Enstar Group LTD
Form 10-K
February 27, 2017

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K
ANNUAL
REPORT
PURSUANT
TO
SECTION 13
OR 15(d) OF
THE
SECURITIES
EXCHANGE
ACT OF 1934
For the fiscal year ended December 31, 2016
Commission File Number 001-33289

ENSTAR GROUP LIMITED
(Exact name of Registrant as specified in its charter)

BERMUDA	N/A
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

Windsor Place, 3rd Floor, 22 Queen Street, Hamilton HM JX, Bermuda
(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: (441) 292-3645

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

Title of Each Class	Name of Each Exchange on Which Registered
Ordinary shares, par value $1.00 per share	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act: None

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

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

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 ý No ¨

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ý

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer ý Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company ¨

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

The aggregate market value of the registrant's voting and non-voting common equity held by non-affiliates as of June 30, 2016 was approximately $1.59 billion based on the closing price of $161.99 per ordinary share on the NASDAQ Stock Market on that date. Shares held by officers and directors of the registrant and their affiliated entities have been excluded from this computation. Such exclusion is not intended, nor shall it be deemed, to be an admission that such persons are affiliates of the registrant.

As of February 23, 2017, the registrant had outstanding 16,419,889 voting ordinary shares and 3,004,443 non-voting convertible ordinary shares, each par value $1.00 per share.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A relating to its 2017 annual general meeting of shareholders are incorporated by reference in Part III of this Form 10-K.

Enstar Group Limited
Annual Report on Form 10-K
For the Fiscal Year Ended December 31, 2016

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This annual report and the documents incorporated by reference contain statements that constitute "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act, with respect to our financial condition, results of operations, business strategies, operating efficiencies, competitive positions, growth opportunities, plans and objectives of our management, as well as the markets for our ordinary shares and the insurance and reinsurance sectors in general. Statements that include words such as "estimate," "project," "plan," "intend," "expect," "anticipate," "believe," "would," "should," "could," "seek," "may" and similar statements of a future or forward-looking nature identify forward-looking statements for purposes of the federal securities laws or otherwise. All forward-looking statements are necessarily estimates or expectations, and not statements of historical fact, reflecting the best judgment of our management and involve a number of risks and uncertainties that could cause actual results to differ materially from those suggested by the forward-looking statements. These forward looking statements should, therefore, be considered in light of various important factors, including those set forth in this annual report and the documents incorporated by reference, which could cause actual results to differ materially from those suggested by the forward looking statements. These factors include:

- risks associated with implementing our business strategies and initiatives;
- risks that we may require additional capital in the future, which may not be available or may be available only on unfavorable terms;
- the adequacy of our loss reserves and the need to adjust such reserves as claims develop over time;
- risks relating to the availability and collectability of our reinsurance;
- changes and uncertainty in economic conditions, including interest rates, inflation, currency exchange rates, equity markets and credit conditions, which could affect our investment portfolio, our ability to finance future acquisitions and our profitability;
- the risk that ongoing or future industry regulatory developments will disrupt our business, affect the ability of our subsidiaries to operate in the ordinary course or to make distributions to us, or mandate changes in industry practices in ways that increase our costs, decrease our revenues or require us to alter aspects of the way we do business;
- losses due to foreign currency exchange rate fluctuations;
- increased competitive pressures, including the consolidation and increased globalization of reinsurance providers;
- emerging claim and coverage issues;
- lengthy and unpredictable litigation affecting assessment of losses and/or coverage issues;
- loss of key personnel;
- the ability of our subsidiaries to distribute funds to us and the resulting impact on our liquidity;
- our ability to comply with covenants in our debt agreements;
- changes in our plans, strategies, objectives, expectations or intentions, which may happen at any time at management’s discretion;
- operational risks, including system, data security or human failures and external hazards;
- risks relating to our acquisitions, including our ability to continue to grow, successfully price acquisitions, evaluate opportunities, address operational challenges, support our planned growth and assimilate acquired companies into our internal control system in order to maintain effective internal controls, provide reliable financial reports and prevent fraud;
- risks relating to our ability to obtain regulatory approvals, including the timing, terms and conditions of any such approvals, and to satisfy other closing conditions in connection with our acquisition agreements, which could affect our ability to complete acquisitions;

- risks relating to our active underwriting businesses, including unpredictability and severity of catastrophic and other major loss events, failure of risk management and loss limitation methods, the risk of a ratings downgrade or withdrawal, cyclicality of demand and pricing in the insurance and reinsurance markets;
- our ability to implement our strategies relating to our active underwriting businesses;
- risks relating to our life and annuities business, including mortality and morbidity rates, lapse rates, the performance of assets to support the insured liabilities, and the risk of catastrophic events;
- risks relating to our investments in life settlements contracts, including that actual experience may differ from our assumptions regarding longevity, cost projections, and risk of non-payment from the insurance carrier;
- risks relating to our subsidiaries with liabilities arising from legacy manufacturing operations;
- risks relating to the performance of our investment portfolio and our ability to structure our investments in a manner that recognizes our liquidity needs;
- tax, regulatory or legal restrictions or limitations applicable to us or the insurance and reinsurance business generally;
- changes in tax laws or regulations applicable to us or our subsidiaries, or the risk that we or one of our non-U.S. subsidiaries become subject to significant, or significantly increased, income taxes in the United States or elsewhere;
- changes in Bermuda law or regulation or the political stability of Bermuda; and
- changes in accounting policies or practices.

The factors listed above should be not construed as exhaustive and should be read in conjunction with the Risk Factors that are included in Item 1A below. We undertake no obligation to publicly update or review any forward looking statement, whether to reflect any change in our expectations with regard thereto, or as a result of new information, future developments or otherwise, except as required by law.

PART I

ITEM 1. BUSINESS

Company Overview

Enstar Group Limited ("Enstar") is a Bermuda-based holding company, formed in 2001. Enstar is a multi-faceted insurance group that offers innovative capital release solutions and specialty underwriting capabilities through its network of group companies in Bermuda, the United States, the United Kingdom, Continental Europe, Australia, and other international locations. Enstar is listed on the NASDAQ Global Select Market under the ticker symbol "ESGR". In this report, the terms "Enstar," "the Company," "us," and "we" are used interchangeably to describe Enstar and our subsidiary companies.

Our fundamental corporate objective is growing our net book value per share. We strive to achieve this primarily through growth in net earnings from both organic and accretive sources, including the completion of new acquisitions, the effective management of companies and portfolios of business acquired, and the execution of active underwriting strategies.

Enstar acquires and manages insurance and reinsurance companies and portfolios of insurance and reinsurance business in run-off. Since formation, we have completed the acquisition of over 75 insurance and reinsurance companies and portfolios of business.

Enstar also manages specialty active underwriting businesses:

- Atrium Underwriting Group Limited and its subsidiaries ("Atrium"), which manage and underwrite specialist insurance and reinsurance business for Lloyd’s Syndicate 609; and
- StarStone Insurance Bermuda Limited and its subsidiaries ("StarStone"), which is an A.M. Best A- rated global specialty insurance group with multiple underwriting platforms.

Business Strategy

Enstar aims to maximize growth in net book value per share by employing the following strategies:

We Leverage Management’s Experience and Industry Relationships to Solidify Enstar’s Position in the Run-Off Market. Enstar leverages the extensive experience and relationships of our senior management team to solidify our position as a leading run-off acquirer and generate future growth opportunities.

We Engage in Highly Disciplined Acquisition, Management and Reinsurance Practices across a Diverse Portfolio of Loss Reserves. Enstar employs a disciplined approach when assessing and acquiring portfolios of risk, which we believe minimizes risk and increases the probability of delivering positive operating results from the companies and portfolios acquired. Enstar is highly selective in reviewing potential acquisition targets. When considering any acquisition we carefully analyze the target’s risk exposures, claims practices and reserve requirements.

We Aim to Profitably Underwrite Selected Specialty Lines to Enhance Future Growth Opportunities. Through our Atrium and StarStone segments, Enstar selectively underwrites in chosen specialty lines, with a focus on balancing risk exposures. Through Atrium and StarStone, the group’s underwriting activity grows organically; and when Enstar acquires run-off businesses, the group’s active underwriting companies are well-positioned to capture profitable active business in specialty lines previously identified as attractive.

We Manage Claims Professionally, Expeditiously, and Cost-Effectively. Enstar aims to manage claims made against group companies and portfolios in a professional and disciplined manner, drawing on in-house expertise to dispose of claims efficiently. Enstar strives to pay valid claims on a timely basis, while relying on well-documented policy terms and exclusions where applicable, and litigation when necessary, to defend against paying invalid claims.

We Seek to Commute Assumed Liabilities and Insurance and Reinsurance Assets at a Discount to the Ultimate Liability. Using detailed claims analysis and actuarial projections, Enstar seeks to negotiate with policyholders in the non-life run-off insurance and reinsurance companies or portfolios that we own with a goal of commuting existing insurance and reinsurance liabilities at a discount to the ultimate liability.

We Prudently Manage Investments and Capital. In managing investments and deploying group capital, Enstar strives to achieve superior risk-adjusted returns, while growing profitability and generating long-term growth in shareholder value.

Strategic Growth

Enstar transactions typically take the form of either acquisitions or portfolio transfers. In an acquisition, we acquire an insurance or reinsurance company and manage the run-off or continued underwriting of risk in its business lines. In a portfolio transfer, a reinsurance contract transfers risk from the initial insurance or reinsurance company to a company in the Enstar group. Enstar also enters into reinsurance to close ("RITC") transactions with Lloyd's of London ("Lloyd's") insurance and reinsurance syndicates in run-off, whereby a portfolio of run-off liabilities is transferred from one Lloyd's syndicate to another.

The substantial majority of Enstar's acquisitions have been in the non-life run-off business, which generally includes property and casualty, workers' compensation, asbestos and environmental, construction defect, marine, aviation and transit, and other closed business. Enstar also owns closed life and annuities businesses.

Enstar evolved from a stand-alone run-off consolidator to a more diversified insurance group with active underwriting capabilities following our acquisitions of Atrium and StarStone, in 2013 and 2014, respectively. We had several rationales for acquiring Atrium and StarStone:

- Atrium's and StarStone's underwriting businesses provide Enstar with a more diversified earnings stream, which reduces the impact of volatility in earnings from non-life run-off businesses, while concurrently offering the group new growth avenues.
- We believe that having active underwriting businesses enhances the group's overall ability to compete for new acquisition targets because the addition of active underwriting capabilities allows the group to acquire renewal rights or provide loss portfolio reinsurance in connection with such acquisitions. These capabilities can attract certain vendors, and may provide Enstar with additional flexibility in structuring proposed transactions.
- Having both run-off and active underwriting businesses within our group allows Enstar to evaluate an acquisition target not only for its fundamental run-off potential, but also for the ongoing value of its profitable business lines.

We partnered with the Trident V funds ("Trident") (managed by Stone Point Capital LLC) in the acquisitions of the active underwriting businesses. Stone Point Capital is a financial services-focused private equity firm that has significant experience investing in insurance and reinsurance companies and other insurance-related businesses, which Enstar believes is valuable in our active underwriting joint ventures.

In each of the Atrium and StarStone transactions, Enstar has a 59.0% equity interest, Trident has a 39.3% equity interest, and Dowling Capital Partners, L.P. ("Dowling") has a 1.7% equity interest.

Recent Acquisitions and Significant New Business

RSA

On February 7, 2017, we entered into an agreement to reinsure U.K. employers' liability legacy business of RSA Insurance Group PLC ("RSA"). Pursuant to the transaction, our subsidiary will assume gross insurance reserves of approximately £957 million (approximately $1.2 billion), relating to 2005 and prior year business. Net insurance reserves are approximately £834 million (approximately $1.0 billion) and the reinsurance premium payable to Enstar's subsidiary is £799 million (approximately $1.0 billion). The transaction is subject to finalizing and effecting certain security arrangements.

Following the initial reinsurance transaction, which will transfer the economics of the portfolio up to the policy's limits, we and RSA will pursue a portfolio transfer of the business under Part VII of the Financial Services and Markets Act 2000, which would provide legal finality for RSA's obligations. The transfer is subject to court, regulatory and other approvals.

QBE

On January 11, 2017, we announced the closing of a transaction to reinsure multi-line property and casualty business of QBE Insurance Group Limited ("QBE"). Our subsidiary assumed gross reinsurance reserves of approximately $919 million (net reserves of $444 million) relating to the portfolio, which primarily includes workers' compensation, construction defect, and general liability discontinued lines of business. In addition our subsidiary has pledged a portion of the premium as collateral to a subsidiary of QBE, and we have provided additional collateral and a limited parental guarantee.

Dana Companies
On December 30, 2016, we acquired Dana Companies, LLC ("Dana Companies") from Dana Incorporated for a total purchase price of $88.5 million. Dana Companies holds liabilities associated with personal injury asbestos claims and environmental claims arising from its legacy automotive thermal-management manufacturing operations. Dana Companies' assets include, among others, insurance rights related to coverage against these liabilities and marketable securities. We financed the transaction through a draw on our revolving credit facility.
Shelbourne RITC Transaction
On November 15, 2016, we entered into a RITC transaction of the 2007 and prior underwriting years of account of a Lloyd’s syndicate managed by Neon Underwriting Limited (formerly Marketform), under which we assumed total net insurance reserves of £121.5 million ($158.0 million) for cash consideration of an equal amount.
Coca-Cola
On August 5, 2016, we entered into a reinsurance transaction with The Coca-Cola Company and its subsidiaries (“Coca-Cola”) pursuant to which we reinsured certain of Coca-Cola’s retention and deductible risks under its subsidiaries’ U.S. workers’ compensation, auto liability, general liability, and product liability insurance coverage. We assumed total gross reserves of $108.8 million, received total assets of $101.3 million and recorded a deferred charge of $7.5 million, included in other assets. We have transferred $108.8 million into a trust to support our obligations under the reinsurance agreements. We provided a limited parental guarantee, subject to an overall maximum of $27.0 million.
Allianz SE
On March 31, 2016, we completed a transaction with Allianz SE ("Allianz") to reinsure portfolios of Allianz's run-off business. Pursuant to the reinsurance agreement, our subsidiary has reinsured 50% of certain portfolios of workers' compensation, construction defect, and asbestos, pollution, and toxic tort business originally held by Fireman's Fund Insurance Company, and in the process assumed net reinsurance reserves of $1.1 billion. Affiliates of Allianz retained $1.1 billion of reinsurance premium as funds withheld collateral for the obligations of our subsidiary under the reinsurance agreement and we transferred $110.0 million to a reinsurance trust to further support our subsidiary's obligations. We have also provided a limited parental guarantee, which is subject to a maximum cap. The combined monetary total of the initial support offered by us through the trust and parental guarantee is capped at $270.0 million. In addition to the reinsurance transaction described above, we have entered into a consulting agreement with San Francisco Reinsurance Company, an affiliate of Allianz, with respect to the entire $2.2 billion portfolio, including the 50% share retained by affiliates of Allianz.
The tables below set forth summaries of acquisitions and significant new business in excess of $50 million in acquired assets that we have signed or completed since January 1, 2016. For a more detailed explanation of these transactions, as well as transactions completed in 2015 and 2014, refer to "Note 3 - Acquisitions" and "Note 4 - Significant New Business" in the notes to our consolidated financial statements included within Item 8 of this Annual Report on Form 10-K.
Acquisitions (January 1, 2016 - Present)

Company Name	Purchase Price	Assets Acquired	Liabilities Acquired	Goodwill	Segment	Primary Nature of Business
Dana Companies, LLC	$88.5 million	$329.3 million	$240.8 million	Nil	Non-life Run-off	Liabilities associated with personal injury asbestos claims and environmental claims arising from legacy manufacturing operations

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Significant New Business (January 1, 2016 - Present)

Company Name	Purchase Price	Assets Acquired	Liabilities Acquired	Deferred Charge	Segment	Primary Nature of Business
RSA Insurance Group PLC	N/A	$1.2 billion	$1.2 billion	Nil	Non-life Run-off	U.K. employers' liability
QBE Insurance Group Limited	N/A	$0.9 billion	$0.9 billion	Nil	Non-life Run-off	U.S. workers' compensation, construction defect, and general liability
Neon (formerly Marketform)	N/A	$158.0 million	$158.0 million	Nil	Non-life Run-off	Italian medical malpractice
The Coca-Cola Company	N/A	$101.3 million	$108.8 million	$7.5 million	Non-life Run-off	U.S. workers' compensation, auto liability, general liability, and product liability
Allianz SE	N/A	$1.1 billion	$1.1 billion	Nil	Non-life Run-off	U.S. workers' compensation, construction defect, asbestos, pollution and toxic tort

Business Held for Sale

Pavonia

On February 17, 2017, we entered into a definitive agreement to sell Pavonia Holdings (US) Inc. and its subsidiaries (“Pavonia”) for total consideration of $120.0 million. The closing of the transaction is subject to certain conditions, including obtaining regulatory approvals or non-disapprovals and other customary closing conditions. The proceeds are expected to be used to pay down our revolving credit facility. Pavonia represents a substantial portion of the Life and Annuities segment. We have classified Pavonia as discontinuing operations and held-for-sale. For further information, refer to "Note 5 - Held-for-sale Business" in the notes to our consolidated financial statements included within Item 8 of this Annual Report on Form 10-K.

Other Transactions

KaylaRe

On December 15, 2016, we announced the launch of KaylaRe Ltd., a Bermuda-based Class 4 reinsurer offering a diversified range of specialty reinsurance to the global insurance market. in connection with the launch, KaylaRe Holdings Ltd., the parent company of KaylaRe Ltd. completed an initial capital raise of $620 million. Through our subsidiary, Cavello Bay Reinsurance Limited (“Cavello”), we have invested $300 million in common shares of KaylaRe. We also received a warrant to purchase up to 900,000 common shares of KaylaRe, which is exercisable upon an initial public offering or listing of KaylaRe’s common shares, with an exercise price of $20.00 per share. We use the equity method to account for our interest in KaylaRe.

Our subsidiary acts as insurance and reinsurance manager to KaylaRe Ltd., and certain of our affiliates have entered into various reinsurance agreements with KaylaRe Ltd. KaylaRe Ltd. will also have the opportunity to participate in future Enstar legacy transactions. For a detailed discussion of the transactions between us and KaylaRe, refer to "Note 21 - Related Party Transactions" in the notes to our consolidated financial statements included within Item 8 of this Annual Report on Form 10-K.

ClearSpring

On January 1, 2017, we sold SeaBright Insurance Company ("SeaBright Insurance") to an affiliate of Delaware Life Insurance Company ("Delaware Life"), a subsidiary of Guggenheim Partners, LLC. Following the sale, SeaBright Insurance will be renamed ClearSpring Property and Casualty Insurance Company ("ClearSpring") and will focus on underwriting workers' compensation and property business in the U.S. Prior to the sale, SeaBright Insurance had reinsured all of its run-off liabilities into another Enstar entity and at the time of the sale, ClearSpring contained only insurance licenses. We have retained a 20% indirect equity interest in ClearSpring and have agreed to reinsure (on a funds withheld basis) 25% of its new business underwritten. We provide underwriting and claims expertise to ClearSpring through fronting, underwriting and service agreements.

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Operating Segments

We have four segments of