SCOTTISH RE GROUP LIMITED

CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2017

(These consolidated financial statements are unaudited.)

Table of Contents

SCOTTISH RE GROUP LIMITED
CONSOLIDATED BALANCE SHEETS
(Expressed in Thousands of United States Dollars, except share data)

	March 31, 2017 (Unaudited)	December 31, 2016 (Audited)
Assets		
Fixed-maturity investments held as trading securities, at fair value	$ 948,482	$ 1,000,889
Fixed-maturity investments held as available-for-sale securities, at fair value (amortized cost: 2017 – $540,948; 2016 – $477,409)	544,485	478,128
Common stock investments held as available-for-sale securities, at fair value (cost: 2017 – $15,914)	15,970	-
Cash and cash equivalents	186,435	194,920
Other investments	2,325	2,368
Funds withheld at interest	358,688	362,761
Total investments[1]	2,056,385	2,039,066
Accrued interest receivable[2]	9,005	9,219
Amounts recoverable from reinsurers	588,389	652,536
Reinsurance balances receivable	123,072	194,882
Deferred acquisition costs	22,310	23,531
Other assets	1,031	1,290
Total assets	$ 2,800,192	$ 2,920,524
Liabilities		
Reserves for future policy benefits	$ 1,309,048	$ 1,392,659
Interest-sensitive contract liabilities	752,678	765,610
Collateral finance facility, net of debt issuance costs[3]	448,120	447,978
Reinsurance balances payable	132,669	142,739
Accounts payable and other liabilities[4]	105,505	101,858
Embedded derivative liabilities, at fair value	13,282	15,640
Long-term debt, at par value	86,500	86,500
Total liabilities	2,847,802	$ 2,952,984
Shareholders' Deficit		
Ordinary shares, par value $0.01: 218,383,370 shares issued and outstanding	2,184	2,184
Non-cumulative perpetual preferred shares, par value $0.01: 3,246,776 shares issued and outstanding	81,169	81,169
Additional paid-in capital	1,772,547	1,772,547
Accumulated other comprehensive income (loss), net of taxes and deferred acquisition costs	3,219	628
Retained deficit	(1,906,729)	(1,888,988)
Total shareholders' deficit	(47,610)	(32,460)
Total liabilities and total shareholders' deficit	$ 2,800,192	$ 2,920,524

[1] Includes total investments of consolidated variable interest entity ("VIE")	$ 282,844	$ 278,216
[2] Includes accrued interest receivable of consolidated VIE	1,349	1,326
[3] Reflects collateral finance facility, net of debt issuance costs, of consolidated VIE	448,166	448,056
[4] Reflects accounts payable and other liabilities of consolidated VIE	81,717	76,602

See Accompanying Notes to Consolidated Financial Statements (Unaudited)

SCOTTISH RE GROUP LIMITED
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

(Expressed in Thousands of United States Dollars)

	Three month period ended	
	March 31, 2017	**March 31, 2016**
Revenues		
Premiums earned, net	$ 68,744	$ 78,321
Investment income, net	15,003	16,851
Net realized and unrealized gains (losses)	7,325	(3,423)
Change in fair value of embedded derivative assets and liabilities	2,358	(5,960)
Fees and other income	463	484
Total revenues	93,893	86,273
Benefits and expenses		
Claims, policy benefits, and changes in policyholder reserves, net	86,620	83,433
Interest credited to interest-sensitive contract liabilities	4,991	5,474
Other insurance expenses, including amortization and release of deferred acquisition costs, net	10,427	7,102
Operating expenses	5,066	4,456
Collateral finance facilities expense	3,357	2,911
Interest expense	1,173	1,003
Total benefits and expenses	111,634	104,379
Income (loss) before income taxes	(17,741)	(18,106)
Income tax benefit (expense)	-	(206)
Net income (loss)	(17,741)	(18,312)
Other comprehensive income (loss), net:		
Unrealized gains (losses) on available-for-sale investments, net of taxes and deferred acquisition costs	2,591	6,290
Total other comprehensive income (loss), net	2,591	6,290
Total comprehensive income (loss)	$ (15,150)	$ (12,022)

See Accompanying Notes to Consolidated Financial Statements (Unaudited)

SCOTTISH RE GROUP LIMITED
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' DEFICIT
(UNAUDITED)

(Expressed in Thousands of United States Dollars)

	Three month period ended March 31, 2017	Three month period ended March 31, 2016
Share capital:		
Ordinary shares:		
Beginning and end of period	$ 2,184	$ 684
Non-cumulative perpetual preferred shares:		
Beginning and end of period	81,169	81,169
Additional paid-in capital:		
Beginning and end of period	1,772,547	1,218,190
Accumulated other comprehensive income (loss):		
Beginning of period	628	(4,718)
Other comprehensive income (loss), net of taxes and deferred acquisition costs	2,591	6,290
End of period	3,219	1,572
Retained deficit:		
Beginning of period	(1,888,988)	(1,680,837)
Net income (loss)	(17,741)	(18,312)
End of period	(1,906,729)	(1,699,149)
Total shareholders' deficit	$ (47,610)	$ (397,534)

See Accompanying Notes to Consolidated Financial Statements (Unaudited)

SCOTTISH RE GROUP LIMITED
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

(Expressed in Thousands of United States Dollars)

	Three month period ended March 31, 2017	Three month period ended March 31, 2016
Operating activities		
Net income (loss)	$ (17,741)	$ (18,312)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Net realized and unrealized (gains) losses	(7,325)	3,423
Changes in value of embedded derivative assets and liabilities	(2,358)	5,960
Amortization (accretion) of fixed-maturity investments – available-for-sale	237	103
Amortization of deferred acquisition costs	1,221	(660)
Amortization of deferred finance facility costs	142	155
Changes in assets and liabilities:		
Funds withheld at interest	4,073	11,806
Accrued interest receivable	214	(284)
Reinsurance balances receivable	71,810	5,148
Other assets	(21)	192
Reserves for future policy benefits, net of amounts recoverable from reinsurers	(19,464)	11,642
Interest-sensitive contract liabilities	(5,042)	(10,071)
Accounts payable and other liabilities, including deferred tax liabilities	3,647	3,932
Reinsurance balances payable	(10,070)	(1,006)
Net cash used in operating activities	19,323	12,028
Investing activities		
Purchase of fixed-maturity investments – available-for-sale	(74,462)	(77,053)
Purchase of common stock investments – available-for-sale	(15,914)	-
Proceeds from sales and maturities of fixed-maturity investments – trading	59,742	47,710
Proceeds from sales and maturities of fixed-maturity investments – available-for-sale	10,686	2,198
Purchases of and proceeds from affiliated investments, net	-	(298)
Purchase of and proceeds from other investments, net	42	190
Net cash provided by investing activities	(19,906)	(27,253)
Financing activities		
Withdrawals from interest-sensitive contract liabilities	(7,902)	(11,708)
Net cash used in financing activities	(7,902)	(11,708)
Net change in cash and cash equivalents	(8,485)	(26,933)
Cash and cash equivalents, beginning of period	194,920	166,277
Cash and cash equivalents, end of period	$ 186,435	$ 139,344

See Accompanying Notes to Consolidated Financial Statements (Unaudited)

1. Organization, Business Strategy, and Lines of Business

Organization

Scottish Re Group Limited ("SRGL" and, together with SRGL's consolidated subsidiaries and, as a result of the application of FASB ASC 810-10 (as defined in Note 2, "Basis of Presentation" herein), its consolidated VIE*, as applicable, the "Company", "we", "our", and "us") is a holding company incorporated under the laws of the Cayman Islands, and with its principal executive office located in Bermuda. Through its operating subsidiaries, the Company is principally engaged in the reinsurance of life insurance, annuities, and annuity-type products. All of the equity voting power of SRGL, along with the right to designate a controlling number of members of SRGL's Board of Directors (the "Board"), is controlled directly or indirectly by MassMutual Capital Partners LLC, a member of the MassMutual Financial Group ("MassMutual Capital") and SRGL Acquisition, LDC, an affiliate of Cerberus Capital Management L.P. ("Cerberus" and, together with MassMutual Capital, the "Investors"). As of March 31, 2017, SRGL's consolidated subsidiaries (consisting of operating companies, holding companies, and financing companies) and its consolidated VIE (a collateral finance facility), by jurisdiction, were as follows:

<u>Bermuda</u>
Scottish Re Life (Bermuda) Limited ("SRLB")

<u>Cayman Islands</u>
Scottish Annuity & Life Insurance Company (Cayman) Ltd. ("SALIC")

<u>Ireland</u>
Scottish Re (Dublin) dac ("SRD")
Orkney Re II plc ("Orkney Re II")*

<u>Luxembourg</u>
Scottish Financial (Luxembourg) S.á r.l. ("SFL")

<u>United States of America ("U.S." or "United States")</u>
Scottish Holdings, Inc. ("SHI")
Scottish Re (U.S.), Inc. ("SRUS")

* *Orkney Re II is the consolidated VIE. References in the consolidated financial statements and accompanying notes to any discretionary acts of management or of any of the consolidated entities do not, unless explicitly stated otherwise, refer to any such acts by Orkney Re II.*

Business Strategy

In 2008, our insurance operating companies ceased writing new business and notified existing clients that new reinsurance risks no longer would be accepted under existing reinsurance treaties, thereby placing the reinsurance business into run-off (the "Closed Block"). We continue to manage the Closed Block, performing key activities and actively managing the business under the terms of the related reinsurance treaties.

Lines of Business

As defined and described in our audited consolidated financial statements and accompanying notes thereto for the year ended December 31, 2016, we have written reinsurance business that is wholly or partially retained in one or more of our reinsurance subsidiaries and have classified the reinsurance as Traditional Solutions or as Financial Solutions.

1. Organization, Business Strategy, and Lines of Business (continued)

Going Concern

These consolidated financial statements have been prepared using accounting principles applicable to a going concern, which contemplates the realization of assets and the satisfaction of liabilities and commitments in the normal course of business.

The Company's management assesses whether conditions and events raise substantial doubt that the Company will be able to continue as a going concern. Assessment of whether substantial doubt exists requires management to evaluate whether conditions and events, considered in the aggregate, indicate that it is probable that the Company will be unable to meet its obligations as they become due within one year of the issuance of the consolidated financial statements. Our ability to continue as a going concern is, therefore, dependent upon our ability to successfully meet our obligations, satisfy ongoing regulatory requirements and maintain adequate capital and liquidity.

As disclosed in the SRGL's audited consolidated financial statements and accompanying notes thereto for the year ended December 31, 2016, adverse mortality experience on the Traditional Solutions yearly renewable term ("YRT") business has had a substantial negative impact on the operating results. Absent a significant improvement in the performance on the YRT business during the remainder of 2017, the Company will incur additional capital strain, thereby further reducing available funds and eroding the Company's ability to pay the deferred interest on the Capital and Trust Preferred Securities (as defined herein) as such deferred interest payments become due during the first quarter of 2018. Accordingly, substantial doubt exists that the Company will be able to meet these deferred interest payments.

Management continues to monitor and evaluate alternatives to the current situation, however, there currently are no strategies that both are probable of effectively being implemented and that would supply funds in such amounts and at such times as would be necessary to mitigate the conditions and events described above.

These consolidated financial statements do not give effect to any adjustments to recorded amounts and their classification which would be necessary if a liquidation of the Company was imminent. Should this occur, we would be required to realize our assets and discharge our liabilities and commitments in other than the normal course of business and at amounts different from those reflected in the consolidated financial statements.

For further discussion on the Going Concern, please refer to Note 11, "Subsequent Events – *Going Concern*".

2. Basis of Presentation

Accounting Principles – Our consolidated interim financial statements are prepared in accordance with U.S. Generally Accepted Accounting Principles ("U.S. GAAP"). Accordingly, these consolidated interim financial statements do not include all of the information and notes required by U.S. GAAP for annual financial statements. These unaudited consolidated interim financial statements should be read in conjunction with SRGL's audited consolidated financial statements and accompanying notes thereto for the year ended December 31, 2016.

Consolidation – The consolidated interim financial statements include the assets, liabilities, and results of operations of SRGL, its subsidiaries, and the VIE for which we are the primary beneficiary, as defined in Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Subtopic 810-10, Consolidation – Overall. All significant intercompany transactions and balances have been eliminated in consolidation.

2. Basis of Presentation (continued)

We currently consolidate one non-recourse securitization, Orkney Re II, a special purpose VIE incorporated under the laws of Ireland. For further discussion on Orkney Re II, please refer to Note 5, "Collateral Finance Facility and Securitization Structure".

Estimates and Assumptions – The preparation of consolidated interim financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated interim financial statements and accompanying notes. Actual results could differ materially from those estimates and assumptions used by management, and such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and disclosed herein.

Our most significant assumptions are for:

- investment valuations;
- accounting for embedded derivative instruments;
- assessment of risk transfer for structured insurance and reinsurance contracts;
- estimates of premiums;
- reserves for future policy benefits;
- retrocession arrangements and amounts recoverable from reinsurers;
- interest-sensitive contract liabilities; and
- current taxes, deferred taxes, and the determination of associated valuation allowances.

Where applicable, management periodically reviews and revises these estimates, as appropriate. Any adjustments made to these estimates are reflected in the period in which the estimates are revised.

3. Investments

Trading Investments

The estimated fair values of our fixed-maturity investments held as trading securities as of March 31, 2017 and December 31, 2016, were as follows:

(U.S. dollars in thousands)	March 31, 2017	December 31, 2016
U.S. Treasury securities and U.S. government agency obligations	$ 16,502	$ 17,682
Corporate securities	279,912	293,161
Municipal bonds	26,119	26,167
Residential mortgage-backed securities	352,802	359,126
Commercial mortgage-backed securities	109,250	112,129
Asset-backed securities	163,897	192,624
Total trading securities	$ 948,482	$ 1,000,889

3. Investments (continued)

The contractual maturities of the fixed-maturity investments held as trading securities as of March 31, 2017 and December 31, 2016, were as follows (actual maturities may differ as a result of calls and prepayments):

(U.S. dollars in thousands)	Estimated Fair Value March 31, 2017	Estimated Fair Value December 31, 2016
Due in one year or less	$ 40,049	$ 34,631
Due after one year through five years	188,968	196,056
Due after five years through ten years	54,134	62,898
Due after ten years	39,382	43,425
	322,533	337,010
Residential mortgage-backed securities	352,802	359,126
Commercial mortgage-backed securities	109,250	112,129
Asset-backed securities	163,897	192,624
Total trading securities	$ 948,482	$ 1,000,889

Available-for-Sale Investments

The amortized cost and estimated fair value of fixed-maturity and common stock securities classified as available-for-sale as of March 31, 2017 and December 31, 2016, were as follows:

(U.S. dollars in thousands)	March 31, 2017				
		Gross Unrealized			
	Cost or Amortized Cost	Gains	Temporary Losses	Other Than Temporary Losses	Estimated Fair Value
U.S. Treasury securities and U.S. government agency obligations	$ 23,701	$ -	$ (55)	$ -	$ 23,646
Corporate securities	297,199	4,304	(889)	-	300,614
Municipal bonds	2,531	50	(1)	-	2,580
Residential mortgage-backed securities	12,248	34	(46)	-	12,236
Commercial mortgage-backed securities	26,034	243	(339)	-	25,938
Asset-backed securities	179,235	414	(178)	-	179,471
Total fixed-maturity securities	540,948	5,045	(1,508)	-	544,485
Common stock	15,914	56	-	-	15,970
Total available-for-sale securities	$ 556,862	$ 5,101	$ (1,508)	$ -	$ 560,455

3. Investments (continued)

(U.S. dollars in thousands)	December 31, 2016				
		Gross Unrealized			
	Cost or Amortized Cost	Gains	Temporary Losses	Other Than Temporary Losses	Estimated Fair Value
U.S. Treasury securities and U.S. government agency obligations	$ 23,701	$ -	$ (66)	$ -	$ 23,635
Corporate securities	285,453	2,710	(1,706)	-	286,457
Municipal bonds	-	-	-	-	-
Residential mortgage-backed securities	4,477	10	(39)	-	4,448
Commercial mortgage-backed securities	25,932	214	(476)	-	25,670
Asset-backed securities	137,846	298	(226)	-	137,918
Total available-for-sale securities	$ 477,409	$ 3,232	$ (2,513)	$ -	$ 478,128

The estimated fair value and gross unrealized losses of all investments classified as available-for-sale, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, as of March 31, 2017 and December 31, 2016, were as follows:

(U.S. dollars in thousands)	March 31, 2017					
	Less than 12 months		12 months or more		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
U.S. Treasury securities and U.S. government agency obligations	$ 23,646	$ (55)	$ -	$ -	$ 23,646	$ (55)
Corporate securities	75,621	(853)	1,460	(36)	77,081	(889)
Municipal bonds	406	(1)	-	-	406	(1)
Residential mortgage-backed securities	2,942	(46)	-	-	2,942	(46)
Commercial mortgage-backed securities	11,333	(250)	1,751	(89)	13,084	(339)
Asset-backed securities	26,953	(67)	13,781	(111)	40,734	(178)
Total fixed-maturity securities	140,901	(1,272)	16,992	(236)	157,893	(1,508)
Common stock	-	-	-	-	-	-
Total available-for-sale securities	$ 140,901	$ (1,272)	$ 16,992	$ (236)	$ 157,893	$ (1,508)

3. Investments (continued)

(U.S. dollars in thousands)	December 31, 2016					
	Less than 12 months		12 months or more		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
U.S. Treasury securities and U.S. government agency obligations	$ 23,635	$ (66)	$ -	$ -	$ 23,635	$ (66)
Corporate securities	98,857	(1,660)	1,450	(46)	100,307	(1,706)
Municipal bonds	-	-	-	-	-	-
Residential mortgage-backed securities	979	(39)	-	-	979	(39)
Commercial mortgage-backed securities	10,101	(340)	1,705	(136)	11,806	(476)
Asset-backed securities	28,033	(151)	22,035	(75)	50,068	(226)
Total fixed-maturity securities	161,605	(2,256)	25,190	(257)	186,795	(2,513)
Common stock	-	-	-	-	-	-
Total available-for-sale securities	$ 161,605	$ (2,256)	$ 25,190	$ (257)	$ 186,795	$ (2,513)

The total number of securities classified as available-for-sale that had unrealized losses as of March 31, 2017 and December 31, 2016, were 119 and 155, respectively. The Company's unrealized losses on its fixed-maturity investments were the result of interest rate increases. Since the decline in estimated fair value is attributable to changes in interest rates and not credit quality, and the Company has the intent and ability to hold these maturities through a recovery of unrealized losses, or until maturity of the individual securities, the Company does not consider these investments other than temporarily impaired.

The contractual maturities of the fixed-maturity investments classified as available-for-sale securities as of March 31, 2017 and December 31, 2016, were as follows (actual maturities may differ as a result of calls and prepayments):

(U.S. dollars in thousands)	Cost or Amortized Cost March 31, 2017	Estimated Fair Value March 31, 2017
Due in one year or less	$ 6,053	$ 6,049
Due after one year through five years	115,414	116,239
Due after five years through ten years	191,500	193,721
Due after ten years	10,464	10,831
	323,431	326,840
Residential mortgage-backed securities	12,248	12,236
Commercial mortgage-backed securities	26,034	25,938
Asset-backed securities	179,235	179,471
Total fixed-maturity available-for-sale securities	$ 540,948	$ 544,485

3. Investments (continued)

(U.S. dollars in thousands)	Cost or Amortized Cost December 31, 2016	Estimated Fair Value December 31, 2016
Due in one year or less	$ 5,156	$ 5,160
Due after one year through five years	113,792	114,072
Due after five years through ten years	181,782	182,338
Due after ten years	8,424	8,522
	309,154	310,092
Residential mortgage-backed securities	4,477	4,448
Commercial mortgage-backed securities	25,932	25,670
Asset-backed securities	137,846	137,918
Total fixed-maturity available-for-sale securities	$ 477,409	$ 478,128

Assets on Deposit

We are required to maintain assets on deposit with various U.S. regulatory authorities, in accordance with the statutory regulations of the individual jurisdictions, to support our insurance and reinsurance operations. As a result of the various regulatory limitations on how these assets may be invested and their unavailability for general corporate purposes, these assets are considered "restricted". We also have established trust funds* in connection with certain transactions for the benefit of the transaction counterparties, which amounts also include assets attributable to the VIE that we consolidate, Orkney Re II. As a result of the restrictions imposed on the foregoing assets in accordance with the respective reinsurance treaties and other agreements to which they relate, these assets (including the assets within the collateral finance facility that are held for the contractual obligations of that structure) are not available for general corporate purposes and also are considered "restricted". (Please also refer to Note 5, "Collateral Finance Facility and Securitization Structure" for additional information.)

The estimated fair value of the components of the restricted assets as of March 31, 2017 and December 31, 2016, were as follows:

(U.S. dollars in thousands)	March 31, 2017	December 31, 2016
Deposits with U.S. regulatory authorities	$ 4,579	$ 4,578
Trust funds* attributable to VIE	440,656	437,957
Trust funds*	821,968	649,511
Total	$ 1,267,203	$ 1,092,046

**"Trust funds" in the above table reflects the fair value of assets held by ceding companies under modified coinsurance arrangements and the fair value of assets we hold in segregated portfolios under coinsurance arrangements. The assets that comprise the "Trust funds" are included in fixed-maturity investments held as trading securities, fixed-maturity investments held as available-for-sale securities, common stock investments held as available-for-sale securities, cash and cash equivalents, and funds withheld at interest in the Consolidated Balance Sheets.*

3. Investments (continued)

Net Investment Income

Net investment income on investments and other balances for the three month periods ended March 31, 2017 and 2016, was derived from the following sources:

(U.S. dollars in thousands)	Three Month Period Ended March 31, 2017	Three Month Period Ended March 31, 2016
Fixed-maturity investments, held as trading	$ 9,250	$ 11,118
Fixed-maturity investments, held as available-for sale	3,689	2,868
Funds withheld at interest	2,560	3,076
Other investments	215	193
Investment expenses	(711)	(404)
Net investment income	$ 15,003	$ 16,851

Realized and Unrealized Gains (Losses)

The components of realized and unrealized gains (losses) on investments and other balances for the three month periods ended March 31, 2017 and 2016, were as follows:

(U.S. dollars in thousands)	Three Month Period Ended March 31, 2017	Three Month Period Ended March 31, 2016
Realized and unrealized gains (losses)		
Fixed-maturity investments		
Gross realized gains	$ 85	$ 102
Net unrealized gains (losses), trading securities	7,248	(1,858)
	7,333	(1,756)
Other		
Cerberus Affiliated Fund* - realized and unrealized gains (losses)	-	(1,647)
Realized gains (losses) on modified coinsurance treaties	(12)	(28)
Other	4	8
	(8)	(1,667)
Net realized and unrealized gains (losses)	$ 7,325	$ (3,423)
Change in unrealized gains (losses) on available-for-sale investments, net		
Fixed-maturity investments	2,816	6,290
Common stock investments	56	-
Change in deferred income taxes	(72)	-
Change in deferred acquisition costs	(209)	-
Unrealized gains (losses) on available-for-sale investments, net of taxes and deferred acquisition costs	$ 2,591	$ 6,290

* *Defined in the "Affiliated Investments" section in this Note.*

3. Investments (continued)

Affiliated Investments

Affiliated investments represented investments accounted for under the equity method, in accordance with FASB ASC 323 Investments – Equity Method and Joint Ventures, for which the resulting equity method carrying value is deemed to approximate fair value. The investments accounted for under the equity method represented executed subscription documents, signed by SALIC on March 26, 2012, pursuant to which SALIC committed to make an investment of up to an aggregate $30.0 million in an investment fund affiliated with and controlled, directly or indirectly, by Cerberus (the “Cerberus Affiliated Fund”).

On December 1, 2016, SALIC entered into an agreement to sell to a third-party purchaser, in a privately-negotiated transaction, its investment in the Cerberus Affiliated Fund for approximately $35.9 million. The cost (capital commitment) of the Cerberus Affiliated Fund by SALIC at the time of the transaction was approximately $28.9 million. The carrying value of the Cerberus Affiliated Fund at the time of the transaction was approximately $41.8 million. In accordance with FASB ASC Topic 323, the Company recorded a $5.9 million realized loss in the fourth quarter of 2016 on the Cerberus Affiliated Fund. The $5.9 million realized loss on the Cerberus Affiliated Fund investment was included in the Consolidated Statements of Comprehensive Income for the year ended December 31, 2016, under the caption, “Net unrealized and unrealized gains (losses)”.

4. Fair Value Measurements

FASB ASC 820 Fair Value Measurements and Disclosures (“FASB ASC 820”) defines fair value, establishes a framework for measuring fair value based on an exit price definition, establishes a fair value hierarchy based on the quality of inputs used to measure fair value, and provides disclosure requirements for fair value measurements. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements), as described in Note 5, “Fair Value Measurements” in our audited consolidated financial statements and accompanying notes thereto for the year ended December 31, 2016, which, along with Note 3, “Investments” above, also includes additional disclosures regarding our fair value measurements.

4. Fair Value Measurements (continued)

Fair Value Measurements on a Recurring Basis

The following tables set forth our assets and liabilities that were measured at fair value on a recurring basis, as of the dates indicated:

	March 31, 2017			
(U.S. dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Investments – trading				
U.S. Treasury securities and U.S. government agency obligations	$ -	$ 16,502	$ -	$ 16,502
Corporate securities	-	274,090	5,822	279,912
Municipal bonds	-	26,119	-	26,119
Residential mortgage-backed securities	-	93,444	259,358	352,802
Commercial mortgage-backed securities	-	109,250	-	109,250
Asset-backed securities	-	139,753	24,144	163,897
Fixed-maturity investments, held as trading	-	659,158	289,324	948,482
Investments – available-for-sale				
U.S. Treasury securities and U.S. government agency obligations	$ -	$ 23,646	$ -	$ 23,646
Corporate securities	-	300,614	-	300,614
Municipal bonds	-	2,580	-	2,580
Residential mortgage-backed securities	-	12,236	-	12,236
Commercial mortgage-backed securities	-	25,938	-	25,938
Asset-backed securities	-	177,465	2,006	179,471
Fixed-maturity investments, held as available-for-sale	-	542,479	2,006	544,485
Common stock	-	15,970	-	15,970
Total investments, held as available-for-sale	-	558,449	2,006	560,455
Total assets at fair value	$ -	$ 1,217,607	$ 291,330	$ 1,508,937
Embedded derivative liabilities	-	-	(13,282)	(13,282)
Total liabilities at fair value	$ -	$ -	$ (13,282)	$ (13,282)

4. Fair Value Measurements (continued)

	December 31, 2016			
(U.S. dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Investments – trading				
U.S. Treasury securities and U.S. government agency obligations	$ -	$ 17,682	$ -	$ 17,682
Corporate securities	-	287,323	5,838	293,161
Municipal bonds	-	26,167	-	26,167
Residential mortgage-backed securities	-	99,982	259,144	359,126
Commercial mortgage-backed securities	-	112,118	11	112,129
Asset-backed securities	-	168,226	24,398	192,624
Fixed-maturity investments, held as trading	-	711,498	289,391	1,000,889
Investments – available-for-sale				
U.S. Treasury securities and U.S. government agency obligations	$ -	$ 23,635	$ -	$ 23,635
Corporate securities	-	286,457	-	286,457
Municipal bonds	-	-	-	-
Residential mortgage-backed securities	-	4,448	-	4,448
Commercial mortgage-backed securities	-	25,670	-	25,670
Asset-backed securities	-	137,859	59	137,918
Fixed-maturity investments, held as available-for-sale	-	478,069	59	478,128
Total assets at fair value	$ -	$ 1,189,567	$ 289,450	$ 1,479,017
Embedded derivative liabilities	-	-	(15,640)	(15,640)
Total liabilities at fair value	$ -	$ -	$ (15,640)	$ (15,640)

4. Fair Value Measurements (continued)

The following tables present additional information about our assets and liabilities measured at fair value on a recurring basis for which we have utilized significant unobservable (Level 3) inputs to determine fair values:

Fair Value Measurements Using Significant Unobservable Inputs (Level 3) for the three month period ended March 31, 2017

(U.S. dollars in thousands)	Corporate securities	Municipal bonds	Residential mortgage-backed securities	Commercial mortgage-backed securities	Asset-backed securities	Total assets at fair value	Total liabilities at fair value
Beginning balance as of January 1, 2017	$ 5,838	$ -	$ 259,144	$ 11	$ 24,457	$ 289,450	$ (15,640)
Total realized and unrealized gains (losses) included on trading securities in net income	30	-	2,903	-	177	3,110	2,358
Total unrealized gains (losses) included on available-for-sale securities in comprehensive net income (loss)	-	-	-	-	1	1	-
Purchases	-	-	-	-	1,974	1,974	-
Settlements	(46)	-	(6,574)	(11)	(475)	(7,106)	-
Accretion (amortization)	-	-	3,885	-	16	3,901	-
Transfers into and/or (out of) Level 3, net	-	-	-	-	-	-	-
Ending balance as of March 31, 2017	$ 5,822	$ -	$ 259,358	$ -	$ 26,150	$ 291,330	$ (13,282)

4. Fair Value Measurements (continued)

(U.S. dollars in thousands)	Corporate securities	Municipal bonds	Residential mortgage-backed securities	Commercial mortgage-backed securities	Asset-backed securities	Total assets at fair value	Total liabilities at fair value
	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) for the year ended December 31, 2016						
Beginning balance as of January 1, 2016	$ 6,996	$ -	$ 267,849	$ 121	$ 26,110	$ 301,076	$ (16,871)
Total realized and unrealized gains (losses) included on trading securities in net income	(191)	-	(47)	2	15	(221)	1,231
Total unrealized gains (losses) included on available-for-sale securities in comprehensive net income (loss)	-	-	(742)	-	(2)	(744)	-
Purchases	-	-	-	-	-	-	-
Settlements	(1,067)	-	(23,088)	(113)	(1,352)	(25,620)	-
Accretion (amortization)	100	-	15,172	1	65	15,338	-
Transfers into and/or (out of) Level 3, net	-	-	-	-	(379)	(379)	-
Ending balance as of December 31, 2016	$ 5,838	$ -	$ 259,144	$ 11	$ 24,457	$ 289,450	$ (15,640)

Changes in classifications impacting Level 3 financial instruments were reported in the above tables as transfers into (out of) the Level 3 category at the end of each quarterly period in which the transfers occurred. The portion of net unrealized gains for the three month periods ended March 31, 2017 that related to Level 3 trading and available-for-sale securities still held at the reporting dates was $3.2 million in net gains. The portion of net unrealized gains and losses for the three month periods ended March 31, 2016 related to Level 3 trading and available-for-sale securities still held at the reporting dates was $4.3 million of net losses.

4. Fair Value Measurements (continued)

The following tables summarizes the fair values, the valuation techniques, and significant unobservable inputs of the Level 3 fair value measurements as of March 31, 2017 and December 31, 2016, for which we have been able to obtain quantitative information about the significant unobservable inputs used in those fair value measurements:

March 31, 2017

Assets (U.S. dollars in millions)	Fair Value	Valuation Technique	Significant Unobservable Inputs	Input Ranges
Corporate securities	$ 1,720	Discounted Cash Flow	Liquidity/duration adjustment*	1.1% - 1.5%
Mortgage and asset-backed securities	$ 10,121	Discounted Cash Flow	Liquidity/duration adjustment*	1.5% - 1.6%

December 31, 2016

Assets (U.S. dollars in millions)	Fair Value	Valuation Technique	Significant Unobservable Inputs	Input Ranges
Corporate securities	$ 1,761	Discounted Cash Flow	Liquidity/duration adjustment*	1.1% - 1.7%
Mortgage and asset-backed securities	$ 10,228	Discounted Cash Flow	Liquidity/duration adjustment*	1.5% - 1.6%

** The liquidity/duration adjustment input represents an estimated market participant composite interest spread that would be applied to the risk-free rate to discount the estimated projected cash flows for individual securities, and such liquidity/duration adjustment would reflect adjustments attributable to liquidity premiums, expected durations, credit structures, credit quality, etc., as applicable.*

We have excluded from the tables above Level 3 fair value measurements obtained from independent, third-party pricing sources, including prices obtained from brokers, for which we do not develop the significant inputs used to measure the fair values and information regarding the significant inputs is not readily available to us from the independent, third-party pricing sources or brokers.

Fair Value Measurements on a Non-Recurring Basis

As disclosed in this Note, the fair values of financial assets and liabilities are estimated in accordance with the framework established under FASB ASC 820. The methodology for determining the fair value of financial instruments on a non-recurring basis, in addition to the fair value of financial instruments on a recurring basis and to those disclosed above in Note 3, “Investments”, are described in Note 2, “Summary of Significant Accounting Policies - *Investments*”, and Note 5, “Fair Value Measurements” in the Company’s audited consolidated financial statements and accompanying notes thereto for the year ended December 31, 2016. The following table sets forth the fair values of our financial instruments, as of the dates indicated:

4. Fair Value Measurements (continued)

(U.S. dollars in thousands)	March 31, 2017 Carrying Balance	Level 1	Level 2	Level 3
		Estimated Fair Value		
Assets				
Cash and cash equivalents	$ 186,435	$ 186,435	$ -	$ -
Other investments	2,325	-	-	2,325
Funds withheld at interest	358,688	-	-	358,688
Accrued interest receivable	9,005	-	9,005	-
Liabilities				
Interest-sensitive contract liabilities	$ 752,678	$ -	$ -	$ 752,126
Collateral finance facility, excluding debt issuance costs	450,000	-	-	146,007
Embedded derivative liabilities, at fair value	13,282	-	-	13,282
Long-term debt, at par value	86,500	-	52,544	-

(U.S. dollars in thousands)	December 31, 2016 Carrying Balance	Level 1	Level 2	Level 3
		Estimated Fair Value		
Assets				
Cash and cash equivalents	$ 194,920	$ 194,920	$ -	$ -
Other investments	2,368	-	-	2,368
Funds withheld at interest	362,761	-	-	362,761
Accrued interest receivable	9,219	-	9,219	-
Liabilities				
Interest-sensitive contract liabilities	$ 765,610	$ -	$ -	$ 765,069
Collateral finance facility, excluding debt issuance costs	450,000	-	-	171,601
Embedded derivative liabilities, at fair value	15,640	-	-	15,640
Long-term debt, at par value	86,500	-	51,633	-

5. Collateral Finance Facility and Securitization Structure

Orkney Re II

Historical information regarding the Orkney Re II collateral finance facility and securitization structure is discussed in Note 7, "Collateral Finance Facility and Securitization Structure – *Orkney Re II*" in the Company's audited consolidated financial statements and accompanying notes thereto for the year ended December 31, 2016.

The following table reflects the significant balances included in the accompanying Consolidated Balance Sheets that were attributable to the Orkney Re II collateral finance facility and securitization structure providing collateral support to the Company:

5. Collateral Finance Facility and Securitization Structure (continued)

(U.S. dollars in thousands)	March 31, 2017	December 31, 2016
Assets		
Fixed-maturity investments held as available-for-sale securities, at fair value	$ 8,072	$ 8,072
Funds withheld at interest	377,555	376,623
Cash and cash equivalents	3,383	3,422
Embedded derivative assets	51,896	50,044
All other assets	5,822	5,211
Total assets	$ 446,728	$ 443,372
Liabilities		
Reserves for future policy benefits	$ 128,440	$ 130,106
Collateral finance facility, net of debt issuance costs	448,166	448,056
All other liabilities	81,717	78,030
Total liabilities	$ 658,323	$ 652,192

The assets listed in the foregoing table are subject to a variety of restrictions on their use, as set forth in and governed by the transaction documents for the Orkney Re II collateral finance facility and securitization structure. The total investments of the consolidated VIE disclosed in the accompanying Consolidated Balance Sheets include the deduction of the assets needed to satisfy future policy benefits, based on current projections ("economic reserves"). The following table provides a reconciliation of the aforementioned adjustments:

(U.S. dollars in thousands)	March 31, 2017	December 31, 2016
Fixed-maturity investments held as available-for-sale securities, at fair value	$ 8,072	$ 8,072
Funds withheld at interest	377,555	376,623
Cash and cash equivalents	3,383	3,422
Embedded derivative assets	51,896	50,044
Total investments	$ 440,906	$ 438,161
Less: Economic reserves	(158,062)	(159,945)
Total investments in consolidated VIE	$ 282,844	$ 278,216

The reinsurance liabilities of Orkney Re II have been eliminated from the Consolidated Balance Sheets.

Orkney Re II - Settlement of Litigation

On March 25, 2017, Orkney Re II agreed in principle to settle litigation brought by Assured, the guarantor of the Series A-1 Notes of Orkney Re II, in Assured's own right and in the right of Orkney Re II, against J.P. Morgan Investment Management, Inc. ("JPMIM"), the former investment manager of Orkney Re II, relating to the management of Orkney Re II's investment accounts, which were funded with the proceeds of the Orkney Re II Notes, as explained in Note 7, "Collateral Finance Facility and Securitization Structure" in the Company's audited consolidated financial statements and accompanying notes thereto for the year ended December 31, 2016.

5. Collateral Finance Facility and Securitization Structure (continued)

Assured, suing in its own right and on behalf of Orkney Re II, commenced litigation against JPMIM in the Supreme Court of the State of New York on or about May 13, 2009. The legal proceedings have been ongoing since 2009, and up until the date of the settlement of March 25, 2017, there was no assurances over the outcome of the litigation.

For further discussion on the Orkney Re II settlement of litigation, please refer to Note 11, "Subsequent Events - *Orkney Re II – Settlement of Litigation*".

Orkney Re II Event of Default, Acceleration, and Foreclosure

Orkney Re II has been unable to make scheduled interest payments on the Series A-1 Notes and Series A-2 Notes on all scheduled quarterly interest payment dates since May 11, 2009. As of March 31, 2017, Assured Guaranty (UK) Ltd. ("Assured") has made guarantee payments in the cumulative amount of $25.9 million on the Series A-1 Notes which are the subject of a financial guaranty policy issued by Assured in connection with the Orkney Re II transaction. Unlike the Series A-1 Notes, the Series A-2 Notes were not guaranteed under the Orkney Re II transaction and the amount of cumulative interest on the Series A-2 Notes was $3.9 million as of March 31, 2017. We have accrued this amount of cumulative interest on the Series A-1 Notes and the Series A-2 Notes in Accounts Payable and Other Liabilities in the Consolidated Balance Sheets. Interest on the Series A-1 Notes on which Assured is making guarantee payments is payable quarterly at a rate equivalent to three-month LIBOR plus 0.425%.

As of March 31, 2017, the interest rate on the Series A-1 Notes was 1.46% (compared to 1.31% as of December 31, 2016). Interest on the Series A-2 Notes, which are not guaranteed as part of the Orkney Re II transaction, is payable quarterly at a rate equivalent to three-month LIBOR plus 0.730%. As of March 31, 2017, the interest rate on the Series A-2 Notes was 1.76% (compared to 1.62% as of December 31, 2016). For further discussion on Orkney Re II and scheduled interest payments on the Series A-1 Notes and the Series A-2 Notes, please refer to Note 11, "Subsequent Events - *Orkney Re II – Scheduled Interest Payments*".

6. Debt Obligations and Other Funding Arrangements

Long-term debt, at par value (collectively, the "Capital and Trust Preferred Securities"), is individually defined and described in Note 8, "Debt Obligations and Other Funding Arrangements" in the notes accompanying the Company's audited consolidated financial statements for the year ended December 31, 2016. The pertinent details regarding long-term debt, at par value are shown in the following table:

(U.S. dollars in thousands)	Capital Securities Due 2032*	Preferred Trust Securities Due 2033*	Trust Preferred Securities Due 2033*	Trust Preferred Securities Due 2034*	Trust Preferred Securities Due December 2034*
Issuer of long-term debt	Capital Trust*	Capital Trust II*	GPIC Trust*	Capital Trust III*	SFL Trust I*
Long-term debt outstanding	$17,500	$nil**	$nil***	$19,000****	$50,000
Maturity date	Dec 4, 2032	Oct 29, 2033	Sept 30, 2033	June 17, 2034	Dec 15, 2034
Redeemable (in whole or in part) after	Dec 4, 2007	Oct 29, 2008	Sept 30, 2008	June 17, 2009	Dec 15, 2009
Interest Payable	Quarterly	Quarterly	Quarterly	Quarterly	Quarterly
Interest rate: 3-month LIBOR +	4.00%	3.95%	3.90%	3.80%	3.50%
Interest rate as of March 31, 2017	5.15%	5.10%	5.05%	4.95%	4.65%
Interest rate as of December 31, 2016	5.00%	4.95%	4.90%	4.80%	4.50%
Maximum number of quarters for which interest may be deferred	20	20	20	20	20
Number of quarters for which interest has been deferred as of March 31, 2017	17	17	17	17	17

* *Defined in the notes accompanying SRGL's audited consolidated financial statements for the year ended December 31, 2016.*
***SRGL owns all $20.0 million of the Preferred Trust Securities Due 2033 securities.*
****SRGL owns all $10.0 million of the Trust Preferred Securities Due 2033 securities.*
*****SRGL owns $13.0 million of the Trust Preferred Securities Due 2034 securities.*

Deferral of Interest Payments on the Capital and Trust Preferred Securities

We began deferring interest payments as of January 29, 2013 on the Capital and Trust Preferred Securities as permitted by the terms of the indentures governing the securities. As of March 31, 2017, we had accrued and deferred payments of $25.1 million in interest on the Capital and Trust Preferred Securities. Of these deferred payments, $8.6 million are attributable to SRGL, leaving a net amount of accrued deferred interest of $16.5 million on the Capital and Trust Securities due to external parties. SHI, SFL, and SALIC generally are restricted in their ability to make certain dividend payments and payments in respect of obligations ranking junior or *pari passu* to the Capital and Trust Preferred Securities in any period where interest payment obligations on these securities are not current.

For further discussion on the accrued and deferred payment on our Capital and Trust Preferred Securities subsequent to March 31, 2017, please refer to Note 11, "Subsequent Events – *Deferral of Interest Payments on the Capital and Trust Preferred Securities*".

7. Mezzanine Equity – Convertible Cumulative Participating Preferred Shares

On May 7, 2007, we completed the equity investment transaction by the Investors, announced by us on November 27, 2006 (the "2007 New Capital Transaction"). Pursuant to the 2007 New Capital Transaction, the

7. Mezzanine Equity – Convertible Cumulative Participating Preferred Shares (continued)

Investors invested an aggregate $600.0 million in the Company in exchange for 1,000,000, in the aggregate, newly-issued Convertible Cumulative Participating Preferred Shares (the “CCPP Shares”). Aggregate net proceeds of $555.9 million were received after payment of $44.1 million in closing costs. Each CCPP Share had a par value of $0.01 per share with an initial stated value and liquidation preference of $600 per share, as adjusted for the accretion of dividends or the payment of dividends or distributions as described further below.

The CCPP Shares were convertible at the option of the holder, at any time, into an aggregate of 150,000,000 ordinary shares (the “Ordinary Shares”) of SRGL. We accounted for the 2007 issuance of the CCPP Shares to the Investors, in accordance with FASB ASC Subtopic 470-20, Debt – Debt with Conversion and Other Options (“FASB ASC 470-20”), which incorporates EITF D-98: “Classification and Measurement of Redeemable Securities”. We were not required at any time to redeem the CCPP Shares for cash, except in the event of a liquidation or upon the occurrence of a change-in-control event.

On the ninth anniversary of issue, May 7, 2016, and in accordance with the CCPP Certificate of Designations, the CCPP Shares automatically converted into an aggregate of 150,000,000 Ordinary Shares of the Company.

We accounted for the conversion of the CCPP Shares in accordance with FASB ASC 470-20. As a result, and in accordance with the CCPP Certificate of Designations, the CCPP Shares were converted into an aggregate of 150,000,000 Ordinary Shares, with each Ordinary Share having a par value of $0.01, representing an additional $1.5 million in the Ordinary Shares amount in the Company's Consolidated Balance Sheets. The remaining balance of the CCPP Shares amount of approximately $554.4 million that was previously classified under Mezzanine Equity in the Consolidated Balance Sheets, and was over and above the Ordinary Share conversion amount of $1.5 million as described earlier, was reclassified to Additional Paid-in Capital (“APIC”).

The conversion of the CCPP Shares had no material impact on the results of operations of the Company and only impacted the Consolidated Balance Sheets and Consolidated Statements of Shareholders’ Equity.

The table below provides an illustration of the changes to the Company's Consolidated Balance Sheets during 2016 as follows:

	May 6, 2016	Adjustment	May 7, 2016
(U.S. dollars in thousands)			
Total Mezzanine Equity			
Total Mezzanine Equity	$ 555,857	$ (555,857)	$ -
Total Mezzanine Equity	$ 555,857	$ (555,857)	$ -
Equity			
Share Capital	$ 684	$ 1,500	$ 2,184
APIC	1,218,190	554,357	1,772,547
Share Capital & APIC	$ 1,218,874	$ 555,857	$ 1,774,731

8. Shareholders' Deficit

Ordinary Shares

We are authorized to issue 590,000,000 Ordinary Shares with a par value of $0.01 per share.

As of March 31, 2017 and December 31, 2016, we had 218,383,370 Ordinary Shares issued and outstanding.

Perpetual Preferred Shares

We are authorized to issue 50,000,000 preferred shares with a par value of $0.01 per share.

In 2005, we issued 5,000,000 non-cumulative Perpetual Preferred Shares (the "Perpetual Preferred Shares"). Gross proceeds were $125 million, and related expenses were $4.6 million. As of March 31, 2017, we have repurchased and cancelled 1,753,224 Perpetual Preferred Shares. As of March 31, 2017 and December 31, 2016, we had 3,246,776 Perpetual Preferred Shares issued and outstanding.

The dividend rate on the Perpetual Preferred Shares may be at a fixed rate determined through remarketing of the Perpetual Preferred Shares for specific periods of varying length not less than six months or may be at a floating rate reset quarterly based on a predefined set of interest rate benchmarks. The quarterly floating rates for March 31, 2017 and 2016 were 6.39% and 6.09% respectively. During any dividend period, unless the full dividends for the current dividend period on all outstanding Perpetual Preferred Shares have been declared or paid, no dividend may be paid or declared on the Ordinary Shares and no Ordinary Shares or other junior shares may be purchased, redeemed, or otherwise acquired for consideration by SRGL. Please refer below to "*Dividends on Perpetual Preferred Shares*" in the Note below for additional information.

Dividends on Ordinary Shares

The Investors, as the holders of the Ordinary Shares, are entitled to receive dividends and are allowed one vote per share subject to certain restrictions in our Memorandum and Articles of Association.

All future payments of dividends are at the discretion of our Board and will depend on such factors as the Board may deem relevant. Notwithstanding the foregoing, if dividends on the Perpetual Preferred Shares have not been declared and paid (or declared and a sum sufficient for the payment thereof set aside) for a dividend period, we generally are precluded from paying or declaring any dividend on the Ordinary Shares.

Dividends on Perpetual Preferred Shares

In accordance with the relevant financial tests under the terms of the Perpetual Preferred Shares, our Board was precluded from declaring and paying a dividend in connection with the January 15, April 15, and July 15, 2016 dividend payment dates.

In accordance with the relevant financial tests under the terms of the Perpetual Preferred Shares, our Board was permitted to declare and pay a dividends for the October 15, 2016 payment date and the January 15, 2017 payment date. Our Board resolved, in its discretion, not to declare and pay a dividend on the Perpetual Preferred Shares on the October 15, 2016 and the January 15, 2017 dividend payment dates.

There can be no assurances when or whether, as a result of the application of the financial tests contained in the terms of the Perpetual Preferred Shares, our Board will be permitted to make subsequent dividend payments on the Perpetual Preferred Shares or, if permitted, when or whether our Board will choose in its discretion to make any such dividend payments on the Perpetual Preferred Shares. For further discussion on the non-declaration of the

8. Shareholders' Deficit (continued)

Perpetual Preferred Shares dividends, please refer to Note 11, "Subsequent Events – *Non-declaration of Dividend on Perpetual Preferred Shares*".

Perpetual Preferred Shares – Right to Appoint Directors

Pursuant to the terms of, and subject to the procedures set forth in, the Certificate of Designations related to the Perpetual Preferred Shares (the "PPS Certificate of Designations"), the holders of the Perpetual Preferred Shares are entitled to elect two directors to our Board in the event dividends on the Perpetual Preferred Shares have not been declared and paid for six or more dividend periods, whether or not consecutive (a "Nonpayment"). Failure to declare and pay dividends on the July 15, 2009 dividend payment date marked the sixth dividend period for which dividends had not been declared and paid (i.e., a Nonpayment).

If and when dividends for at least four dividend periods, whether or not consecutive, following a Nonpayment have been paid in full, this right will cease.

9. Income Taxes

There was no income tax expense or benefit for the three month period ended March 31, 2017. The income tax expense for the three month period ended March 31, 2016 was $0.2 million. Any net incomes from the operations of our Cayman Island entities are not subject to income tax. The operations of our U.S., Bermuda, and Irish entities did not generate a current tax expense due to the operating performance and the availability of tax losses from prior tax years. The utilization of tax losses results in a reduction in deferred tax assets and a corresponding reduction in the valuation allowance established against those deferred tax assets. The income tax expense for the three period ended March 31, 2016 were due to an increase of the deferred tax liability for items reversing outside of the 15 year net operating loss carry-forward period in the U.S.

As of March 31, 2017, we had total unrecognized tax benefits (excluding interest and penalties) of $1.5 million, the recognition of which is not expected to create a tax benefit at the effective tax rate for the applicable period. The total unrecognized tax benefits figure (excluding interest and penalties) and the resulting tax benefit recognition figure were unchanged from March 31, 2017 and December 31, 2016.

As of March 31, 2016, we had total unrecognized tax benefits (excluding interest and penalties) of $1.5 million, the recognition of which is not expected to create a tax benefit at the effective tax rate for the applicable period. The total unrecognized tax benefits figure (excluding interest and penalties) and the resulting tax benefit recognition figure changed from March 31, 2016 and December 31, 2015 due to the expiration of the statute of limitations for a portion of the unrecognized tax benefits.

Our deferred tax assets are principally supported by the reversal of deferred tax liabilities. We currently establish a valuation allowance against deferred tax assets when it is more likely than not that some portion, or all, of our deferred tax assets will not be realized. We have maintained a full valuation allowance against any remaining deferred tax asset associated with our operations in the U.S. and Ireland, given our inability to rely on future taxable income projections and the scheduling of our current deferred tax liabilities.

As of March 31, 2017 and December 31, 2016, the projections of GAAP life insurance reserves no longer provide for deferred tax liabilities that reverse after the expiration of net operating loss carryforwards in applicable jurisdictions. Therefore, a scheduled deferred tax liability, in excess of the established valuation allowance, has not been recorded as of March 31, 2017 and December 31, 2016.

9. Income Taxes (continued)

We file our tax returns as prescribed by the tax laws of the jurisdictions in which we operate. As of March 31, 2017, we remained subject to examination in the following major tax jurisdictions for the returns filed for the years indicated below:

Major Tax Jurisdictions	Open Years
U.S.	
Life Group	2013 through 2015
Non-Life Group	2013 through 2015
Ireland	2012 through 2015

Our U.S. subsidiaries are subject to U.S. federal and state corporate income taxes and other taxes applicable to U.S. corporations. Upon distribution of current or accumulated earnings and profits in the form of dividends or otherwise from our U.S. subsidiaries to us, we would be subject to U.S. withholding taxes at a 30% rate.

Net operating losses are being carried forward from closed years and could be examined by the applicable tax authorities if utilized in an open tax year in the future. Additionally, to the extent that a net operating loss is carried back to an otherwise closed year, that earlier year could be subject to examination as long as the loss year remains open.

10. Commitments and Contingencies

Ballantyne Re plc

Ballantyne Re plc (“Ballantyne Re”), which previously was a consolidated VIE of the Company, is a special purpose reinsurance vehicle incorporated under the laws of Ireland. In May 2006, Ballantyne Re issued, in a private offering, $1.74 billion of debt to third party investors, $178.0 million of Class C Notes to SALIC, $181.2 million in preference shares to SALIC, and $500,000 in Class D Notes to SRGL.

We have no remaining direct loss exposure related to Ballantyne Re since our interests in the Ballantyne Re Class D Notes and Preferred Shares are valued at $0. The Class C Notes were fully written-off in 2008 under the contractual terms of the Ballantyne Re indenture.

SRUS remains liable for the accuracy and performance of certain representations, warranties, covenants, and other obligations that relate to periods before the assignment and novation to Security Life of Denver Insurance Company of the reinsurance agreement with Ballantyne Re. In addition, SRGL and SRUS remain responsible for certain ongoing covenants and indemnities made for the benefit of Ballantyne Re and the financial guarantors of certain of the notes issued by Ballantyne Re.

Indemnification of Our Directors, Officers, Employees, and Agents

We indemnify our directors, officers, employees, and agents against any action, suit, or proceeding, whether civil, criminal, administrative, or investigative, by reason of the fact that they are our director, officer, employee, or agent, as provided in our Articles of Association. Since this indemnity generally is not subject to limitation with respect to duration or amount, we do not believe that it is possible to determine the maximum potential amount due under this indemnity in the future.

10. Commitments and Contingencies (continued)

Davis v. Scottish Re Group Limited, et al.

SRGL and SRUS (together, "Scottish Re") learned that a lawsuit was filed on or about November 20, 2013, in New York state court against Scottish Re, SRGL's shareholders and certain of their affiliates, and various former and current directors of Scottish Re (collectively, the "Defendant Parties"). The plaintiff, identified in the court documents as a holder of Perpetual Preferred Shares and a former holder of Ordinary Shares (please refer to Note 8, "Shareholders' Deficit" for information regarding the Perpetual Preferred Shares and the Ordinary Shares), alleges, among other things, claims against the Defendant Parties for breach of contract, breach of fiduciary duty, tortious interference, and derivative claims centered largely around the following events:

- the 2011 unwind of a formerly consolidated collateral finance facility and the associated acquisition by Cerberus affiliates of debt related to the collateral finance facility;
- the completion in 2011 of a cash-out merger between SRGL and affiliates of the Investors;
- the cancellation by SRGL of Perpetual Preferred Shares acquired pursuant to cash tender offers made by SRGL in 2010 and 2012; and
- a purported distribution policy affecting the Perpetual Preferred Shares.

On February 21, 2014, Motions to Dismiss were filed with the court on behalf of the Defendant Parties pursuant to a briefing schedule previously agreed with the court and the plaintiff. Pursuant to that schedule, the plaintiff submitted on May 7, 2014 its opposition to the Motions to Dismiss. The Defendant Parties submitted replies in further support of their Motions to Dismiss on June 23, 2014. Oral arguments on the Motions to Dismiss were heard by the court on September 29, 2014.

Following oral arguments on the Motions to Dismiss on September 29, 2014, on October 7, 2014, the presiding judge issued a decision dismissing all claims against the Defendant Parties, with the exception of two breach of contract claims against SRGL. The judge directed that the plaintiff and SRGL engage in jurisdictional discovery limited to these two claims, after which the court would decide whether these claims should also be dismissed on jurisdictional grounds.

The plaintiff filed on October 28, 2014 his opening appellate brief challenging the court's October 7, 2014 decision. Following this, Scottish Re and the other Defendant Parties filed opposition briefs, and the plaintiff thereafter filed his reply brief. Oral arguments on the appellate brief were heard by the Appellate Division of the New York Supreme Court on June 9, 2015.

Jurisdictional discovery commenced on the two breach of contract claims concluded on October 26, 2015. Thereafter, the Company filed with the court its renewed Motion to Dismiss in respect of the two remaining claims. Pursuant to the schedule agreed with the court, the plaintiff's brief opposing the Motion to Dismiss was filed with the court on November 25, 2015 and the Company's reply was filed on December 16, 2015. A hearing on the Company's renewed Motion to Dismiss was held with the trial court on January 26, 2016.

On March 10, 2016, the appellate court issued a decision on the plaintiff's appeal argued before it on June 9, 2015, relating to the trial court's previous dismissal of eight of the ten claims originally brought by the plaintiff in this case. The appellate court's majority decision (representing three of the five justices) affirmed the trial court's dismissal of all but two of the claims on appeal against all defendants. With respect to the remaining claims, the appellate court remanded the matter to the trial court to allow the plaintiff to re-plead two breach of fiduciary duty claims against the three Directors of SRGL who remain in the case (the "Director Defendants"). The two dissenting justices would have affirmed the dismissal of all claims on appeal.

10. Commitments and Contingencies (continued)

On April 25, 2016, the plaintiff filed a motion with appellate court, seeking permission to appeal the dismissal of three derivative breach of fiduciary duty claims to the New York Court of Appeals. On May 12, 2016, the Director Defendants who remain in the case and SRGL's shareholders and certain of their affiliates filed an opposition brief to plaintiff's motion. On May 18, 2016, the plaintiff filed a reply brief in further support of his motion.

Notwithstanding the appellate court's March 10, 2016 decision remanding the matter to the trial court to allow the plaintiff to replead only two breach of fiduciary duty claims against the remaining Director Defendants, on May 3, 2016, the plaintiff filed an amended complaint with the trial court in which the plaintiff repleaded eight of the original ten claims, removing two of the original claims and adding a new claim against certain of the Defendant Parties. On June 7, 2016, the Director Defendants filed a Motion to Dismiss the repleaded breach of fiduciary duty claims. On July 14, 2016, the plaintiff filed his response to the Director Defendants' Motion to Dismiss the repleaded breach of fiduciary duty claims. The reply brief of the Director Defendants was filed on August 5, 2016. Oral arguments for the Director Defendant's Motion to Dismiss the repleaded breach of fiduciary duty claims were held on November 7, 2016. The trial court has not yet issued a decision on the Motion.

On July 7, 2016, the appellate court granted plaintiff's motion for leave to appeal the dismissal of the three derivative breach of fiduciary duty claims to the New York Court of Appeals. On September 27, 2016, the plaintiff filed his opening brief in the New York Court of Appeals. The response brief by the Director Defendants who remain in the case and SRGL's shareholders and certain of their affiliates was filed on November 17, 2016. The plaintiff's reply brief was filed on December 5, 2016. Oral argument has not yet been scheduled.

On July 11, 2016, the trial court issued a ruling that dismissed one of the two breach of contract claims. The plaintiff did not file an interlocutory appeal from the dismissal prior to the deadline for doing so. The plaintiff has not pursued discovery on the remaining claim.

Scottish Re has certain obligations to indemnify those Defendant Parties who are current or former directors for the reasonable cost of their defense of the Davis lawsuit.

We believe the plaintiff's allegations to be without merit and are vigorously defending our interest in the action. Accordingly, it is not possible to estimate any loss in respect of the plaintiff's claims.

For further discussion regarding the Davis v. Scottish Re Group Limited, et al. litigation, please refer to Note 11, "Subsequent Events – *Commitments and Contingencies – Davis v. Scottish Re Group Limited, et al.*".

Other Contingencies

On January 20, 2016, SRUS initiated an arbitration proceeding against a third-party ceding company related to a dispute regarding the applicable premium tables and other related claims in respect of certain business ceded to SRUS from the third-party ceding company. The arbitration hearing is scheduled for the last week of June 2017.

On April 22, 2016, SRUS initiated an arbitration proceeding against a third-party ceding company seeking among other things, the enforcement of certain premium calculations under various YRT Reinsurance Agreements between the third-party ceding company and SRUS, as well as rescission of some YRT Reinsurance Agreements based upon misrepresentations and mismanagement by the third-party ceding company. On September 30, 2016, SRUS sent a notice to the third-party ceding company that SRUS was terminating the reinsurance for non-payment of premiums pursuant to the terms of the YRT Reinsurance Agreements. On October 20, 2016, SRUS received a counter-demand to the arbitration demand from the third-party ceding company alleging certain issues relating to premium calculation and certain claims ceded to SRUS. The parties expect that the final hearing will be held late 2017 or early 2018.

10. Commitments and Contingencies (continued)

For further discussion regarding the arbitration initiated on April 22, 2016, please refer to Note 11, "Subsequent Events – *Commitments and Contingencies – Other Contingencies*".

On October 6, 2016, SRUS received an arbitration demand from a third-party ceding company related to a YRT Reinsurance Agreement. The arbitration demand alleges certain issues relating to premium calculation and certain claims ceded to the Company. On October 21, 2016, SRUS responded to the arbitration demand, denying each of the allegations. SRUS also served a counter-demand on the third-party ceding company seeking, among other things, rescission of the YRT Reinsurance Agreement based upon misrepresentations and mismanagement by the third-party ceding company, and the enforcement of certain premium calculations under the YRT Reinsurance Agreement. The parties are in the process of selecting an arbitration panel.

For further discussion regarding the arbitration initiated on October 6, 2016, please refer to Note 11, "Subsequent Events – *Commitments and Contingencies – Other Contingencies*".

11. Subsequent Events

The subsequent events disclosed in these notes to the consolidated financial statements have been evaluated by Company management up to and including the filing of these consolidated financial statements on June 12, 2017.

Orkney Re II - Settlement of Litigation

Orkney Re II finalized the settlement litigation documentation, as disclosed in Note 5, "Collateral Finance Facility and Securitization Structure – *Orkney Re II - Settlement of Litigation*", and received $74.4 million in cash on April 17, 2017, in return for releases of all claims by Orkney Re II and Assured in the litigation. Neither SRGL or its consolidated subsidiaries are direct beneficiaries to any part of this settlement of litigation amount that Orkney Re II has received.

Orkney Re II – Scheduled Interest Payments

On the scheduled interest payment date of May 11, 2017, Orkney Re II was unable to make scheduled interest payments on the Series A-1 Notes and the Series A-2 Notes. As a result, and pursuant to the financial guaranty policy issued by Assured (as discussed in Note 5, "Collateral Finance Facility and Securitization Structure – *Orkney Re II Event of Default, Acceleration, and Foreclosure*"), Assured made guarantee payments on the Series A-1 Notes in the amount of $1.4 million. The unpaid interest amount for the Series A-2 Notes, which was not guaranteed under the Orkney Re II transaction, was $0.2 million. We have accrued the interest on both the Series A-1 Notes and the Series A-2 Notes.

Deferral of Interest Payments on the Capital and Trust Preferred Securities

We continued to accrue and defer payments of interest on our Capital and Trust Preferred Securities (as outlined in Note 6, "Debt Obligations and Other Funding Arrangements"). These deferrals are permitted by terms of the indentures governing the Capital and Trust Preferred Securities and have been made at the discretion of our Board. As of June 12, 2017, we had accrued and deferred payments on a total of $25.4 million of interest on our Capital and Trust Preferred Securities. Of these deferred payments, $8.9 million are attributable to SRGL, leaving a net amount of accrued deferred interest of $16.5 million on the Capital and Trust Securities due to external parties.

Non-declaration of Dividends on Perpetual Preferred Shares

Our Board resolved, in its discretion, not to declare and pay a dividend on the Perpetual Preferred Shares on the April 15, 2017 dividend payment date.

11. Subsequent Events (continued)

Commitments and Contingencies

Davis v. Scottish Re Group Limited, et al.

The trial court had scheduled a status conference for April 18, 2017, but this has been postponed to June 27, 2017.

Other Contingencies

For the arbitration initiated on April 22, 2016, the parties have tentatively agreed to a final hearing date during the week of February 5, 2018.

For the arbitration initiated on October 6, 2016, the parties have selected an arbitration panel. An organizational meeting was held on May 9, 2017, at which time the parties agreed to a final hearing date beginning on March 12, 2018.

Going Concern

On May 17, 2017, SRGL commenced voluntary provisional winding up proceedings in Bermuda (where SRGL has its principal executive office is located) and filed for parallel winding up proceedings in the Cayman Islands (where SRGL is incorporated).

In connection with the Bermuda proceedings, on May 18, 2017, the Supreme Court of Bermuda granted an order appointing personnel from Finance & Risk Services Ltd. of Bermuda and Kalo (Cayman) Limited of the Cayman Islands as Joint Provisional Liquidators ("JPLs") of SRGL. As such, these JPLs will work with our Board and management to effectuate a restructuring plan for SRGL, which may involve the sale of SRGL's immediate subsidiary, SALIC. SRGL pro-actively filed these winding up petitions in an effort to facilitate the restructuring process and to maximize value to its stakeholders.