred Stock and the Zenith Preferred Stock obligations, which have fixed interest and dividend rates. As a result, White Mountains' exposure to interest rate risk resulting from variable interest rate obligations is insignificant.

The Senior Notes were issued in 2003 and mature on May 15, 2013. At December 31, 2005, the fair value of the Senior Notes was approximately \$705 million, which compared to a carrying value of \$699 million. The Berkshire Preferred Stock and Zenith Preferred Stock

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obligations were issued in 2001 and mature on May 31, 2008 and May 31, 2011, respectively. At December 31, 2005, the fair values of the Berkshire Preferred Stock and Zenith Preferred Stock obligations were approximately \$332 million and \$22 million, respectively, which compared to carrying values of \$214 million and \$20 million, respectively.

The fair values of these obligations were estimated by discounting future cash flows using current market rates for similar obligations or using quoted market prices.

### **Equity Price Risk**

The carrying values of White Mountains' common equity securities and its other investments are based on quoted market prices or management's estimates of fair value (which is based, in part, on quoted market prices) as of the balance sheet date. Market prices of common equity securities, in general, are subject to fluctuations which could cause the amount to be realized upon sale or exercise of the instruments to differ significantly from the current reported value. The fluctuations may result from perceived changes in the underlying economic characteristics of the investee, the relative price of alternative investments, general market conditions and supply and demand imbalances for a particular security.

### **Foreign Currency Exchange Rates**

White Mountains' foreign assets and liabilities are valued using period-end exchange rates and its foreign revenues and expenses are valued using average exchange rates. Foreign currency exchange rate risk is the risk that White Mountains will incur losses on a U.S. dollar basis due to adverse changes in foreign currency exchange rates.

At December 31, 2005, OneBeacon held approximately \$254 million in bonds denominated in foreign currencies, mostly those denominated in British Pounds and Australian dollars. Assuming a hypothetical 10% increase or decrease in the rate of exchange from the British Pound and Australian dollar to the U.S. dollar as of December 31, 2005, the carrying value of OneBeacon's foreign currency-denominated bond portfolio would have respectively decreased or increased by approximately \$25 million.

The functional currency of Sirius International is the Swedish Krona. Assuming a hypothetical 10% increase or decrease in the rate of exchange from the Swedish Krona to the U.S. dollar as of December 31, 2005, the carrying value of White Mountains' net assets denominated in Swedish Kronor would have respectively decreased or increased by approximately \$33 million.

## **Item 8. Financial Statements and Supplementary Data**

The financial statements and supplementary data have been filed as a part of this Annual Report on Form 10-K as indicated in the Index to Consolidated Financial Statements and Financial Statement Schedules appearing on page 84 of this report.

## **Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure**

None.

## **Item 9A. Controls and Procedures**

The Principal Executive Officer ( PEO ) and the Principal Financial Officer ( PFO ) of White Mountains have evaluated the effectiveness of its disclosure controls and procedures (as defined in Rule 13a-15(e) of the Exchange Act) as of December 31, 2005. Based on that evaluation, the PEO and PFO have concluded that White Mountains' disclosure controls and procedures are adequate and effective.

The PEO and the PFO of White Mountains have evaluated the effectiveness of its internal control over financial reporting as of December 31, 2005. Based on that evaluation, the PEO and PFO have concluded that White Mountains' internal control over financial reporting is effective. Management's annual report on internal control over financial reporting is included on page F-67 of this report. The attestation report on management's assessment of its internal control over financial reporting by PricewaterhouseCoopers LLP is included on pages F-68 through F-69 of this report.

There have been no significant changes in White Mountains' internal controls, or in factors that could significantly affect internal controls, subsequent to their most recent evaluation of such controls.

**Item 9B. Other Information**

None.

**PART III**

**Item 10. Directors and Executive Officers of the Registrant**

**a. Directors**

Reported under the caption "The Board of Directors" of the Company's 2006 Proxy Statement, herein incorporated by reference.

**b. Executive Officers**

Reported in Part I pursuant to General Instruction G to Form 10-K.

**c. Audit Committee Financial Expert**

Reported under the caption "Corporate Governance - Committees of the Board - Audit Committee" of the Company's 2006 Proxy Statement, herein incorporated by reference.

**d. Code of Business Conduct and Ethics**

The Company's Code of Business Conduct, which applies to all directors, officers and employees in carrying out their responsibilities to and on behalf of the Company, has been filed herein as Exhibit 14.

**e. Compliance with Section 16(a) of the Exchange Act**

Reported under the caption "Compliance with Section 16(a) of the Exchange Act" of the Company's 2006 Proxy Statement, herein incorporated by reference.

**Item 11. Executive Compensation**

Reported under the captions Compensation of Executive Officers , Report of the Compensation Committee on Executive Compensation and Member Performance Graph of the Company s 2006 Proxy Statement, herein incorporated by reference.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

Reported under the captions Voting Securities and Principal Holders Thereof and Equity Compensation Plan Table of the Company s 2006 Proxy Statement, herein incorporated by reference.

**Item 13. Certain Relationships and Related Transactions**

Reported under the caption Certain Relationships and Related Transactions of the Company s 2006 Proxy Statement, herein incorporated by reference.

**Item 14. Principal Accountant Fees and Services**

Reported under the caption Independent Registered Public Accountant Fees and Services of the Company s 2006 Proxy Statement, herein incorporated by reference.

**PART IV****Item 15. Exhibits and Financial Statement Schedules****a. Documents Filed as Part of the Report**

The financial statements and financial statement schedules and reports of independent auditors have been filed as part of this Annual Report on Form 10-K as indicated in the Index to Consolidated Financial Statements and Financial Statement Schedules appearing on page 84 of this report. A listing of exhibits filed as part of the report appear on pages 81 through 82 of this report.

**b. Exhibits**

Exhibit number	Name
2	Plan of Reorganization (incorporated by reference herein to the Company's Registration Statement on S-4 (No. 333-87649) dated September 23, 1999)
3.1	Memorandum of Continuance of the Company (incorporated by reference herein to Exhibit (3)(I) of the Company's Current Report on Form 8-K dated November 1, 1999)
3.2	Bye-Laws of the Company (incorporated by reference herein to Annex III of the Company's Registration Statement on Form S-4 (No. 333-87649) dated September 23, 1999)
4	Amended and Restated Certificate of Designation of Series A Preferred Stock of Fund American (incorporated by reference herein to Exhibit 99.1 of the Company's Report on Form 8-K dated December 3, 2004)
10.1	Amendment Agreement dated as of November 30, 2004, between General Reinsurance Corporation, a Delaware corporation, the Company and Fund American (incorporated by reference herein to Exhibit 99.2 of the Company's Report on Form 8-K dated December 3, 2004)
10.2	Keep-Well Agreement, dated as of November 30, 2004, by and between the Company and Fund American (incorporated by reference herein to Exhibit 99.3 of the Company's Report on Form 8-K dated December 3, 2004)
10.3	Stock Purchase Agreement by and among Safeco Corporation, General America Corporation, The Company, Occum Acquisition Corp. dated as of March 31, 2004 (incorporated by reference herein to Exhibit 10 of the Company's Report on Form 8-K dated March 15, 2004)
10.4	\$400,000,000 Credit Agreement, dated as of August 26, 2004, among the Company and Fund American, as the borrowers, the several lenders from time to time parties hereto, JPMorgan Chase Bank, as Syndication Agent, and Bank of America, NA as Administrative Agent. (incorporated by reference herein to Exhibit 10 of the Company's Report on Form 10-Q dated November 2, 2004)
10.5	Adverse Development Agreement of Reinsurance No. 8888 between Potomac Insurance Company and GRC dated April 13, 2001 (incorporated by reference herein to Exhibit 99(m) of the Company's Report on Form 8-K dated June 1, 2001)
10.6	Adverse Development Agreement of Reinsurance between NICO (and certain of its affiliates) and Potomac Insurance Company dated April 13, 2001 and related documents (incorporated by reference herein to Exhibits 99(n), 99(o), 99(p) and 99(q) of the Company's Report on Form 8-K dated June 1, 2001)
10.7	Subscription Agreement among Berkshire, Fund American and the Registrant dated May 30, 2001 (incorporated by reference herein to Exhibits 99(t) of the Company's Report on Form 8-K dated June 1, 2001)
10.8	Master Agreement by and among the Company, OneBeacon and Liberty Mutual including the Liberty RRA and related documents (incorporated by reference herein to Exhibits 99(d), 99(e), 99(f), 99(g) and 99(h) of the Company's Report on Form 8-K dated November 1, 2001)
10.9	Investment Management Agreement between Prospector Partners, LLC and White Mountains Advisors LLC. (incorporated by reference herein to Exhibit 99.1 of the Company's Report on Form 8-K dated June 20, 2005)



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- 10.10 Amendment to the investment Management Agreement between Prospector Partners, LLC and White Mountains Advisors, LLC dated February 23, 2006 (incorporated by reference herein the Company's Report on Form 8-K dated February 28, 2006)
- 10.11 Consulting Letter Agreement between Prospector Partners, LLC and White Mountains Advisors LLC (incorporated by reference herein to Exhibit 99.2 of the Company's Report on Form 8-K dated June 20, 2005)
- 10.12 Folksamerica Holding Company, Inc. Long-Term Incentive Plan - 2003 and Prior (incorporated by reference herein to Exhibit 10.10 of the Company's 2004 Annual Report on Form 10-K)
- 10.13 White Mountains Re Group, Ltd. Long-Term Incentive Unit Plan (incorporated by reference herein to Exhibit 10.11 of the Company's 2004 Annual Report on Form 10-K)
- 10.14 Folksamerica Holding Company, Inc. Voluntary Deferred Compensation Plan (incorporated by reference herein to Exhibit 10.14 of the Company's 2004 Annual Report on Form 10-K)
- 10.15 Folksamerica Holding Company, Inc. Deferred Benefit Plan (incorporated by reference herein to Exhibit 10.15 of the Company's 2004 Annual Report on Form 10-K)

Exhibit number	Name
10.16	White Mountains Long-Term Incentive Plan, as amended, (incorporated by reference to Appendix A of the Company's Notice of 2005 Annual General Meeting of Shareholders and Proxy Statement dated April 5, 2005)
10.17	White Mountains Bonus Plan (incorporated by reference herein to Exhibit 10.17 of the Company's 2004 Annual Report on Form 10-K)
10.18	The Company's Voluntary Deferred Compensation Plan (incorporated by reference herein to Exhibit 4(c) of the Company's Report on Form S-8 dated October 19, 1999)
10.19	White Mountains Insurance Group Deferred Compensation Plan (incorporated by reference herein to Exhibit 10.14 of the Company's 2003 Annual Report on Form 10-K)
10.20	Fund American Deferred Compensation Plan (incorporated by reference herein to Exhibit 10.15 of the Company's 2003 Annual Report on Form 10-K)
10.21	Esurance Holdings, Inc. Select Deferred Compensation Plan (*)
10.22	OneBeacon Insurance Performance Unit Plan (incorporated by reference herein to Exhibit 10.16 of the Company's 2003 Annual Report on Form 10-K)
10.23	OneBeacon's 2005 Management Incentive Plan (*)
10.24	OneBeacon Insurance Deferred Compensation Plan (incorporated by reference herein to Exhibit 10.18 of the Company's 2003 Annual Report on Form 10-K)
10.25	OneBeacon Performance Plan (*)
10.26	Amended and Restated Revenue Sharing Agreement among John D. Gillespie, Fund American Companies, Inc. and Folksamerica Reinsurance Company (incorporated by reference herein to Exhibit 10.26 of the Company's 2004 Annual Report on Form 10-K)
11	Statement Re Computation of Per Share Earnings (**)
12	Statement Re Computation of Ratio of Earnings to Fixed Charges (*)
14	The Company's Code of Business Conduct, which applies to all directors, officers and employees in carrying out their responsibilities to and on behalf of the Company (incorporated by reference herein to Exhibit 14 of the Company's 2004 Annual Report on Form 10-K)
21	Subsidiaries of the Registrant (*)
23	Consent of PricewaterhouseCoopers LLP dated March 7, 2006 (*)
24	Powers of Attorney (*)
31.1	Principal Executive Officer Certification Pursuant to Rule 13a-14 (a) of the Securities Exchange Act of 1934 (*)
31.2	Principal Financial Officer Certification Pursuant to Rule 13a-14 (a) of the Securities Exchange Act of 1934 (*)
32.1	Principal Executive Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (*)
32.2	Principal Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (*)
99	Text entitled "Non-Asbestos and Environmental Reserves" under the caption "Loss and Loss Adjustment Expense Reserves" (incorporated by reference herein to pages 31 through 43 of the Company's Form S-3 dated March 14, 2003)

(\*) Included herein.

(\*\*) Not included herein as the information is contained elsewhere within report. See Note 1 of the Notes to Consolidated Financial Statements.

### c. Financial Statement Schedules

The financial statement schedules and report of independent registered public accounting firm have been filed as part of this Annual Report on Form 10-K as indicated in the Index to Consolidated Financial Statements and Financial Statement Schedules appearing on page 84 of this report.



**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**WHITE MOUNTAINS INSURANCE GROUP, LTD.**

Date: March 7, 2006

By: /s/ J. BRIAN  
PALMER  
Chief Accounting Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Company and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ STEVEN E. FASS Steven E. Fass	Director, President and CEO (Principal Executive Officer)	March 7, 2006
BRUCE R. BERKOWITZ* Bruce R. Berkowitz	Director	March 7, 2006
JOHN J. BYRNE* John J. Byrne	Director	March 7, 2006
HOWARD L. CLARK, JR.* Howard L. Clark, Jr.	Director	March 7, 2006
ROBERT P. COCHRAN* Robert P. Cochran	Director	March 7, 2006
A. MICHAEL FRINQUELLI* A. Michael Frinquelli	Director	March 7, 2006
/s/ DAVID T. FOY David T. Foy	Executive Vice President and CFO (Principal Financial Officer)	March 7, 2006
GEORGE J. GILLESPIE, III* George J. Gillespie, III	Chairman	March 7, 2006
JOHN D. GILLESPIE* John D. Gillespie	Director	March 7, 2006
EDITH E. HOLIDAY* Edith E. Holiday	Director	March 7, 2006
/s/ J. BRIAN PALMER J. Brian Palmer	Chief Accounting Officer (Principal Accounting Officer)	March 7, 2006
LOWNDES A. SMITH* Lowndes A. Smith	Director	March 7, 2006
ALLAN L. WATERS* Allan L. Waters	Director	March 7, 2006

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\*By: /s/ STEVEN E. FASS  
Steven E. Fass,  
Attorney-in-Fact



**WHITE MOUNTAINS INSURANCE GROUP, LTD.**

**Index to Consolidated Financial Statements and Financial Statement Schedules**

**Consolidated financial statements:**

<u>Consolidated balance sheets at December 31, 2005 and 2004</u>	F-1
<u>Consolidated statements of income and comprehensive income for each of the years ended December 31, 2005, 2004 and 2003</u>	F-2
<u>Consolidated statements of common shareholders' equity for each of the years ended December 31, 2005, 2004 and 2003</u>	F-3
<u>Consolidated statements of cash flows for each of the years ended December 31, 2005, 2004 and 2003</u>	F-4
<u>Notes to consolidated financial statements</u>	F-5

**Other financial information:**

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**Financial statement schedules:**

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III. Supplementary insurance information	FS-4
IV. Reinsurance	FS-5
V. Valuation and qualifying accounts	FS-6
VI. Supplemental information for property and casualty insurance underwriters	FS-7

## CONSOLIDATED BALANCE SHEETS

(dollars in millions, except share amounts)	December 31,	
	2005	2004
<b>Assets</b>		
Fixed maturity investments, at fair value (amortized cost \$7,548.4 and \$7,684.1)	\$ 7,582.7	\$ 7,900.0
Common equity securities, at fair value (cost \$796.5 and \$775.9)	967.8	1,043.9
Short-term investments, at amortized cost (which approximates fair value)	727.8	1,058.2
Other investments (cost \$510.8 and \$442.7)	588.1	527.4
Total investments	9,866.4	10,529.5
Cash	187.7	243.1
Reinsurance recoverable on unpaid losses	3,003.6	2,036.2
Reinsurance recoverable on unpaid losses - Berkshire Hathaway Inc.	2,022.1	1,761.2
Reinsurance recoverable on paid losses	77.0	92.0
Insurance and reinsurance premiums receivable	1,014.3	942.2
Securities lending collateral	674.9	593.3
Funds held by ceding companies	620.4	943.8
Investments in unconsolidated insurance affiliates	479.7	466.6
Deferred tax asset	341.2	271.5
Deferred acquisition costs	288.4	308.2
Ceded unearned premiums	200.7	224.1
Investment income accrued	93.5	102.4
Accounts receivable on unsettled investment sales	21.7	19.9
Other assets	526.5	481.1
Total assets	\$ 19,418.1	\$ 19,015.1
<b>Liabilities</b>		
Loss and loss adjustment expense reserves	\$ 10,231.2	\$ 9,398.5
Reserves for structured contracts	224.6	375.9
Unearned insurance and reinsurance premiums	1,582.0	1,739.4
Debt	779.1	783.3
Securities lending payable	674.9	593.3
Deferred tax liability	274.3	316.3
Ceded reinsurance payable	204.5	201.4
Funds held under reinsurance treaties	171.4	155.4
Accounts payable on unsettled investment purchases	43.4	30.9
Other liabilities	1,165.5	1,324.9
Preferred stock subject to mandatory redemption:		
Held by Berkshire Hathaway Inc. (redemption value \$300.0)	214.0	191.9
Held by others (redemption value \$20.0)	20.0	20.0
Total liabilities	15,584.9	15,131.2
<b>Common shareholders equity</b>		
Common shares at \$1 par value per share – authorized 50,000,000 shares; issued and outstanding 10,779,223 and 10,772,789 shares	10.8	10.8
Paid-in surplus	1,716.4	1,719.2
Retained earnings	1,899.8	1,695.9
Accumulated other comprehensive income, after-tax:		