ARCH CAPITAL GROUP LTD.
Form 10-Q
August 07, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the period ended June 30, 2015

Or

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

Commission file number: 001-26456

ARCH CAPITAL GROUP LTD.
(Exact name of registrant as specified in its charter)

Bermuda
(State or other jurisdiction of incorporation or organization)

Not Applicable
(I.R.S. Employer Identification No.)

Waterloo House, Ground Floor
100 Pitts Bay Road, Pembroke HM 08
(Address of principal executive offices)

(441) 278-9250
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ   No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated Filer þ Accelerated Filer o Non-accelerated Filer o Smaller reporting company o

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

As of July 31, 2015, there were 122,441,665 common shares, $0.0033 par value per share, of the registrant outstanding.

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
Arch Capital Group Ltd.:

We have reviewed the accompanying consolidated balance sheet of Arch Capital Group Ltd. and its subsidiaries (the "Company") as of June 30, 2015, and the related consolidated statements of income and comprehensive income for the three-month and six-month periods ended June 30, 2015 and June 30, 2014, and the consolidated statements of changes in shareholders' equity and cash flows for the six-month periods ended June 30, 2015 and June 30, 2014. These interim financial statements are the responsibility of the Company's management.

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

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

We previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2014, and the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for the year then ended (not presented herein), and in our report dated February 27, 2015, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet information as of December 31, 2014, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP

New York, New York
August 7, 2015

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(U.S. dollars in thousands, except share data)

	(Unaudited) June 30, 2015	December 31, 2014
Assets		
Investments:		
Fixed maturities available for sale, at fair value (amortized cost: $9,945,598 and $10,701,557)	$9,927,603	$10,750,770
Short-term investments available for sale, at fair value (amortized cost: $878,437 and $801,758)	875,727	797,226
Collateral received under securities lending, at fair value (amortized cost: $373,909 and $40,473)	377,897	44,301
Equity securities available for sale, at fair value (cost: $615,055 and $562,534)	701,623	658,182
Other investments available for sale, at fair value (cost: $333,438 and $264,747)	377,677	296,224
Investments accounted for using the fair value option	2,613,487	2,425,053
Investments accounted for using the equity method	472,926	349,014
Total investments	15,346,940	15,320,770
Cash	525,074	485,702
Accrued investment income	80,129	74,316
Securities pledged under securities lending, at fair value (amortized cost: $374,447 and $52,076)	373,969	50,802
Premiums receivable	1,181,636	948,695
Reinsurance recoverable on unpaid and paid losses and loss adjustment expenses	1,831,227	1,812,845
Contractholder receivables	1,393,138	1,309,192
Prepaid reinsurance premiums	442,141	377,078
Deferred acquisition costs, net	448,647	414,525
Receivable for securities sold	454,057	78,170
Goodwill and intangible assets	102,518	109,539
Other assets	905,449	1,024,447
Total assets	$23,084,925	$22,006,081
Liabilities		
Reserve for losses and loss adjustment expenses	$9,082,281	$9,036,448
Unearned premiums	2,442,923	2,231,578
Reinsurance balances payable	252,462	219,312
Contractholder payables	1,393,138	1,309,192
Deposit accounting liabilities	277,523	327,384
Senior notes	791,222	791,141
Revolving credit agreement borrowings	100,000	100,000
Securities lending payable	383,965	50,529
Payable for securities purchased	468,015	128,413
Other liabilities	756,005	693,438
Total liabilities	15,947,534	14,887,435
Commitments and Contingencies		
Redeemable noncontrolling interests	204,996	219,512

Shareholders' Equity		
Non-cumulative preferred shares	325,000	325,000
Common shares ($0.0033 par, shares issued: 172,780,590 and 171,672,408)	576	572
Additional paid-in capital	437,533	383,073
Retained earnings	7,242,728	6,854,571
Accumulated other comprehensive income, net of deferred income tax	66,441	128,856
Common shares held in treasury, at cost (shares: 50,376,681 and 44,304,474)	(1,934,763)	(1,562,019)
Total shareholders' equity available to Arch	6,137,515	6,130,053
Non-redeemable noncontrolling interests	794,880	769,081
Total shareholders' equity	6,932,395	6,899,134
Total liabilities, noncontrolling interests and shareholders' equity	$23,084,925	$22,006,081

See Notes to Consolidated Financial Statements

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(U.S. dollars in thousands, except share data)

	(Unaudited) Three Months Ended June 30,		(Unaudited) Six Months Ended June 30,	
	2015	2014	2015	2014
Revenues				
Net premiums written	$943,580	$971,928	$2,010,575	$2,036,918
Change in unearned premiums	(142)	(64,776)	(156,873)	(269,986)
Net premiums earned	943,438	907,152	1,853,702	1,766,932
Net investment income	86,963	72,990	165,957	139,984
Net realized gains (losses)	(35,725)	54,144	47,623	73,841
Other-than-temporary impairment losses	(1,126)	(14,749)	(8,373)	(17,720)
Less investment impairments recognized in other comprehensive income, before taxes	13	—	1,461	—
Net impairment losses recognized in earnings	(1,113)	(14,749)	(6,912)	(17,720)
Other underwriting income	7,717	2,033	19,253	3,615
Equity in net income of investment funds accounted for using the equity method	16,167	9,240	22,056	12,493
Other income	2,205	4,850	317	2,746
Total revenues	1,019,652	1,035,660	2,101,996	1,981,891
Expenses				
Losses and loss adjustment expenses	519,426	485,518	1,013,142	921,758
Acquisition expenses	175,425	158,158	338,501	318,500
Other operating expenses	168,608	156,350	326,490	302,149
Interest expense	4,011	14,334	16,747	28,738
Net foreign exchange losses (gains)	19,583	2,294	(46,918)	8,857
Total expenses	887,053	816,654	1,647,962	1,580,002
Income before income taxes	132,599	219,006	454,034	401,889
Income tax expense	(6,780)	(7,289)	(19,458)	(11,027)
Net income	$125,819	$211,717	$434,576	$390,862
Amounts attributable to noncontrolling interests	(10,029)	(3,701)	(35,450)	(346)
Net income available to Arch	115,790	208,016	399,126	390,516
Preferred dividends	(5,485)	(5,485)	(10,969)	(10,969)
Net income available to Arch common shareholders	$110,305	$202,531	$388,157	$379,547
Net income per common share				
Basic	$0.91	$1.53	$3.16	$2.87
Diluted	$0.88	$1.48	$3.05	$2.78
Weighted average common shares and common share equivalents outstanding				
Basic	121,719,214	132,650,634	122,957,384	132,256,462
Diluted	125,885,420	136,889,944	127,156,713	136,716,889

See Notes to Consolidated Financial Statements

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(U.S. dollars in thousands)

	(Unaudited) Three Months Ended June 30,		(Unaudited) Six Months Ended June 30,	
	2015	2014	2015	2014
Comprehensive Income				
Net income	$125,819	$211,717	$434,576	$390,862
Other comprehensive income (loss), net of deferred income tax				
Unrealized appreciation (decline) in value of available-for-sale investments:				
Unrealized holding gains (losses) arising during period	(81,935)	108,428	2,369	179,781
Portion of other-than-temporary impairment losses recognized in other comprehensive income, net of deferred income tax	(13)	—	(1,461)	—
Reclassification of net realized gains, net of income taxes, included in net income	(21,214)	(8,285)	(52,146)	(29,534)
Foreign currency translation adjustments	11,580	10,021	(11,177)	8,672
Comprehensive income	34,237	321,881	372,161	549,781
Amounts attributable to noncontrolling interests	(10,029)	(3,701)	(35,450)	(346)
Comprehensive income available to Arch	$24,208	$318,180	$336,711	$549,435

See Notes to Consolidated Financial Statements

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(U.S. dollars in thousands)

	(Unaudited) Six Months Ended June 30, 2015	2014
Non-cumulative preferred shares		
Balance at beginning and end of period	$325,000	$325,000
Common shares		
Balance at beginning of year	572	565
Common shares issued, net	4	5
Balance at end of period	576	570
Additional paid-in capital		
Balance at beginning of year	383,073	299,517
Common shares issued, net	7,378	6,360
Exercise of stock options	9,624	11,233
Amortization of share-based compensation	36,044	35,627
Other	1,414	471
Balance at end of period	437,533	353,208
Retained earnings		
Balance at beginning of year	6,854,571	6,042,154
Net income	434,576	390,862
Amounts attributable to noncontrolling interests	(35,450)	(346)
Preferred share dividends	(10,969)	(10,969)
Balance at end of period	7,242,728	6,421,701
Accumulated other comprehensive income		
Balance at beginning of year	128,856	74,964
Unrealized appreciation in value of available-for-sale investments, net of deferred income tax:		
Balance at beginning of year	161,598	80,692
Unrealized holding (losses) gains arising during period, net of reclassification adjustment	(49,777)	150,247
Portion of other-than-temporary impairment losses recognized in other comprehensive income, net of deferred income tax	(1,461)	—
Balance at end of period	110,360	230,939
Foreign currency translation adjustments:		
Balance at beginning of year	(32,742)	(5,728)
Foreign currency translation adjustments	(11,177)	8,672
Balance at end of period	(43,919)	2,944
Balance at end of period	66,441	233,883
Common shares held in treasury, at cost		
Balance at beginning of year	(1,562,019)	(1,094,704)
Shares repurchased for treasury	(372,744)	(10,259)

Balance at end of period	(1,934,763)	(1,104,963)
Total shareholders' equity available to Arch	6,137,515	6,229,399
Non-redeemable noncontrolling interests	794,880	792,340
Total shareholders' equity	$6,932,395	$7,021,739

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(U.S. dollars in thousands)

	(Unaudited) Six Months Ended June 30,	
	2015	2014
Operating Activities		
Net income	$434,576	$390,862
Adjustments to reconcile net income to net cash provided by operating activities:		
Net realized gains	(60,818)	(87,520)
Net impairment losses recognized in earnings	6,912	17,720
Equity in net income or loss of investment funds accounted for using the equity method and other income or loss	(10,349)	(135)
Share-based compensation	36,044	35,627
Changes in:		
Reserve for losses and loss adjustment expenses, net of unpaid losses and loss adjustment expenses recoverable	91,616	60,474
Unearned premiums, net of prepaid reinsurance premiums	156,873	269,986
Premiums receivable	(206,642)	(325,953)
Deferred acquisition costs, net	(39,009)	(55,822)
Reinsurance balances payable	19,657	65,803
Other liabilities	(94,841)	43,133
Other items	51,180	38,888
Net Cash Provided By Operating Activities	385,199	453,063
Investing Activities		
Purchases of fixed maturity investments	(14,641,391)	(14,311,748)
Purchases of equity securities	(288,535)	(174,687)
Purchases of other investments	(1,273,780)	(1,022,987)
Proceeds from sales of fixed maturity investments	14,355,519	13,204,854
Proceeds from sales of equity securities	272,343	98,687
Proceeds from sales, redemptions and maturities of other investments	1,078,675	618,707
Proceeds from redemptions and maturities of fixed maturity investments	474,984	432,040
Proceeds from investment in joint venture	40,000	—
Net sales of short-term investments	3,707	430,304
Change in cash collateral related to securities lending	(18,329)	18,701
Purchase of business, net of cash acquired	818	(235,578)
Purchases of furniture, equipment and other assets	(43,165)	(10,360)
Net Cash Used For Investing Activities	(39,154)	(952,067)
Financing Activities		
Purchases of common shares under share repurchase program	(361,877)	—
Proceeds from common shares issued, net	2,178	2,521
Change in cash collateral related to securities lending	18,329	(18,701)
Third party investment in non-redeemable noncontrolling interests	—	796,903
Third party investment in redeemable noncontrolling interests	—	219,233
Dividends paid to redeemable noncontrolling interests	(9,313)	(4,816)
Other	55,018	4,706

Preferred dividends paid	(10,969)	(10,969)
Net Cash Provided By (Used For) Financing Activities	(306,634)	988,877
Effects of exchange rate changes on foreign currency cash	(39)	2,513
Increase in cash	39,372	492,386
Cash beginning of year	485,702	434,057
Cash end of period	$525,074	$926,443
Income taxes paid	$25,992	$8,279
Interest paid	$25,076	$21,696

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. General

Arch Capital Group Ltd. (“ACGL”) is a Bermuda public limited liability company which provides insurance and reinsurance on a worldwide basis through its subsidiaries (together with ACGL, the “Company”). The Company’s consolidated financial statements include the results of Watford Holdings Ltd., the parent of Watford Re Ltd. (see Note 3).

The interim consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”). All significant intercompany transactions and balances have been eliminated in consolidation. 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 and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and assumptions. In the opinion of management, the accompanying unaudited interim consolidated financial statements reflect all adjustments (consisting of normally recurring accruals) necessary for a fair statement of results on an interim basis. The results of any interim period are not necessarily indicative of the results for a full year or any future periods.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted; however, management believes that the disclosures are adequate to make the information presented not misleading. This report should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2014 (“2014 Form 10-K”), including the Company’s audited consolidated financial statements and related notes.

The Company has reclassified the presentation of certain prior year information to conform to the current presentation. Such reclassifications had no effect on the Company’s net income, comprehensive income, shareholders’ equity or cash flows. Tabular amounts are in U.S. Dollars in thousands, except share amounts, unless otherwise noted.

Acquisition of Gulf Reinsurance Limited

In May 2008, the Company provided $100.0 million of funding to Gulf Reinsurance Limited, a wholly owned subsidiary of Gulf Re Holdings Limited (collectively, “Gulf Re”), pursuant to the joint venture agreement with Gulf Investment Corporation GSC (“GIC”). Under the agreement, Arch Re Bermuda and GIC each owned 50% of Gulf Re. The Company entered into a number of strategic initiatives related to Gulf Re in the 2014 fourth quarter, including an agreement to acquire complete ownership and effective control of Gulf Re. Such agreement was approved by the Dubai Financial Services Authority in April 2015 and the transaction closed on May 14, 2015. Pursuant to the agreement, Gulf Re distributed $130.6 million in total to the Company and GIC, and Gulf Re maintained $50.7 million of equity capital. The Company purchased GIC’s remaining investment in Gulf Re for $25.6 million through a transfer of fixed maturity investments. GIC will continue to participate equally with the Company in the financial results of Gulf Re and have the ability to purchase shares in Gulf Re over the next seven years. The acquisition resulted in no goodwill or other intangible assets as the fair value of Gulf Re was equal to its book value at closing.

2. Recent Accounting Pronouncements

Recently Issued Accounting Standards Adopted

The Company adopted accounting guidance in the 2015 second quarter which changes the accounting for repurchase and resale-to-maturity agreements by requiring that such agreements be recognized as financing arrangements, and requires that a transfer of a financial asset and a repurchase agreement entered into contemporaneously be accounted for separately. The new accounting guidance also requires additional disclosures about certain transferred financial assets accounted for as sales and certain securities lending transactions. Disclosures are not required to be presented for comparative periods before the effective date. See Note 6, “Investment Information—Securities Lending Agreements.”

The Company adopted accounting guidance in the 2015 second quarter which relates to the presentation of debt issuance costs. Such guidance requires presentation of debt issuance costs in the balance sheet as a deduction from the carrying amount of the related debt liability instead of a deferred charge. The Company previously included its debt issuance costs within ‘other assets.’ The guidance was applied retrospectively and resulted in reductions in ‘other assets’ and ‘senior notes’ at June 30, 2015 of $8.8 million, respectively, and $8.9 million at December 31, 2014, respectively. The adoption of this change in accounting principle did not impact the Company's shareholders' equity or net income.

The Company adopted accounting guidance pertaining to the categorization within the fair value hierarchy of certain investments measured at fair value using the net asset value per share as a practical expedient. These investments are no longer required to be categorized within the fair value hierarchy but are still required to be reported in the fair value hierarchy table to permit reconciliation back to the consolidated balance sheet. Additionally, certain disclosures are no longer applicable for investments that are eligible to be measured using the practical expedient, but for which the practical expedient was not elected. The guidance was applied retrospectively and only impacted the Company's disclosures. See Note 7, "Fair Value."

Recently Issued Accounting Standards Not Yet Adopted

An accounting standard was issued in the 2014 second quarter which will change the manner in which most companies recognize revenue. The standard requires that revenue reflect the transfer of goods or services to customers based on the consideration or payment the company expects to be entitled to in exchange for those goods or services; however, the standard does not change the accounting for insurance contracts or financial instruments. The new standard also requires enhanced disclosures about revenue. This accounting guidance is effective in the 2018 first quarter and may be applied on a full retrospective or modified retrospective approach. The Company is assessing the impact the implementation of this standard will have on its consolidated financial statements.

An accounting standard was issued in the 2015 first quarter providing targeted improvements to consolidation guidance for limited partnerships and other similarly structured entities. The new standard addresses instances where a reporting entity consolidates another entity when the reporting entity is simply acting on the behalf of others, amongst other related issues. While the standard is targeted, the application is relevant for all companies that are required to assess whether or not to consolidate certain entities. The standard is effective in the 2016 first quarter and early adoption is permitted. The Company is assessing the impact the implementation of this standard will have on its consolidated financial statements.

A new accounting standard was issued in the 2015 second quarter requiring new disclosures about the reserve for losses and loss adjustment expenses for short-duration insurance contracts. These disclosures will provide additional insight into an insurance entity's ability to underwrite and anticipate costs associated with claims. This accounting guidance is effective for the 2016 annual reporting period and interim periods thereafter and should be applied retrospectively. The Company is assessing the impact the implementation of this standard will have on its consolidated financial statements.

3. Variable Interest Entity and Noncontrolling Interests

Variable interest entity

On March 20, 2014, the Company invested $100.0 million and acquired approximately 11% of Watford Holdings Ltd.'s common equity and a warrant to purchase additional common equity. Watford Holdings Ltd. is the parent of Watford Re Ltd., a multi-line Bermuda reinsurance company (together with Watford Holdings Ltd., "Watford Re"). Watford Re is considered a variable interest entity ("VIE") and the Company concluded that it is the primary beneficiary of Watford Re. As such, the results of Watford Re are included in the Company's consolidated financial statements.

The Company concluded that Watford Re represents a separate operating segment and provides the income statement and total investable assets, total assets and total liabilities of Watford Re within Note 5. At June 30, 2015, Watford Re’s liabilities included unearned premiums of $247.6 million and reserves for losses and loss adjustment expenses of $173.2 million, some of which is related to transactions with the Company. For the six months ended June 30, 2015, Watford Re generated $137.8 million of cash provided by operating activities and $40.3 million of cash provided by financing activities, partially offset by $134.9 million of cash used for investing activities.

Because Watford Re is an independent company, the assets of Watford Re can be used only to settle obligations of Watford Re and Watford Re is solely responsible for its own liabilities and commitments. The Company’s financial exposure to Watford Re is limited to its investment in Watford Re’s common shares and counterparty credit risk (mitigated by collateral) arising from the reinsurance transactions.

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Non-redeemable noncontrolling interests

The Company accounts for the portion of Watford Re's common equity attributable to third party investors in the shareholders' equity section of its consolidated balance sheets. The noncontrolling ownership in Watford Re's common shares was approximately 89% at June 30, 2015. The portion of Watford Re's income or loss attributable to third party investors is recorded in the consolidated statements of income in 'amounts attributable to noncontrolling interests.' The following table sets forth activity in the non-redeemable noncontrolling interests:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Balance, beginning of period	$789,594	$793,496	$769,081	$—
Sale of shares to noncontrolling interests	—	—	—	796,903
Amounts attributable to noncontrolling interests	5,286	(1,156)	25,799	(4,563)
Balance, end of period	$794,880	$792,340	$794,880	$792,340

Redeemable noncontrolling interests

The Company accounts for redeemable noncontrolling interests in the mezzanine section of its consolidated balance sheets in accordance with applicable accounting guidance. Such redeemable noncontrolling interests relate to the 9,065,200 cumulative redeemable preference shares ("Watford Preference Shares") issued in late March 2014 with a par value of $0.01 per share and a liquidation preference of $25.00 per share. Preferred dividends, including the accretion of the discount and issuance costs, are included in 'amounts attributable to noncontrolling interests' in the Company's consolidated statements of income. The following table sets forth activity in the redeemable non-controlling interests:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Balance, beginning of period	$219,604	$219,234	$219,512	$—
Sale of shares to noncontrolling interests	—	—	—	219,233
Shares acquired by the Company (1)	(14,700)	—	(14,700)	—
Accretion of preference share issuance costs	92	92	184	93
Balance, end of period	$204,996	$219,326	$204,996	$219,326

(1) During the 2015 second quarter, the Company acquired Gulf Re, which owns 600,000 Watford Preference Shares. Such shares, net of a discount, along with related dividends and accretion of the discount, are eliminated in consolidation.

The portion of Watford Re's income or loss attributable to third party investors is recorded in the consolidated statements of income in 'amounts attributable to noncontrolling interests' as summarized in the table below:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Amounts attributable to non-redeemable noncontrolling interests	$(5,286)	$1,156	$(25,799)	$4,563
Dividends attributable to redeemable noncontrolling interests	(4,743)	(4,857)	(9,651)	(4,909)
Amounts attributable to noncontrolling interests	$(10,029)	$(3,701)	$(35,450)	$(346)

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4. Earnings Per Common Share

The following table sets forth the computation of basic and diluted earnings per common share:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Numerator:				
Net income	$125,819	$211,717	$434,576	$390,862
Amounts attributable to noncontrolling interests	(10,029)	(3,701)	(35,450)	(346)
Net income available to Arch	115,790	208,016	399,126	390,516
Preferred dividends	(5,485)	(5,485)	(10,969)	(10,969)
Net income available to Arch common shareholders	$110,305	$202,531	$388,157	$379,547
Denominator:				
Weighted average common shares outstanding — basic	121,719,214	132,650,634	122,957,384	132,256,462
Effect of dilutive common share equivalents:				
Nonvested restricted shares	1,258,741	1,144,621	1,334,633	1,236,408
Stock options (1)	2,907,465	3,094,689	2,864,696	3,224,019
Weighted average common shares and common share equivalents outstanding — diluted	125,885,420	136,889,944	127,156,713	136,716,889
Earnings per common share:				
Basic	$0.91	$1.53	$3.16	$2.87
Diluted	$0.88	$1.48	$3.05	$2.78

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(1) Certain stock options were not included in the computation of diluted earnings per share where the exercise price of the stock options exceeded the average market price and would have been anti-dilutive or where, when applying the treasury stock method to in-the-money options, the sum of the proceeds, including unrecognized compensation, exceeded the average market price and would have been anti-dilutive. For the 2015 second quarter and 2014 second quarter, the number of stock options excluded were 1,009,113 and 978,237, respectively. For the six months ended June 30, 2015 and 2014, the number of stock options excluded were 1,187,162 and 1,318,662, respectively.

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5. Segment Information

The Company classifies its businesses into three underwriting segments — insurance, reinsurance and mortgage — and two other operating segments — ‘other’ and corporate (non-underwriting). The Company determined its reportable segments using the management approach described in accounting guidance regarding disclosures about segments of an enterprise and related information. The accounting policies of the segments are the same as those used for the preparation of the Company’s consolidated financial statements. Intersegment business is allocated to the segment accountable for the underwriting results.

The Company’s insurance, reinsurance and mortgage segments each have managers who are responsible for the overall profitability of their respective segments and who are directly accountable to the Company’s chief operating decision makers, the Chairman, President and Chief Executive Officer of ACGL and the Chief Financial Officer of ACGL. The chief operating decision makers do not assess performance, measure return on equity or make resource allocation decisions on a line of business basis. Management measures segment performance for its three underwriting segments based on underwriting income or loss. The Company does not manage its assets by underwriting segment, with the exception of goodwill and intangible assets, and, accordingly, investment income is not allocated to each underwriting segment.

The insurance segment consists of the Company’s insurance underwriting units which offer specialty product lines on a worldwide basis. Product lines include: construction and national accounts; excess and surplus casualty; lenders products; professional lines; programs; property, energy, marine and aviation; travel, accident and health; and other (consisting of alternative markets, excess workers' compensation and surety business).

The reinsurance segment consists of the Company’s reinsurance underwriting units which offer specialty product lines on a worldwide basis. Product lines include: casualty; marine and aviation; other specialty; property catastrophe; property excluding property catastrophe (losses on a single risk, both excess of loss and pro rata); and other (consisting of life reinsurance, casualty clash and other).

The mortgage segment consists of the Company’s mortgage insurance and reinsurance business and includes the results of Arch Mortgage Insurance Company (“Arch MI U.S.”). Arch MI U.S. is approved as an eligible mortgage insurer by Federal National Mortgage Association (“Fannie Mae”) and Federal Home Loan Mortgage Corporation (“Freddie Mac”), each a government sponsored enterprise, or “GSE.” Arch MI U.S. provides mortgage insurance to banks, credit unions and other lenders nationwide. The mortgage segment also provides reinsurance on a global basis, direct mortgage insurance in Europe and various risk-sharing products to government agencies and mortgage lenders.

The corporate (non-underwriting) segment results include net investment income, other income (loss), other expenses incurred by the Company, interest expense, net realized gains or losses, net impairment losses included in earnings, equity in net income or loss of investment funds accounted for using the equity method, net foreign exchange gains or losses, income taxes and items related to the Company’s non-cumulative preferred shares. Such amounts exclude the results of the ‘other’ segment.

The ‘other’ segment includes the results of Watford Re (see Note 3). Watford Re has its own management and board of directors that is responsible for the overall profitability of the ‘other’ segment. For the ‘other’ segment, performance is measured based on net income or loss.

The following tables summarize the Company's underwriting income or loss by segment, together with a reconciliation of underwriting income or loss to net income available to common shareholders:

	Three Months Ended June 30, 2015					
	Insurance	Reinsurance	Mortgage	Sub-Total	Other	Total
Gross premiums written (1)	$744,810	$342,101	$68,572	$1,155,253	$127,954	$1,199,209
Premiums ceded	(235,743)	(89,446)	(6,902)	(331,861)	(7,766)	(255,629)
Net premiums written	509,067	252,655	61,670	823,392	120,188	943,580
Change in unearned premiums	758	21,310	(9,211)	12,857	(12,999)	(142)
Net premiums earned	509,825	273,965	52,459	836,249	107,189	943,438
Other underwriting income	521	2,658	3,686	6,865	852	7,717
Losses and loss adjustment expenses	(320,926)	(111,183)	(9,639)	(441,748)	(77,678)	(519,426)
Acquisition expenses, net	(76,723)	(58,360)	(10,200)	(145,283)	(30,142)	(175,425)
Other operating expenses	(89,054)	(39,007)	(19,679)	(147,740)	(3,450)	(151,190)
Underwriting income (loss)	$23,643	$68,073	$16,627	108,343	(3,229)	105,114
Net investment income				67,171	19,792	86,963
Net realized gains (losses)				(26,860)	(8,865)	(35,725)
Net impairment losses recognized in earnings				(1,113)	—	(1,113)
Equity in net income of investment funds accounted for using the equity method				16,167	—	16,167
Other income (loss)				2,205	—	2,205
Other expenses				(17,418)	—	(17,418)
Interest expense				(4,011)	—	(4,011)
Net foreign exchange gains (losses)				(22,571)	2,988	(19,583)
Income (loss) before income taxes				121,913	10,686	132,599
Income tax expense				(6,780)	—	(6,780)
Net income (loss)				115,133	10,686	125,819
Dividends attributable to redeemable noncontrolling interests				—	(4,743)	(4,743)
Amounts attributable to noncontrolling interests				—	(5,286)	(5,286)
Net income (loss) available to Arch				115,133	657	115,790
Preferred dividends				(5,485)	—	(5,485)
Net income (loss) available to Arch common shareholders				$109,648	$657	$110,305

Underwriting Ratios

Loss ratio	62.9 %	40.6 %	18.4 %	52.8 %	72.5 %	55.1 %
Acquisition expense ratio	15.0 %	21.3 %	19.4 %	17.4 %	28.1 %	18.6 %
Other operating expense ratio	17.5 %	14.2 %	37.5 %	17.7 %	3.2 %	16.0 %
Combined ratio	95.4 %	76.1 %	75.3 %	87.9 %	103.8 %	89.7 %
Goodwill and intangible assets	$30,968	$2,420	$69,130	$102,518	$—	$102,518
Total investable assets				$14,513,554	$1,340,574	$15,854,128
Total assets				21,323,611	1,761,314	23,084,925
Total liabilities				15,299,256	648,278	15,947,534

(1) Certain amounts included in the gross premiums written of each segment are related to intersegment transactions. Accordingly, the sum of gross premiums written for each segment does not agree to the total gross premiums written as shown in the table above due to the elimination of intersegment transactions in the total.

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	Three Months Ended June 30, 2014					
	Insurance	Reinsurance	Mortgage	Sub-Total	Other	Total
Gross premiums written (1)	$852,231	$349,841	$55,476	$1,256,934	$54,562	$1,271,761
Premiums ceded	(273,349)	(58,994)	(5,079)	(336,808)	(2,760)	(299,833)
Net premiums written	578,882	290,847	50,397	920,126	51,802	971,928
Change in unearned premiums	(71,170)	44,780	436	(25,954)	(38,822)	(64,776)
Net premiums earned	507,712	335,627	50,833	894,172	12,980	907,152
Other underwriting income	514	303	1,216	2,033	—	2,033
Losses and loss adjustment expenses	(311,526)	(150,325)	(15,473)	(477,324)	(8,194)	(485,518)
Acquisition expenses, net	(76,449)	(66,035)	(11,481)	(153,965)	(4,193)	(158,158)
Other operating expenses	(85,829)	(37,666)	(16,288)	(139,783)	(1,635)	(141,418)
Underwriting income (loss)	$34,422	$81,904	$8,807	125,133	(1,042)	124,091
Net investment income				72,458	532	72,990
Net realized gains (losses)				50,966	3,178	54,144
Net impairment losses recognized in earnings				(14,749)	—	(14,749)
Equity in net income of investment funds accounted for using the equity method				9,240	—	9,240
Other income (loss)				4,850	—	4,850
Other expenses				(15,279)	347	(14,932)
Interest expense				(14,334)	—	(14,334)
Net foreign exchange gains (losses)				(2,764)	470	(2,294)
Income (loss) before income taxes				215,521	3,485	219,006
Income tax expense				(7,289)	—	(7,289)
Net income (loss)				208,232	3,485	211,717
Dividends attributable to redeemable noncontrolling interests				—	(4,857)	(4,857)
Amounts attributable to noncontrolling interests				—	1,156	1,156
Net income (loss) available to Arch				208,232	(216)	208,016
Preferred dividends				(5,485)	—	(5,485)
Net income (loss) available to Arch common shareholders				$202,747	$(216)	$202,531
Underwriting Ratios						
Loss ratio	61.4%	44.8%	30.4%	53.4%	63.1%	53.5%
Acquisition expense ratio	15.1%	19.7%	22.6%	17.2%	32.3%	17.4%
Other operating expense ratio	16.9%	11.2%	32.0%	15.6%	12.6%	15.6%

Combined ratio	93.4 %	75.7 %	85.0 %	86.2 %	108.0 %	86.5 %
Goodwill and intangible assets	$24,498	$4,942	$89,281	$118,721	$—	$118,721
Total investable assets				$14,688,808	$1,114,719	$15,803,527
Total assets				21,204,129	1,363,318	22,567,447
Total liabilities				15,072,875	253,507	15,326,382

(1) Certain amounts included in the gross premiums written of each segment are related to intersegment transactions. Accordingly, the sum of gross premiums written for each segment does not agree to the total gross premiums written as shown in the table above due to the elimination of intersegment transactions in the total.

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
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	Six Months Ended June 30, 2015					
	Insurance	Reinsurance	Mortgage	Sub-Total	Other	Total
Gross premiums written (1)	$1,510,963	$827,213	$129,113	$2,466,931	$256,587	$2,541,231
Premiums ceded	(459,893)	(226,015)	(15,572)	(701,122)	(11,821)	(530,656)
Net premiums written	1,051,070	601,198	113,541	1,765,809	244,766	2,010,575
Change in unearned premiums	(33,331)	(47,516)	(10,715)	(91,562)	(65,311)	(156,873)
Net premiums earned	1,017,739	553,682	102,826	1,674,247	179,455	1,853,702
Other underwriting income	948	4,087	11,404	16,439	2,814	19,253
Losses and loss adjustment expenses	(638,822)	(223,715)	(23,448)	(885,985)	(127,157)	(1,013,142)
Acquisition expenses, net	(151,801)	(114,964)	(20,618)	(287,383)	(51,118)	(338,501)
Other operating expenses	(177,173)	(77,051)	(40,048)	(294,272)	(5,455)	(299,727)
Underwriting income (loss)	$50,891	$142,039	$30,116	223,046	(1,461)	221,585
Net investment income				137,459	28,498	165,957
Net realized gains (losses)				38,649	8,974	47,623
Net impairment losses recognized in earnings				(6,912)	—	(6,912)
Equity in net income of investment funds accounted for using the equity method				22,056	—	22,056
Other income (loss)				317	—	317
Other expenses				(26,763)	—	(26,763)
Interest expense				(16,747)	—	(16,747)
Net foreign exchange gains (losses)				44,282	2,636	46,918
Income (loss) before income taxes				415,387	38,647	454,034
Income tax expense				(19,458)	—	(19,458)
Net income (loss)				395,929	38,647	434,576
Dividends attributable to redeemable noncontrolling interests				—	(9,651)	(9,651)
Amounts attributable to noncontrolling interests				—	(25,799)	(25,799)
Net income (loss) available to Arch				395,929	3,197	399,126
Preferred dividends				(10,969)	—	(10,969)
Net income (loss) available to Arch common shareholders				$384,960	$3,197	$388,157
Underwriting Ratios						
Loss ratio	62.8%	40.4%	22.8%	52.9%	70.9%	54.7%
Acquisition expense ratio	14.9%	20.8%	20.1%	17.2%	28.5%	18.3%
Other operating expense ratio	17.4%	13.9%	38.9%	17.6%	3.0%	16.2%

Combined ratio	95.1	%	75.1	%	81.8	%	87.7	%	102.4	%	89.2	%

(1) Certain amounts included in the gross premiums written of each segment are related to intersegment transactions. Accordingly, the sum of gross premiums written for each segment does not agree to the total gross premiums written as shown in the table above due to the elimination of intersegment transactions in the total.

ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
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	Six Months Ended June 30, 2014					
	Insurance	Reinsurance	Mortgage	Sub-Total	Other	Total
Gross premiums written (1)	$1,582,877	$866,894	$103,383	$2,552,070	$86,756	$2,566,897
Premiums ceded	(458,393)	(132,121)	(9,718)	(599,148)	(2,760)	(529,979)
Net premiums written	1,124,484	734,773	93,665	1,952,922	83,996	2,036,918
Change in unearned premiums	(139,271)	(57,798)	(4,067)	(201,136)	(68,850)	(269,986)
Net premiums earned	985,213	676,975	89,598	1,751,786	15,146	1,766,932
Other underwriting income	1,014	619	1,982	3,615	—	3,615
Losses and loss adjustment expenses	(598,296)	(289,961)	(23,951)	(912,208)	(9,550)	(921,758)
Acquisition expenses, net	(153,381)	(139,468)	(20,635)	(313,484)	(5,016)	(318,500)
Other operating expenses	(166,973)	(73,861)	(30,164)	(270,998)	(2,744)	(273,742)
Underwriting income (loss)	$67,577	$174,304	$16,830	258,711	(2,164)	256,547
Net investment income				139,451	533	139,984
Net realized gains (losses)				70,663	3,178	73,841
Net impairment losses recognized in earnings				(17,720)	—	(17,720)
Equity in net income of investment funds accounted for using the equity method				12,493	—	12,493
Other income (loss)				2,746	—	2,746
Other expenses				(26,078)	(2,329)	(28,407)
Interest expense				(28,738)	—	(28,738)
Net foreign exchange gains (losses)				(9,420)	563	(8,857)
Income (loss) before income taxes				402,108	(219)	401,889
Income tax expense				(11,027)	—	(11,027)
Net income (loss)				391,081	(219)	390,862
Dividends attributable to redeemable noncontrolling interests				—	(4,909)	(4,909)
Amounts attributable to noncontrolling interests				—	4,563	4,563
Net income (loss) available to Arch				391,081	(565)	390,516
Preferred dividends				(10,969)	—	(10,969)
Net income (loss) available to Arch common shareholders				$380,112	$(565)	$379,547
Underwriting Ratios						
Loss ratio	60.7%	42.8%	26.7%	52.1%	63.1%	52.2%
Acquisition expense ratio	15.6%	20.6%	23.0%	17.9%	33.1%	18.0%
Other operating expense ratio	16.9%	10.9%	33.7%	15.5%	18.1%	15.5%

Combined ratio	93.2	%	74.3	%	83.4	%	85.5	%	114.3	%	85.7	%

(1) Certain amounts included in the gross premiums written of each segment are related to intersegment transactions. Accordingly, the sum of gross premiums written for each segment does not agree to the total gross premiums written as shown in the table above due to the elimination of intersegment transactions in the total.

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ARCH CAPITAL GROUP LTD. AND SUBSIDIARIES
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6. Investment Information

At June 30, 2015, total investable assets of $15.85 billion included $14.51 billion managed by the Company and $1.34 billion attributable to Watford Re.

Available For Sale Investments

The following table summarizes the fair value and cost or amortized cost of the Company's investments classified as available for sale:

	Estimated Fair Value	Gross Unrealized Gains	Gross Unrealized Losses	Cost or Amortized Cost	OTTI Unrealized Losses (2)
June 30, 2015					
Fixed maturities (1):					
Corporate bonds	$2,833,849	$26,401	$(51,717)	$2,859,165	$(681)
Mortgage backed securities	837,680	12,315	(4,231)	829,596	(3,564)
Municipal bonds	1,760,384	19,601	(9,004)	1,749,787	—
Commercial mortgage backed securities	832,159	6,760	(4,922)	830,321	—
U.S. government and government agencies	1,899,868	8,463	(3,720)	1,895,125	—
Non-U.S. government securities	786,276	10,343	(32,720)	808,653	—
Asset backed securities	1,351,356	7,324	(3,364)	1,347,396	(22)
Total	10,301,572	91,207	(109,678)	10,320,043	(4,267)
Equity securities	701,623	105,174	(18,606)	615,055	—
Other investments	377,677	46,166	(1,927)	333,438	—
Short-term investments	875,727	55	(2,767)	878,439	—
Total	$12,256,599	$242,602	$(132,978)	$12,146,975	$(4,267)
December 31, 2014					
Fixed maturities (1):					
Corporate bonds	$3,108,513	$37,928	$(38,974)	$3,109,559	$(317)
Mortgage backed securities	943,343	18,843	(3,842)	928,342	(3,307)
Municipal bonds	1,494,122	31,227	(1,044)	1,463,939	—
Commercial mortgage backed securities	1,114,528	14,594	(3,822)	1,103,756	—
U.S. government and government agencies	1,447,972	8,345	(1,760)	1,441,387	—
Non-U.S. government securities	1,015,153	21,311	(37,203)	1,031,045	—
Asset backed securities	1,677,941	8,425	(6,089)	1,675,605	(22)
Total	10,801,572	140,673	(92,734)	10,753,633	(3,646)
Equity securities	658,182	109,012	(13,364)	562,534	—
Other investments	296,224	31,839	(362)	264,747	—
Short-term investments	797,226	738	(5,270)	801,758	—
Total	$12,553,204	$282,262	$(111,730)	$12,382,672	$(3,646)

(1)

In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See "—Securities Lending Agreements."

(2) Represents the total other-than-temporary impairments ("OTTI") recognized in accumulated other comprehensive income ("AOCI"). It does not include the change in fair value subsequent to the impairment measurement date. At June 30, 2015, the net unrealized gain related to securities for which a non-credit OTTI was recognized in AOCI was \$0.3 million, compared to a net unrealized gain of \$0.9 million at December 31, 2014.

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The following table summarizes, for all available for sale securities in an unrealized loss position, the fair value and gross unrealized loss by length of time the security has been in a continual unrealized loss position:

	Less than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
June 30, 2015						
Fixed maturities (1):						
Corporate bonds	$1,659,276	$(40,616)	$92,244	$(11,101)	$1,751,520	$(51,717)
Mortgage backed securities	437,043	(3,574)	45,082	(657)	482,125	(4,231)
Municipal bonds	784,691	(8,562)	3,530	(442)	788,221	(9,004)
Commercial mortgage backed securities	374,338	(4,912)	2,893	(10)	377,231	(4,922)
U.S. government and government agencies	426,224	(3,720)	—	—	426,224	(3,720)
Non-U.S. government securities	431,360	(16,841)	77,314	(15,879)	508,674	(32,720)
Asset backed securities	281,650	(2,161)	130,987	(1,203)	412,637	(3,364)
Total	4,394,582	(80,386)	352,050	(29,292)	4,746,632	(109,678)
Equity securities	286,325	(18,606)	—	—	286,325	(18,606)
Other investments	89,863	(1,927)	—	—	89,863	(1,927)
Short-term investments	60,287	(2,767)	—	—	60,287	(2,767)
Total	$4,831,057	$(103,686)	$352,050	$(29,292)	$5,183,107	$(132,978)
December 31, 2014						
Fixed maturities (1):						
Corporate bonds	$1,309,637	$(32,903)	$148,963	$(6,071)	$1,458,600	$(38,974)
Mortgage backed securities	293,624	(1,476)	59,107	(2,366)	352,731	(3,842)
Municipal bonds	210,614	(588)	13,643	(456)	224,257	(1,044)
Commercial mortgage backed securities	232,147	(770)	125,894	(3,052)	358,041	(3,822)
U.S. government and government agencies	618,381	(1,626)	3,438	(134)	621,819	(1,760)
Non-U.S. government securities	510,766	(31,172)	46,910	(6,031)	557,676	(37,203)
Asset backed securities	612,950	(2,486)	243,452	(3,603)	856,402	(6,089)
Total	3,788,119	(71,021)	641,407	(21,713)	4,429,526	(92,734)
Equity securities	181,002	(13,364)	—	—	181,002	(13,364)
Other investments	59,638	(362)	—	—	59,638	(362)
Short-term investments	79,271	(5,270)	—	—	79,271	(5,270)
Total	$4,108,030	$(90,017)	$641,407	$(21,713)	$4,749,437	$(111,730)

(1) In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See “—Securities Lending

Agreements.”

At June 30, 2015, on a lot level basis, approximately 2,620 security lots out of a total of approximately 5,580 security lots were in an unrealized loss position and the largest single unrealized loss from a single lot in the Company’s fixed maturity portfolio was $2.9 million. At December 31, 2014, on a lot level basis, approximately 1,900 security lots out of a total of approximately 4,790 security lots were in an unrealized loss position and the largest single unrealized loss from a single lot in the Company’s fixed maturity portfolio was $2.9 million.

The contractual maturities of the Company's fixed maturities are shown in the following table. Expected maturities, which are management's best estimates, will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	June 30, 2015		December 31, 2014	
Maturity	Estimated Fair Value	Amortized Cost	Estimated Fair Value	Amortized Cost
Due in one year or less	$369,356	$374,710	$235,930	$233,794
Due after one year through five years	4,101,484	4,106,002	4,074,562	4,077,408
Due after five years through 10 years	2,468,013	2,487,840	2,475,726	2,461,356
Due after 10 years	341,524	344,178	279,542	273,372
	7,280,377	7,312,730	7,065,760	7,045,930
Mortgage backed securities	837,680	829,596	943,343	928,342
Commercial mortgage backed securities	832,159	830,321	1,114,528	1,103,756
Asset backed securities	1,351,356	1,347,396	1,677,941	1,675,605
Total (1)	$10,301,572	$10,320,043	$10,801,572	$10,753,633

(1) In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See "—Securities Lending Agreements."

Securities Lending Agreements

From time to time, the Company enters into securities lending agreements with financial institutions to enhance investment income. The Company loans certain of its securities to third parties, primarily major brokerage firms, for short periods of time through a lending agent. The Company maintains legal control over the securities it lends, retains the earnings and cash flows associated with the loaned securities and receives a fee from the borrower for the temporary use of the securities. An indemnification agreement with the lending agent protects the Company in the event a borrower becomes insolvent or fails to return any of the securities on loan to the Company.

The Company receives collateral in the form of cash or securities. Cash collateral primarily consists of short-term investments. At June 30, 2015, the fair value of the cash collateral received on securities lending was $62.6 million, which included $5.7 million that was reinvested in sub-prime mortgage backed securities, and the fair value of security collateral received was $315.1 million. At December 31, 2014, the fair value of the cash collateral received on securities lending was $44.3 million, which included $5.8 million that was reinvested in sub-prime mortgage backed securities, and the fair value of security collateral received was nil.

The Company's securities lending transactions were accounted for as secured borrowings with significant investment categories as follows:

	June 30, 2015				
	Remaining Contractual Maturity of the Agreements				
Securities Lending Transactions	Overnight and Continuous	Less than 30 Days	30-90 Days	90 Days or More	Total
U.S. government and government agencies	$335,233	$—	$—	$—	$335,233
Corporate bonds	44,139	—	—	—	44,139

Equity securities	4,593	—	—	—	4,593
Total	$383,965	$—	$—	$—	$383,965
Gross amount of recognized liabilities for securities lending in offsetting disclosure in Note 8					$—
Amounts related to securities lending not included in offsetting disclosure in Note 8					$383,965

Other Investments

The following table summarizes the Company’s other investments, including available for sale and fair value option components:

	June 30, 2015	December 31, 2014
Available for sale:		
Asian and emerging markets	$287,666	$ 236,586
Investment grade fixed income	58,829	59,638
Credit related funds	13,773	—
Other	17,409	—
Total available for sale	377,677	296,224
Fair value option:		
Term loan investments (par value: $1,077,945 and $1,094,337)	1,061,696	1,073,649
Mezzanine debt funds	115,019	121,341
Credit related funds	138,070	114,436
Investment grade fixed income	60,383	69,108
Asian and emerging markets	26,494	25,800
Other (1)	189,709	137,094
Total fair value option	1,591,371	1,541,428
Total	$1,969,048	$ 1,837,652

(1) Includes fund investments with strategies in mortgage servicing rights, transportation and infrastructure assets and other.

Certain of the Company’s other investments are in investment funds for which the Company has the option to redeem at agreed upon values as described in each investment fund’s subscription agreement. Depending on the terms of the various subscription agreements, investments in investment funds may be redeemed daily, monthly, quarterly or on other terms. Two common redemption restrictions which may impact the Company’s ability to redeem these investment funds are gates and lockups. A gate is a suspension of redemptions which may be implemented by the general partner or investment manager of the fund in order to defer, in whole or in part, the redemption request in the event the aggregate amount of redemption requests exceeds a predetermined percentage of the investment fund’s net assets which may otherwise hinder the general partner or investment manager’s ability to liquidate holdings in an orderly fashion in order to generate the cash necessary to fund extraordinarily large redemption payouts. A lockup period is the initial amount of time an investor is contractually required to hold the security before having the ability to redeem. If the investment funds are eligible to be redeemed, the time to redeem such fund can take weeks or months following the notification.

Fair Value Option

The following table summarizes the Company’s assets and liabilities which are accounted for using the fair value option:

	June 30, 2015	December 31, 2014
Fixed maturities	$854,170	$ 632,024
Other investments	1,591,371	1,541,428
Short-term investments	167,698	251,601

Equity securities	248	—
Investments accounted for using the fair value option	$2,613,487	$ 2,425,053

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Net Investment Income

The components of net investment income were derived from the following sources:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Fixed maturities	$71,275	$65,869	$139,871	$128,318
Term loan investments	18,033	6,908	32,777	12,577
Equity securities (dividends)	2,578	3,271	5,257	6,192
Short-term investments	225	107	421	512
Other (1)	10,489	9,100	23,236	13,819
Gross investment income	102,600	85,255	201,562	161,418
Investment expenses	(15,637)	(12,265)	(35,605)	(21,434)
Net investment income	$86,963	$72,990	$165,957	$139,984

(1) Includes income distributions from investment funds and other items.

Net Realized Gains (Losses)

Net realized gains (losses) were as follows, excluding other-than-temporary impairment provisions:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Available for sale securities:				
Gross gains on investment sales	$82,233	$56,763	$179,824	$122,814
Gross losses on investment sales	(58,974)	(33,028)	(114,134)	(73,041)
Change in fair value of assets and liabilities accounted for using the fair value option:				
Fixed maturities	(5,191)	10,984	(8,493)	9,341
Other investments	785	17,985	7,072	28,761
Equity securities	(69)	—	(71)	—
Short-term investments	(4,375)	—	1,471	—
Derivative instruments (1)	(41,496)	12,402	(4,820)	(366)
Other (2)	(8,638)	(10,962)	(13,226)	(13,668)
Net realized gains (losses)	$(35,725)	$54,144	$47,623	$73,841

(1) See Note 8 for information on the Company’s derivative instruments.
(2) Includes the re-measurement of contingent consideration liability amounts.

Other-Than-Temporary Impairments

The Company performs quarterly reviews of its available for sale investments in order to determine whether declines in fair value below the amortized cost basis were considered other-than-temporary in accordance with applicable guidance. The following table details the net impairment losses recognized in earnings by asset class:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Fixed maturities:				
Mortgage backed securities	$(326)	$—	$(1,398)	$—
Corporate bonds	(10)	(664)	(1,986)	(664)
Asset backed securities	—	(5)	—	(11)
Total	(336)	(669)	(3,384)	(675)
Short-term investments	—	—	(2,341)	—
Equity securities	(124)	(278)	(253)	(278)
Other investments	(653)	(13,802)	(934)	(16,767)
Net impairment losses recognized in earnings	$(1,113)	$(14,749)	$(6,912)	$(17,720)

A description of the methodology and significant inputs used to measure the amount of net impairment losses recognized in earnings 2015 second quarter is as follows:

- Other investments — the Company utilized information received from fund managers and positive and negative evidence, including the business prospects, recent events, industry and market data and other factors. Net impairment losses for the 2015 second quarter related to a reduction in the carrying value of one fund investment;

- Mortgage backed securities — the Company utilized underlying data provided by asset managers, cash flow projections and additional information from credit agencies in order to determine an expected recovery value for each security. The analysis includes expected cash flow projections under base case and stress case scenarios which modify the expected default expectations and loss severities and slow down prepayment assumptions. The significant inputs in the models include the expected default rates, delinquency rates and foreclosure costs. Net impairment losses for the 2015 second quarter primarily resulted from small adjustments in a number of holdings. The amortized cost basis of the mortgage backed securities were adjusted down, if required, to the expected recovery value calculated in the OTTI review process;

- Equity securities – the Company utilized information received from asset managers on common stocks, including the business prospects, recent events, industry and market data and other factors. For certain equities which were in an unrealized loss position and where the Company determined that it did not have the intent or ability to hold such securities for a reasonable period of time by which the fair value of the securities would increase and the Company would recover its cost, the cost basis of such securities was adjusted down accordingly.

The Company believes that the $4.3 million of OTTI included in accumulated other comprehensive income at June 30, 2015 on the securities which were considered by the Company to be impaired was due to market and sector-related factors (i.e., not credit losses). At June 30, 2015, the Company did not intend to sell these securities, or any other securities which were in an unrealized loss position, and determined that it is more likely than not that the Company will not be required to sell such securities before recovery of their cost basis.

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The following table provides a roll forward of the amount related to credit losses recognized in earnings for which a portion of an OTTI was recognized in accumulated other comprehensive income:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Balance at start of period	$24,344	$47,256	$20,196	$60,062
Credit loss impairments recognized on securities not previously impaired	281	—	4,770	—
Credit loss impairments recognized on securities previously impaired	55	5	134	11
Reductions for increases in cash flows expected to be collected that are recognized over the remaining life of the security	—	—	—	—
Reductions for securities sold during the period	(3,774)	(25,820)	(4,194)	(38,632)
Balance at end of period	$20,906	$21,441	$20,906	$21,441

Restricted Assets

The Company is required to maintain assets on deposit, which primarily consist of fixed maturities, with various regulatory authorities to support its insurance and reinsurance operations. The Company’s insurance and reinsurance subsidiaries maintain assets in trust accounts as collateral for insurance and reinsurance transactions with affiliated companies and also have investments in segregated portfolios primarily to provide collateral or guarantees for letters of credit to third parties. See Note 9 for further details. The following table details the value of the Company’s restricted assets:

	June 30, 2015	December 31, 2014
Assets used for collateral or guarantees:		
Affiliated transactions	$3,651,244	$ 4,138,527
Third party agreements	1,040,156	970,120
Deposits with U.S. regulatory authorities	406,777	337,981
Trust funds	60,864	72,461
Total restricted assets	$5,159,041	$ 5,519,089

7. Fair Value

Accounting guidance regarding fair value measurements addresses how companies should measure fair value when they are required to use a fair value measure for recognition or disclosure purposes under GAAP and provides a common definition of fair value to be used throughout GAAP. It defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly fashion between market participants at the measurement date. In addition, it establishes a three-level valuation hierarchy for the disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The level in the hierarchy within which a given fair value measurement falls is determined based on the lowest level input that is significant to the measurement (Level 1 being the highest priority and Level 3 being the lowest priority).

The levels in the hierarchy are defined as follows:

Level 1: Inputs to the valuation methodology are observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets

Level 2: Inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement

Following is a description of the valuation methodologies used for securities measured at fair value, as well as the general classification of such securities pursuant to the valuation hierarchy. The Company reviews its securities measured at fair value and discusses the proper classification of such investments with investment advisers and others.

The Company determines the existence of an active market based on its judgment as to whether transactions for the financial instrument occur in such market with sufficient frequency and volume to provide reliable pricing information. The independent pricing sources obtain market quotations and actual transaction prices for securities that have quoted prices in active markets. The Company uses quoted values and other data provided by nationally recognized independent pricing sources as inputs into its process for determining fair values of its fixed maturity investments. To validate the techniques or models used by pricing sources, the Company's review process includes, but is not limited to: (i) quantitative analysis (e.g., comparing the quarterly return for each managed portfolio to its target benchmark, with significant differences identified and investigated); (ii) a review of the average number of prices obtained in the pricing process and the range of resulting fair values; (iii) initial and ongoing evaluation of methodologies used by outside parties to calculate fair value; (iv) a comparison of the fair value estimates to the Company’s knowledge of the current market; (v) a comparison of the pricing services' fair values to other pricing services' fair values for the same investments; and (vi) periodic back-testing, which includes randomly selecting purchased or sold securities and comparing the executed prices to the fair value estimates from the pricing service. A price source hierarchy was maintained in order to determine which price source would be used (i.e., a price obtained from a pricing service with more seniority in the hierarchy will be used over a less senior one in all cases). The hierarchy prioritizes pricing services based on availability and reliability and assigns the highest priority to index providers. Based on the above review, the Company will challenge any prices for a security or portfolio which are considered not to be representative of fair value. The Company did not adjust any of the prices obtained from the independent pricing sources at June 30, 2015.

In certain circumstances, when fair values are unavailable from these independent pricing sources, quotes are obtained directly from broker-dealers who are active in the corresponding markets. Such quotes are subject to the validation procedures noted above. Of the $14.97 billion of financial assets and liabilities measured at fair value at June 30, 2015, approximately $301.7 million, or 2.0%, were priced using non-binding broker-dealer quotes. Of the $15.06 billion of financial assets and liabilities measured at fair value at December 31, 2014, approximately $260.8 million, or 1.7%, were priced using non-binding broker-dealer quotes.

Fixed maturities. The Company uses the market approach valuation technique to estimate the fair value of its fixed maturity securities, when possible. The market approach includes obtaining prices from independent pricing services, such as index providers and pricing vendors, as well as to a lesser extent quotes from broker-dealers. The independent pricing sources obtain market quotations and actual transaction prices for securities that have quoted prices in active markets. Each source has its own proprietary method for determining the fair value of securities that are not actively traded. In general, these methods involve the use of “matrix pricing” in which the independent pricing source uses observable market inputs including, but not limited to, investment yields, credit risks and spreads, benchmarking of like securities, broker-dealer quotes, reported trades and sector groupings to determine a reasonable fair value.

The following describes the significant inputs generally used to determine the fair value of the Company's fixed maturity securities by asset class:

- U.S. government and government agencies — valuations provided by independent pricing services, with all prices provided through index providers and pricing vendors. The Company determined that all U.S. Treasuries would be classified as Level 1 securities due to observed levels of trading activity, the high number of strongly correlated pricing quotes received on U.S. Treasuries and other factors. The fair values of U.S. government agency securities are generally determined using the spread above the risk-free yield curve. As the yields for the risk-free yield curve and the spreads for these securities are observable market inputs, the fair values of U.S. government agency securities are classified within Level 2.

- Corporate bonds — valuations provided by independent pricing services, substantially all through index providers and pricing vendors with a small amount through broker-dealers. The fair values of these securities are generally determined using the spread above the risk-free yield curve. These spreads are generally obtained from the new issue market, secondary trading and from broker-dealers who trade in the relevant security market. As the significant inputs used in the pricing process for corporate bonds are observable market inputs, the fair value of these securities are classified within Level 2.

- Mortgage-backed securities — valuations provided by independent pricing services, substantially all through pricing vendors and index providers with a small amount through broker-dealers. The fair values of these securities are generally determined through the use of pricing models (including Option Adjusted Spread) which use spreads to determine the expected average life of the securities. These spreads are generally obtained from the new issue market, secondary trading and from broker-dealers who trade in the relevant security market. The pricing services also review prepayment speeds and other indicators, when applicable. As the significant inputs used in the pricing process for mortgage-backed securities are observable market inputs, the fair value of these securities are classified within Level 2.

- Municipal bonds — valuations provided by independent pricing services, with all prices provided through index providers and pricing vendors. The fair values of these securities are generally determined using spreads obtained from broker-dealers who trade in the relevant security market, trade prices and the new issue market. As the significant inputs used in the pricing process for municipal bonds are observable market inputs, the fair value of these securities are classified within Level 2.

- Commercial mortgage-backed securities — valuations provided by independent pricing services, substantially all through index providers and pricing vendors with a small amount through broker-dealers. The fair values of these securities are generally determined through the use of pricing models which use spreads to determine the appropriate average life of the securities. These spreads are generally obtained from the new issue market, secondary trading and from broker-dealers who trade in the relevant security market. The pricing services also review prepayment speeds and other indicators, when applicable. As the significant inputs used in the pricing process for commercial mortgage-backed securities are observable market inputs, the fair value of these securities are classified within Level 2.

- Non-U.S. government securities — valuations provided by independent pricing services, with all prices provided through index providers and pricing vendors. The fair values of these securities are generally based on international indices or valuation models which include daily observed yield curves, cross-currency basis index spreads and country credit spreads. As the significant inputs used in the pricing process for non-U.S. government securities are observable market inputs, the fair value of these securities are classified within Level 2.

- Asset-backed securities — valuations provided by independent pricing services, substantially all through index providers and pricing vendors with a small amount through broker-dealers. The fair values of these securities generally determined through the use of pricing models (including Option Adjusted Spread) which use spreads to determine the appropriate average life of the securities. These spreads are generally obtained from the new issue market, secondary trading and from broker-dealers who trade in the relevant security market. The pricing services also review prepayment speeds and other indicators, when applicable. As the significant inputs used in the pricing process for asset-backed securities are observable market inputs, the fair value of these securities are classified within Level 2.

During the 2015 second quarter, the Company transferred $44.6 million of U.S. government agency securities from Level 1 to Level 2 based on a review of the pricing of such securities, as described above.

Equity securities. The Company determined that exchange-traded equity securities would be included in Level 1 as their fair values are based on quoted market prices in active markets. Other equity securities are included in Level 2 of the valuation hierarchy.

Other investments. The Company determined that exchange-traded investments in mutual funds would be included in Level 1 as their fair values are based on quoted market prices in active markets. Other investments also include term loan investments for which fair values are estimated by using quoted prices of term loan investments with similar characteristics, pricing models or matrix pricing. Such investments are generally classified within Level 2. The fair values for certain of the Company's other investments are determined using net asset values as advised by external fund managers. The net asset value is based on the fund manager's valuation of the underlying holdings in accordance with the fund's governing documents. In accordance with applicable accounting guidance, certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy.

During the 2015 second quarter, the Company transferred $99.7 million of other investments from Level 2 to Level 1 based on a review of the pricing of such securities, as described above.

Derivative instruments. The Company's futures contracts, foreign currency forward contracts, interest rate swaps and other derivatives trade in the over-the-counter derivative market. The Company uses the market approach valuation technique to estimate the fair value for these derivatives based on significant observable market inputs from third party pricing vendors, non-binding broker-dealer quotes and/or recent trading activity. As the significant inputs used in the pricing process for these derivative instruments are observable market inputs, the fair value of these securities are classified within Level 2.

Short-term investments. The Company determined that certain of its short-term investments held in highly liquid money market-type funds would be included in Level 1 as their fair values are based on quoted market prices in active markets. The fair values of other short-term investments are generally determined using the spread above the risk-free yield curve and are classified within Level 2.

Contingent consideration liability. The contingent consideration liability (included in 'other liabilities' in the consolidated balance sheets) resulted from the acquisition of CMG Mortgage Insurance Company and its affiliated mortgage insurance companies and is remeasured at fair value at each balance sheet date. Changes in fair value are recognized in 'net realized gains (losses).' To determine the fair value of the contingent consideration liability, the Company estimates future payments using an income approach based on modeled inputs which include a weighted average cost of capital. The Company determined that the contingent consideration liability would be included within Level 3.

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The following table presents the Company’s financial assets and liabilities measured at fair value by level at June 30, 2015:

		Estimated Fair Value Measurements Using:		
	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets measured at fair value:				
Available for sale securities:				
Fixed maturities (1):				
Corporate bonds	$2,833,849	$—	$2,833,849	$—
Mortgage backed securities	837,680	—	837,680	—
Municipal bonds	1,760,384	—	1,760,384	—
Commercial mortgage backed securities	832,159	—	832,159	—
U.S. government and government agencies	1,899,868	1,878,893	20,975	—
Non-U.S. government securities	786,276	—	786,276	—
Asset backed securities	1,351,356	—	1,293,856	57,500
Total	10,301,572	1,878,893	8,365,179	57,500
Equity securities	701,623	698,078	3,545	—
Short-term investments	875,727	870,738	4,989	—
Other investments	89,611	89,611	—	—
Other investments measured at net asset value (2)	288,066			
Total other investments	377,677	89,611	—	—
Derivative instruments (3)	20,142	—	20,142	—
Fair value option:				
Corporate bonds	682,569	—	682,569	—
Non-U.S. government bonds	89,168	—	89,168	—
Mortgage backed securities	58,565	—	58,565	—
Asset backed securities	23,868	—	23,868	—
Short-term investments	167,698	167,698	—	—
Equity securities	248	248	—	—
Other investments	1,158,567	96,871	1,061,696	—
Other investments measured at net asset value (2)	432,804			
Total	2,613,487	264,817	1,915,866	—
Total assets measured at fair value	$14,890,228	$3,802,137	$10,309,721	$57,500
Liabilities measured at fair value:				
Contingent consideration liability	$(71,256)	$—	$—	$(71,256)
Derivative instruments (3)	(11,731)	—	(11,731)	—
Total liabilities measured at fair value	$(82,987)	$—	$(11,731)	$(71,256)

(1) In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See Note 6, “Investment Information—Securities Lending Agreements.”

(2) In accordance with applicable accounting guidance, certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheets.

(3) See Note 8, “Derivative Instruments.”

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The following table presents the Company's financial assets and liabilities measured at fair value by level at December 31, 2014:

	Estimated Fair Value	Estimated Fair Value Measurements Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets measured at fair value:				
Available for sale securities:				
Fixed maturities (1):				
Corporate bonds	$3,108,513	$—	$3,108,513	$—
Mortgage backed securities	943,343	—	943,343	—
Municipal bonds	1,494,122	—	1,494,122	—
Commercial mortgage backed securities	1,114,528	—	1,114,528	—
U.S. government and government agencies	1,447,972	1,447,972	—	—
Non-U.S. government securities	1,015,153	—	1,015,153	—
Asset backed securities	1,677,941	—	1,620,441	57,500
Total	10,801,572	1,447,972	9,296,100	57,500
Equity securities	658,182	658,182	—	—
Short-term investments	797,226	759,621	37,605	—
Other investments	97,372	—	97,372	—
Other investments measured at net asset value (2)	198,852			
Total other investments	296,224	—	97,372	—
Derivative instruments (3)	15,876	—	15,876	—
Fair value option:				
Corporate bonds	497,101	—	497,101	—
Non-U.S. government bonds	88,411	—	88,411	—
Mortgage backed securities	22,190	—	22,190	—
Asset backed securities	24,322	—	24,322	—
Short-term investments	251,601	250,580	1,021	—
Equity securities	—	—	—	—
Other investments	1,140,266	—	1,140,266	—
Other investments measured at net asset value (2)	401,162			
Total	2,425,053	250,580	1,773,311	—
Total assets measured at fair value	$14,994,133	$3,116,355	$11,220,264	$57,500
Liabilities measured at fair value:				
Contingent consideration liability	$(61,845)	$—	$—	$(61,845)
Derivative instruments (3)	(5,397)	—	(5,397)	—
Total liabilities measured at fair value	$(67,242)	$—	$(5,397)	$(61,845)

(1) In securities lending transactions, the Company receives collateral in excess of the fair value of the securities pledged. For purposes of this table, the Company has excluded the collateral received under securities lending, at fair value and included the securities pledged under securities lending, at fair value. See Note 6, “Investment Information—Securities Lending Agreements.”

(2) In accordance with applicable accounting guidance, certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated balance sheets.

(3) See Note 8, “Derivative Instruments.”

The following table presents a reconciliation of the beginning and ending balances for all financial assets and liabilities measured at fair value on a recurring basis using Level 3 inputs:

	Assets					Liabilities
s	Available For Sale			Fair Value Option		
	Asset Backed Securities	Corporate Bonds	Other Investments	Other Investments	Total	Contingent Consideration Liability
Three Months Ended June 30, 2015						
Balance at beginning of period	$57,500	$—	$—	$—	$57,500	$ (66,461)
Total gains or (losses) (realized/unrealized)						
Included in earnings (1)	—	—	—	—	—	(4,795)
Included in other comprehensive income	—	—	—	—	—	—
Purchases, issuances, sales and settlements						
Purchases	—	—	—	—	—	—
Issuances	—	—	—	—	—	—
Sales	—	—	—	—	—	—
Settlements	—	—	—	—	—	—
Transfers in and/or out of Level 3	—	—	—	—	—	—
Balance at end of period	$57,500	$—	$—	$—	$57,500	$ (71,256)
Three Months Ended June 30, 2014						
Balance at beginning of period	$—	$—	$—	$—	$—	$ (43,156)
Total gains or (losses) (realized/unrealized)						
Included in earnings (1)	—	—	—	—	—	(9,943)
Included in other comprehensive income	—	—	—	—	—	—
Purchases, issuances, sales and settlements						
Purchases	—	—	—	—	—	—
Issuances	—	—	—	—	—	—
Sales	—	—	—	—	—	—
Settlements	—	—	—	—	—	—
Transfers in and/or out of Level 3	—	—	—	—	—	—
Balance at end of period	$—	$—	$—	$—	$—	$ (53,099)
Six Months Ended June 30, 2015						
Balance at beginning of period	$57,500	$—	$—	$—	$57,500	$(61,845)
Total gains or (losses) (realized/unrealized)						
Included in earnings (1)	—	—	—	—	—	(8,343)
	—	—	—	—	—	—

Included in other comprehensive income						
Purchases, issuances, sales and settlements						
Purchases	—	—	—	—	—	—
Issuances	—	—	—	—	—	(1,068)
Sales	—	—	—	—	—	—
Settlements	—	—	—	—	—	—
Transfers in and/or out of Level 3	—	—	—	—	—	—
Balance at end of period	$57,500	$—	$—	$—	$57,500	$(71,256)
Six Months Ended June 30, 2014						
Balance at beginning of period	$—	$2,045	$170,420	$377,525	$549,990	$—
Total gains or (losses) (realized/unrealized)						
Included in earnings (1)	—	—	—	—	—	(11,337)
Included in other comprehensive income	—	—	—	—	—	—
Purchases, issuances, sales and settlements						
Purchases	—	—	—	—	—	—
Issuances	—	—	—	—	—	(41,762)
Sales	—	(2,045)	—	—	(2,045)	—
Settlements	—	—	—	—	—	—
Transfers in and/or out of Level 3 (2)	—	—	(170,420)	(377,525)	(547,945)	—
Balance at end of period	$—	$—	$—	$—	$—	$(53,099)

(1) Gains or losses on fixed maturities available for sale were included in net realized gains (losses) while gains or losses on other investments were included in net realized gains (losses) or net investment income. Gains or losses on the contingent consideration liability were included in net realized gains (losses).

(2) In accordance with applicable accounting guidance, certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The transfers out of Level 3 presented in this table are intended to permit reconciliation to information previously presented.

Financial Instruments Disclosed, But Not Carried, At Fair Value

The Company uses various financial instruments in the normal course of its business. The carrying values of cash, accrued investment income, receivable for securities sold, certain other assets, payable for securities purchased and certain other liabilities approximated their fair values at June 30, 2015, due to their respective short maturities. As these financial instruments are not actively traded, their respective fair values are classified within Level 2.

At June 30, 2015, the senior notes of ACGL were carried at their cost, net of debt issuance costs, of $296.8 million and had a fair value of $382.5 million while the senior notes of Arch-U.S. were carried at their cost, net of debt issuance costs, of $494.4 million and had a fair value of $514.2 million. The fair values of the senior notes were obtained from a third party pricing service and are based on observable market inputs. As such, the fair value of the senior notes is classified within Level 2.

8. Derivative Instruments

The Company's investment strategy allows for the use of derivative securities. The Company's derivative instruments are recorded on its consolidated balance sheets at fair value. The Company utilizes exchange traded U.S. Treasury note, Eurodollar and other futures contracts and commodity futures to manage portfolio duration or replicate investment positions in its portfolios and the Company routinely utilizes foreign currency forward contracts, currency options, index futures contracts and other derivatives as part of its total return objective. In addition, certain of the Company's investments are managed in portfolios which incorporate the use of foreign currency forward contracts which are intended to provide an economic hedge against foreign currency movements.

In addition, the Company purchases to-be-announced mortgage backed securities ("TBAs") as part of its investment strategy. TBAs represent commitments to purchase a future issuance of agency mortgage backed securities. For the period between purchase of a TBA and issuance of the underlying security, the Company's position is accounted for as a derivative. The Company purchases TBAs in both long and short positions to enhance investment performance and as part of its overall investment strategy.

The Company did not hold any derivatives which were designated as hedging instruments at June 30, 2015 or December 31, 2014. The following table summarizes information on the fair values and notional values of the Company's derivative instruments.

	Estimated Fair Value			
	Asset Derivatives	Liability Derivatives	Net Derivatives	Notional Value (1)
June 30, 2015				
Futures contracts (2)	$192	$(1,064)	$(872)	$1,683,928
Foreign currency forward contracts (2)	14,452	(7,403)	7,049	1,180,054
TBAs (3)	203,522	(158,718)	44,804	344,758
Other (2)	5,498	(3,264)	2,234	1,624,187
Total	$223,664	$(170,449)	$53,215	
December 31, 2014				
Futures contracts (2)	$2,156	$(1,907)	$249	$2,549,027
Foreign currency forward contracts (2)	10,511	(1,145)	9,366	397,106
TBAs (3)	10,592	—	10,592	10,056
Other (2)	3,209	(2,345)	864	735,684

Total	$26,468	$(5,397)	$21,071

(1) Represents the absolute notional value of all outstanding contracts, consisting of long and short positions.
(2) The fair value of asset derivatives are included in ‘other assets’ and the fair value of liability derivatives are included in ‘other liabilities.’
(3) The fair value of TBAs are included in ‘fixed maturities available for sale, at fair value.’

The Company’s derivative instruments can be traded under master netting agreements, which establish terms that apply to all derivative transactions with a counterparty. In the event of a bankruptcy or other stipulated event of default, such agreements provide that the non-defaulting party may elect to terminate all outstanding derivative transactions, in which case all individual derivative positions (loss or gain) with a counterparty are closed out and netted and replaced with a single amount, usually referred to as the termination amount, which is expressed in a single currency. The resulting single net amount, where positive, is payable to the party “in-the-money” regardless of whether or not it is the defaulting party, unless the parties have agreed that only the non-defaulting party is entitled to receive a termination payment where the net amount is positive and is in its favor. Effectively, contractual close-out netting reduces derivatives credit exposure from gross to net exposure. At June 30, 2015, asset derivatives and liability derivatives of $204.3 million and $159.0 million, respectively, were subject to a master netting agreement, compared to $25.3 million and $5.4 million, respectively, at December 31, 2014. The remaining derivatives included in the table above were not subject to a master netting agreement.

All realized and unrealized contract gains and losses on the Company’s derivative instruments are reflected in net realized gains (losses) in the consolidated statements of income, as summarized in the following table:

Derivatives not designated as hedging instruments:	Three Months Ended June 30, 2015	Three Months Ended June 30, 2014	Six Months Ended June 30, 2015	Six Months Ended June 30, 2014
Net realized gains (losses):				
Futures contracts	$(31,446)	$15,185	$(12,120)	$5,323
Foreign currency forward contracts	(8,724)	(1,811)	8,095	(4,068)
TBAs	(182)	(270)	304	(307)
Other	(1,144)	(702)	(1,099)	(1,314)
Total	$(41,496)	$12,402	$(4,820)	$(366)

9. Commitments and Contingencies

Letter of Credit and Revolving Credit Facilities

As of June 30, 2015, the Company had a $300 million unsecured revolving loan and letter of credit facility and a $500 million secured letter of credit facility (the “Credit Agreement”). The Credit Agreement expires on June 30, 2019. In addition, the Company had access to secured letter of credit facilities of approximately $229.4 million as of June 30, 2015, which are available on a limited basis and for limited purposes (together with the secured portion of the Credit Agreement and these letter of credit facilities, the “LOC Facilities”). At June 30, 2015, the Company had $456.3 million in outstanding letters of credit under the LOC Facilities, which were secured by investments with a fair value of $521.9 million, and had $100.0 million of borrowings outstanding under the Credit Agreement. The Company was in compliance with all covenants contained in the LOC Facilities at June 30, 2015.

As of June 30, 2015, Watford Re reduced its $200 million letter of credit facility to $100 million and extended the term of the facility an additional year expiring on May 19, 2016. Watford Re also entered into an $800 million secured credit facility on June 2, 2015, that provides for borrowings and the issuance of letters of credit not to exceed $400 million. That credit facility expires on June 4, 2018. At June 30, 2015, Watford Re had $36.5 million in outstanding letters of credit. Watford Re was in compliance with all covenants contained in both of its credit facilities at June 30, 2015.

Investment Commitments

The Company’s investment commitments, which are primarily related to agreements entered into by the Company to invest in funds and separately managed accounts when called upon, were approximately $1.12 billion at June 30, 2015, compared to $968.9 million at December 31, 2014.

10. Share Transactions

Share Repurchases

The board of directors of ACGL has authorized the investment in ACGL's common shares through a share repurchase program. Since the inception of the share repurchase program, ACGL has repurchased approximately 124.0 million common shares for an aggregate purchase price of $3.60 billion. During the 2015 second quarter and six months ended June 30, 2015, ACGL repurchased 3.2 million and 5.9 million common shares, respectively, for an aggregate purchase price of $199.0 million and $361.9 million, respectively. During the 2014 second quarter and six months ended June 30, 2014, ACGL did not repurchase any common shares. At June 30, 2015, $525.3 million of share repurchases were available under the program. The timing and amount of the repurchase transactions under this program will depend on a variety of factors, including market conditions and corporate and regulatory considerations.

Share-Based Compensation

During the 2015 second quarter, the Company made a stock grant of 534,267 stock appreciation rights and stock options and 559,332 restricted shares and units to certain employees and directors with weighted average grant-date fair values of $16.09 and $62.51, respectively. During the 2014 second quarter, the Company made a stock grant of 551,836 stock appreciation rights and stock options and 571,108 restricted shares and units to certain employees and directors with weighted average grant-date fair values of $15.23 and $57.25, respectively. The stock appreciation rights and stock options were valued at the grant date using the Black-Scholes option pricing model. Such values are being amortized over the respective substantive vesting period. For awards granted to retirement-eligible employees where no service is required for the employee to retain the award, the grant date fair value is immediately recognized as compensation expense at the grant date because the employee is able to retain the award without continuing to provide service. For employees near retirement eligibility, attribution of compensation cost is over the period from the grant date to the retirement eligibility date.

2015 Long Term Incentive and Share Award Plan (the “2015 Plan”)

The 2015 Plan became effective as of May 13, 2015 following approval by shareholders of the Company. The 2015 Plan is intended to provide for competitive compensation opportunities, to encourage long-term service, to recognize individual contributions and reward achievement of performance goals and to promote the creation of long-term value for shareholders by aligning the interests of such persons with those of shareholders. The 2015 Plan provides for the grant to eligible employees and directors stock options, stock appreciation rights, restricted shares, restricted share units payable in common shares or cash, share awards in lieu of cash awards, dividend equivalents and other share-based awards. The 2015 Plan will terminate as to future awards on February 26, 2025.

The number of common shares reserved for grants of awards under the 2015 Plan, subject to anti-dilution adjustments in the event of certain changes in the Company’s capital structure, is 4,300,000. In addition, no more than 50% of such common shares may be issued in connection with full value awards (i.e., awards other than stock options or stock appreciation rights) and no more than 2,000,000 common shares may be issued as incentive stock options under Section 422 of the Internal Revenue Code of 1986, as amended. At June 30, 2015, 3,235,680 shares are available for grant under the 2015 Plan.

11. Income Taxes

ACGL is incorporated under the laws of Bermuda and, under current Bermuda law, is not obligated to pay any taxes in Bermuda based upon income or capital gains. The Company has received a written undertaking from the Minister of Finance in Bermuda under the Exempted Undertakings Tax Protection Act 1966 that, in the event that any legislation is enacted in Bermuda imposing any tax computed on profits, income, gain or appreciation on any capital asset, or any tax in the nature of estate duty or inheritance tax, such tax will not be applicable to ACGL or any of its operations until March 31, 2035. This undertaking does not, however, prevent the imposition of taxes on any person ordinarily resident in Bermuda or any company in respect of its ownership of real property or leasehold interests in Bermuda.

ACGL and its non-U.S. subsidiaries will be subject to U.S. federal income tax only to the extent that they derive U.S. source income that is subject to U.S. withholding tax or income that is effectively connected with the conduct of a trade or business within the U.S. and is not exempt from U.S. tax under an applicable income tax treaty with the U.S. ACGL and its non-U.S. subsidiaries will be subject to a withholding tax on dividends from U.S. investments and interest from certain U.S. payors (subject to reduction by any applicable income tax treaty). ACGL and its non-U.S. subsidiaries intend to conduct their operations in a manner that will not cause them to be treated as engaged in a trade or business in the United States and, therefore, will not be required to pay U.S. federal income taxes (other than U.S. excise taxes on insurance and reinsurance premium and withholding taxes on dividends and certain other U.S. source investment income). However, because there is uncertainty as to the activities which constitute being engaged in a trade or business within the United States, there can be no assurances that the U.S. Internal Revenue Service will not contend successfully that ACGL or its non-U.S. subsidiaries are engaged in a trade or business in the United States. If ACGL or any of its non-U.S. subsidiaries were subject to U.S. income tax, ACGL’s shareholders’ equity and earnings could be materially adversely affected. ACGL has subsidiaries and branches that operate in various jurisdictions around the world that are subject to tax in the jurisdictions in which they operate. The significant jurisdictions in which ACGL’s subsidiaries and branches are subject to tax are the United States, United Kingdom, Ireland, Canada, Switzerland and Denmark.

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The Company's income tax provision on income before income taxes resulted in an expense of 4.3% for the six months ended June 30, 2015, compared to an expense of 2.7% for the 2014 period. The Company's effective tax rate, which is based upon the expected annual effective tax rate, may fluctuate from period to period based on the relative mix of income or loss reported by jurisdiction and the varying tax rates in each jurisdiction. The Company had a net deferred tax asset of $143.9 million at June 30, 2015, compared to $131.0 million at December 31, 2014. In addition, the Company paid $26.0 million in income taxes for the six months ended June 30, 2015, while the Company paid $8.3 million for the 2014 period.

12. Other Comprehensive Income (Loss)

The following tables present details about amounts reclassified from accumulated other comprehensive income and the tax effects allocated to each component of other comprehensive income (loss):

Details About AOCI Components	Consolidated Statement of Income Line Item That Includes Reclassification	Amounts Reclassified from AOCI Three Months Ended June 30, 2015	2014	Six Months Ended June 30, 2015	2014
Unrealized appreciation on available-for-sale investments					
	Net realized gains (losses)	$23,259	$23,735	$65,690	$49,773
	Other-than-temporary impairment losses	(1,126)	(14,749)	(8,373)	(17,720)
	Total before tax	22,133	8,986	57,317	32,053
	Income tax (expense) benefit	(919)	(701)	(5,171)	(2,519)
	Net of tax	$21,214	$8,285	$52,146	$29,534

	Before Tax Amount	Tax Expense (Benefit)	Net of Tax Amount
Three Months Ended June 30, 2015			
Unrealized appreciation (decline) in value of investments:			
Unrealized holding gains (losses) arising during period	$(96,629)	$(14,694)	$(81,935)
Portion of other-than-temporary impairment losses recognized in other comprehensive income (loss)	(13)	—	(13)
Less reclassification of net realized gains (losses) included in net income	22,133	919	21,214
Foreign currency translation adjustments	11,697	117	11,580
Other comprehensive income (loss)	$(107,078)	$(15,496)	$(91,582)
Three Months Ended June 30, 2014			
Unrealized appreciation (decline) in value of investments:			
Unrealized holding gains (losses) arising during period	$115,150	$6,722	$108,428
Portion of other-than-temporary impairment losses recognized in other comprehensive income (loss)	—	—	—
Less reclassification of net realized gains (losses) included in net income	8,986	701	8,285
Foreign currency translation adjustments	10,021	—	10,021
Other comprehensive income (loss)	$116,185	$6,021	$110,164
Six Months Ended June 30, 2015			
Unrealized appreciation (decline) in value of investments:			
Unrealized holding gains (losses) arising during period	$(2,242)	$(4,611)	$2,369

Portion of other-than-temporary impairment losses recognized in other comprehensive income (loss)	(1,461)	—	(1,461)
Less reclassification of net realized gains (losses) included in net income	57,317	5,171	52,146
Foreign currency translation adjustments	(11,929)	(752)	(11,177)
Other comprehensive income (loss)	$(72,949)	$(10,534)	$(62,415)
Six Months Ended June 30, 2014			
Unrealized appreciation (decline) in value of investments:			
Unrealized holding gains (losses) arising during period	$190,550	$10,769	$179,781
Portion of other-than-temporary impairment losses recognized in other comprehensive income (loss)	—	—	—
Less reclassification of net realized gains (losses) included in net income	32,053	2,519	29,534
Foreign currency translation adjustments	8,672	—	8,672
Other comprehensive income (loss)	$167,169	$8,250	$158,919

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13. Guarantor Financial Information

The following tables present condensed financial information for ACGL, Arch Capital Group (U.S.) Inc. ("Arch-U.S."), a 100% owned subsidiary of ACGL, and ACGL's other subsidiaries.

	June 30, 2015				
Condensed Consolidating Balance Sheet	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Assets					
Total investments	$471	$55,047	$15,306,122	$(14,700)	$15,346,940
Cash	10,864	6,928	507,282	—	525,074
Investments in subsidiaries	6,530,452	1,688,419	—	(8,218,871)	—
Due from subsidiaries and affiliates	11	47,798	417,231	(465,040)	—
Premiums receivable	—	—	1,620,756	(439,120)	1,181,636
Reinsurance recoverable on unpaid and paid losses and loss adjustment expenses	—	—	5,741,646	(3,910,419)	1,831,227
Contractholder receivables	—	—	1,393,138	—	1,393,138
Prepaid reinsurance premiums	—	—	1,595,550	(1,153,409)	442,141
Deferred acquisition costs, net	—	—	448,647	—	448,647
Other assets	4,208	46,157	2,274,796	(409,039)	1,916,122
Total assets	$6,546,006	$1,844,349	$29,305,168	$(14,610,598)	$23,084,925
Liabilities					
Reserve for losses and loss adjustment expenses	$—	$—	$12,970,720	$(3,888,439)	$9,082,281
Unearned premiums	—	—	3,596,332	(1,153,409)	2,442,923
Reinsurance balances payable	—	—	678,216	(425,754)	252,462
Contractholder payables	—	—	1,393,138	—	1,393,138
Deposit accounting liabilities	—	—	495,121	(217,598)	277,523
Senior notes	296,834	494,388	—	—	791,222
Revolving credit agreement borrowings	100,000	—	—	—	100,000
Due to subsidiaries and affiliates	402	35,000	429,638	(465,040)	—
Other liabilities	11,255	44,917	1,778,600	(226,787)	1,607,985
Total liabilities	408,491	574,305	21,341,765	(6,377,027)	15,947,534
Redeemable noncontrolling interests	—	—	219,696	(14,700)	204,996
Shareholders' Equity					
Total shareholders' equity available to Arch	6,137,515	1,270,044	6,948,827	(8,218,871)	6,137,515
Non-redeemable noncontrolling interests	—	—	794,880	—	794,880
Total shareholders' equity	6,137,515	1,270,044	7,743,707	(8,218,871)	6,932,395
Total liabilities, noncontrolling interests and shareholders' equity	$6,546,006	$1,844,349	$29,305,168	$(14,610,598)	$23,084,925

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	December 31, 2014				
Condensed Consolidating Balance Sheet	ACGL (Parent Guarantor)	Arch-U.S. (Subsidiary Issuer)	Other ACGL Subsidiaries	Consolidating Adjustments and Eliminations	ACGL Consolidated
Assets					
Total investments	$107	$62,867	$15,257,796	$—	$15,320,770
Cash	3,218	2,787	479,697	—	485,702
Investments in subsidiaries	6,536,644	1,685,185	—	(8,221,829)	—
Due from subsidiaries and affiliates	48	7,517	370,429	(377,994)	—
Premiums receivable	—	—	1,331,511	(382,816)	948,695
Reinsurance recoverable on unpaid and paid losses and loss adjustment expenses	—	—	5,584,973	(3,772,128)	1,812,845
Contractholder receivables	—	—	1,309,192	—	1,309,192
Prepaid reinsurance premiums	—	—	1,373,008	(995,930)	377,078
Deferred acquisition costs, net	—	—	414,525	—	414,525
Other assets	4,386	43,921	1,705,546	(416,579)	1,337,274
Total assets	$6,544,403	$1,802,277	$27,826,677	$(14,167,276)	$22,006,081
Liabilities					
Reserve for losses and loss adjustment expenses	$—	$—	$12,784,030	$(3,747,582)	$9,036,448
Unearned premiums	—	—	3,227,508	(995,930)	2,231,578
Reinsurance balances payable	—	—	589,289	(369,977)	219,312
Contractholder payables	—	—	1,309,192	—	1,309,192
Deposit accounting liabilities	—	—	587,050	(259,666)	327,384
Senior notes	296,796	494,345	—	—	791,141
Revolving credit agreement borrowings	100,000	—	—	—	100,000
Due to subsidiaries and affiliates	417	7,505	370,072	(377,994)	—
Other liabilities	17,137	49,403	1,000,138	(194,298)	872,380
Total liabilities	414,350	551,253	19,867,279	(5,945,447)	14,887,435
Redeemable noncontrolling interests	—	—	219,512	—	219,512