Zenith National Insurance Corp. and Subsidiaries

Consolidated Financial Statements and Supplementary Consolidating Information December 31, 2018 and 2017 and for the Three Years Ended December 31, 2018

Zenith National Insurance Corp. and Subsidiaries
Consolidated Financial Statements

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Report of Independent Auditors

To the Management of Zenith National Insurance Corp.

We have audited the accompanying consolidated financial statements of Zenith National Insurance Corp. and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2018 and December 31, 2017, and the related consolidated statements of comprehensive income, cash flows and stockholders' equity for each of the three years in the period ended December 31, 2018.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Zenith National Insurance Corp. and its subsidiaries as of December 31, 2018 and December 31, 2017, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2018, in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Accounting principles generally accepted in the United States of America require that information about incurred and paid claims development that precedes the current reporting period and the historical claims payout percentages included in Note 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Financial Accounting Standards Board (FASB) who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

PricewaterhouseCoopers LLP

Los Angeles, California
February 22, 2019

ZENITH NATIONAL INSURANCE CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(In thousands, except par value)	December 31, 2018	December 31, 2017
Assets:		
Investments:		
Fixed maturity securities, at fair value (amortized cost $1,120,817 in 2018 and $433,191 in 2017)	$ 1,135,560	$ 460,349
Equity securities, at fair value (cost $240,098 in 2018 and $376,920 in 2017)	208,698	326,841
Short-term investments, at fair value which approximates cost	106,409	726,952
Other investments	203,944	220,377
Derivative assets, at fair value (cost $48,577 in 2018 and $43,017 in 2017)	9,754	6,804
Assets pledged for derivative obligations, at fair value (amortized cost $24,552 in 2018 and $11,858 in 2017)	24,567	11,858
Total investments	1,688,932	1,753,181
Cash	29,667	13,105
Accrued investment income	3,852	5,533
Premiums receivable	40,453	41,686
Reinsurance recoverables	47,885	54,431
Deferred policy acquisition costs	12,147	12,164
Deferred tax asset	47,393	46,140
Income tax receivable		3,711
Goodwill	20,985	20,985
Other assets	57,875	65,145
Total assets	$ 1,949,189	$ 2,016,081
Liabilities:		
Unpaid losses and loss adjustment expenses	$ 1,147,866	$ 1,191,531
Unearned premiums	86,710	88,701
Policyholders' dividends accrued	43,237	41,995
Long-term debt	38,225	38,196
Income tax payable	3,300	
Derivative liabilities	16,504	4,280
Other liabilities	76,177	76,294
Total liabilities	1,412,019	1,440,997
Commitments and contingencies (see Note 15)		
Stockholders' equity:		
Common stock, $1 par value, 40 authorized shares; 39 shares issued and outstanding	39	39
Additional paid-in capital	398,340	398,821
Retained earnings	145,515	180,072
Accumulated other comprehensive loss	(6,724)	(3,848)
Total stockholders' equity	537,170	575,084
Total liabilities and stockholders' equity	$ 1,949,189	$ 2,016,081

The accompanying notes are an integral part of these financial statements.

ZENITH NATIONAL INSURANCE CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)	Year Ended December 31, 2018	2017	2016
Revenues:			
Net premiums earned	$ 804,299	$ 811,604	$ 807,258
Net investment income	35,819	30,094	27,075
Net realized gains (losses) on investments	(96,736)	(23)	12,786
Change in net unrealized gains/losses on fair value option investments	6,666	90,321	(73,457)
Net losses on derivatives	(1,669)	(13,346)	(124,720)
Service fee income	9,210	9,622	9,071
Total revenues	757,589	928,272	658,013
Expenses:			
Losses and loss adjustment expenses incurred	370,424	403,958	360,082
Underwriting and other operating expenses:			
Policy acquisition costs	147,161	143,239	134,637
Underwriting and other costs	131,160	132,110	130,697
Policyholders' dividends	24,963	25,307	27,590
Interest expense	3,321	3,321	3,321
Total expenses	677,029	707,935	656,327
Income before tax	80,560	220,337	1,686
Current	34,754	45,285	48,285
Deferred (see Note 7)	(708)	26,650	(51,187)
Change in tax rate		30,760	
Total income tax expense (benefit)	34,046	102,695	(2,902)
Net income	$ 46,514	$ 117,642	$ 4,588
Net change in unrealized gains/losses on available-for-sale and other investments, net of tax and reclassification adjustment	(670)	571	(3,010)
Change in unrealized foreign currency translation adjustment, net of tax	(2,206)	2,448	(424)
Other comprehensive income (loss)	(2,876)	3,019	(3,434)
Total comprehensive income	$ 43,638	$ 120,661	$ 1,154

The accompanying notes are an integral part of these financial statements.

ZENITH NATIONAL INSURANCE CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
(In thousands)	2018	2017	2016
Cash flows from operating activities:			
Premiums collected	$ 814,943	$ 828,726	$ 815,367
Investment income received	32,427	18,301	28,364
Losses and loss adjustment expenses paid	(409,261)	(407,877)	(389,468)
Underwriting and other operating expenses paid	(288,360)	(290,390)	(280,795)
Interest paid	(3,292)	(3,292)	(3,292)
Income taxes paid	(27,743)	(50,523)	(29,722)
Net cash provided by operating activities	118,714	94,945	140,454
Cash flows from investing activities:			
Purchases of investments:			
Fixed maturity securities – fair value option	(999,692)	(26,339)	(357,633)
Equity securities – fair value option	(30,462)	(26,372)	(2,065)
Corporate loan – affiliate	(6,101)		
Other investments	(3,506)	(77,346)	(73,151)
Derivatives	(10,902)	(1,959)	(229)
Proceeds from maturities and redemptions of investments:			
Fixed maturities securities – fair value option	68,500	25,190	38,500
Other investments	432	3,329	4,769
Proceeds from sales of investments:			
Fixed maturity securities – available-for-sale			1,000
Fixed maturity securities – fair value option	254,489	121,039	563,028
Equity securities – fair value option	42,086	10,264	129,694
Other investments	3,944	15,000	17
Net decrease (increase) in short-term investments	613,348	(62,459)	(215,255)
Net derivative cash settlements	16,051	(10,839)	(90,860)
Capital expenditures and other	(2,100)	(5,622)	(5,081)
Net cash used in investing activities	(53,913)	(36,114)	(7,266)
Cash flows from financing activities:			
Dividends paid to common stockholders	(42,872)	(60,561)	(130,000)
Purchase of Fairfax shares for restricted stock awards	(5,367)	(6,574)	(4,518)
Net cash used in financing activities	(48,239)	(67,135)	(134,518)
Net increase (decrease) in cash	16,562	(8,304)	(1,330)
Cash at beginning of year	13,105	21,409	22,739
Cash at end of year	$ 29,667	$ 13,105	$ 21,409

The accompanying notes are an integral part of these financial statements.

ZENITH NATIONAL INSURANCE CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

	Year Ended December 31,		
(In thousands)	2018	2017	2016
Reconciliation of net income to net cash provided by operating activities:			
Net income	$ 46,514	$ 117,642	$ 4,588
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation expense	3,781	3,434	3,673
Net accretion	(13,762)	(5,947)	(1,395)
Net realized losses (gains) on investments	96,736	23	(12,786)
Change in net unrealized gains/losses on fair value option investments	(6,666)	(90,321)	73,457
Net losses on derivatives	1,669	13,346	124,720
Equity in earnings/losses of investee	9,566	(6,652)	2,897
Stock-based compensation expense	4,886	4,146	3,174
Decrease (increase) in:			
Accrued investment income	1,681	1,962	1,468
Premiums receivable	1,190	(4,422)	(6,336)
Reinsurance recoverables	6,546	15,226	10,498
Deferred policy acquisition costs	17	(1,236)	(271)
Net income taxes	6,302	52,173	(32,625)
Increase (decrease) in:			
Unpaid losses and loss adjustment expenses	(43,665)	(17,041)	(41,591)
Unearned premiums	(1,991)	8,301	1,949
Policyholders’ dividends accrued	1,242	5,594	11,022
Accrued expenses	(466)	4,418	1,999
Other	5,134	(5,701)	(3,987)
Net cash provided by operating activities	$ 118,714	$ 94,945	$ 140,454

The accompanying notes are an integral part of these financial statements.

ZENITH NATIONAL INSURANCE CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(In thousands)	Year Ended December 31, 2018	2017	2016
Common stock:			
Beginning of year	$ 39	$ 39	$ 39
End of year	39	39	39
Additional paid-in capital:			
Beginning of year	398,821	401,249	402,593
Stock-based compensation expense	4,886	4,146	3,174
Purchases of Fairfax shares for restricted stock awards	(5,367)	(6,574)	(4,518)
End of year	398,340	398,821	401,249
Retained earnings:			
Beginning of year	180,072	173,430	298,842
Net income	46,514	117,642	4,588
Reclassification of certain tax effects from accumulated other comprehensive loss at January 1, 2018 (see Note 13)	829		
Dividends to common stockholders	(81,900)	(111,000)	(130,000)
End of year	145,515	180,072	173,430
Accumulated other comprehensive loss:			
Beginning of year	(3,848)	(6,867)	(3,433)
Reclassification of certain tax effects to retained earnings at January 1, 2018 (see Note 13)	(829)		
Net change in unrealized gains/losses on available-for-sale and other investments, net of tax and reclassification adjustment	(121)	571	(3,010)
Change in unrealized foreign currency translation adjustment, net of tax	(1,926)	2,448	(424)
End of year	(6,724)	(3,848)	(6,867)
Total stockholders' equity	$ 537,170	$ 575,084	$ 567,851

The accompanying notes are an integral part of these financial statements.

Note 1. Basis of Presentation and Summary of Operations

Basis of Presentation

The accompanying Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and include Zenith National Insurance Corp. ("Zenith National") and its subsidiaries. All intercompany transactions and balances have been eliminated in consolidation.

Organization and Operations

Zenith National is a Delaware holding company, which is an indirect wholly-owned subsidiary of Fairfax Financial Holdings Limited ("Fairfax"). Fairfax is a Canadian financial services holding company, whose common stock is publicly traded on the Toronto Stock Exchange, and is principally engaged in property and casualty insurance, reinsurance and associated investment management.

Zenith National's wholly-owned subsidiaries (primarily Zenith Insurance Company ("Zenith Insurance")), specialize in the workers' compensation insurance business nationally and, since 2010, in the property-casualty business for California agriculture. Unless otherwise indicated, all references to the "Company" refer to Zenith National together with its subsidiaries.

The accompanying Consolidated Financial Statements differ from the financial information published by Fairfax in regards to the Company primarily due to differences between GAAP and International Financial Reporting Standards ("IFRS," the reporting basis used by Fairfax), intercompany investment transactions and accounting adjustments recorded by Fairfax related to the acquisition of the Company.

Use of Estimates

GAAP requires the use of assumptions and estimates in reporting certain assets and liabilities and related disclosures. Actual results could differ from those estimates.

Reclassifications

Certain prior year amounts in the accompanying consolidated financial statements have been reclassified to conform to the current year presentation.

Subsequent Events

The Company evaluated subsequent events through the date and time that the Consolidated Financial Statements were issued on February 22, 2019.

Note 2. Summary of Accounting Policies

Investments

At both December 31, 2018 and 2017, $1.5 billion of investments in fixed maturities, equity securities and short-term investments were recorded under the fair value option and changes in fair value for these investments are recorded in the change in net unrealized gains/losses on fair value option investments in the Consolidated Statements of Comprehensive Income. At both December 31, 2018 and 2017, approximately $16 million of investments in equity securities were classified as available-for-sale and reported at fair value, with changes in unrealized gains and losses excluded from earnings and reported in a separate component of stockholders' equity, net of tax.

Other investments at December 31, 2018 and 2017 are comprised of investments in partnerships and limited liability companies managed by professionals across multiple industries, loans to affiliates, as well as common stock investments recorded under the equity method of accounting. Partnerships and limited liability company investments where the Company's ownership is minor and the Company does not have significant operating or financial influence are recorded at fair value using the cost method of accounting. Changes in fair value of these investments are excluded from earnings and reported as a separate component of stockholders' equity, net of tax. Investments in partnerships and limited liability companies where the Company's ownership share is more than minor are recorded under the equity method of accounting. Investments in common stocks of an entity over which the Company is deemed to have significant influence are also recorded under the equity method of accounting, unless a fair value option was elected for such securities. The carrying value of the Company's investments in the equity-method partnerships and common stocks represents the initial cost, adjusted for any additional purchases/distributions, other-than-temporary impairments, if any (as discussed below), and the Company's share of the changes in the investee's net asset value ("NAV") since the initial acquisition. The affiliated corporate loans are carried at fair value, with changes in fair value recorded in the change in unrealized gain/losses of fair value option investments in the Company's Statement of Comprehensive Income.

Investments classified as available-for-sale and other investments could be subject to default by the issuer or declines in fair value that become other-than-temporary. The Company continually assesses the prospects for individual available-for-sale securities, investments in partnerships and limited liability companies and equity-method common stocks as part of its ongoing portfolio management, including the identification of other-than-temporary declines in fair values. The Company's other-than-temporary assessment includes reviewing the extent and duration of declines in fair values of such investments below the cost or amortized cost basis or carrying value, the seniority and duration of the securities, historical and projected company financial performance, company-specific news and other developments, the outlook for industry sectors, credit ratings, and macro-economic changes, including government policy initiatives. For available-for-sale equity securities and other investments, an other-than-temporary impairment is recognized in earnings and reflected as a reduction in the cost basis or carrying value of the security based on the extent and duration that fair value is below cost or carrying value, in addition to issuer specific events. There were no other-than-temporary impairments on equity-method investments or available-for-sale securities for the year ended December 31, 2018 and 2016. The Company recorded other-than-temporary impairments of $0.9 million on one equity-method common stock investment and $0.2 million on one available-for-sale equity security for the year ended December 31, 2017. The Company recorded $1.3 million, $0.1 million and $1.0 million of other-than-temporary impairments on cost-method partnerships and limited liability companies for the years ended December 31, 2018, 2017 and 2016, respectively.

Investment income is recorded when earned. Realized capital gains and losses are determined under the "average cost" method.

Derivative Contracts

Derivative contracts may include interest rate and total return swaps, consumer price index linked ("CPI-linked"), currency forwards, warrants and option contracts, all of which derive their value mainly from changes in underlying interest rates, foreign exchange rates, inflation indexes or equity instruments. A derivative contract may be traded on an exchange or over-the-counter ("OTC"). OTC derivative contracts are individually negotiated between contracting parties and may include the Company's forwards and foreign currency option contracts, CPI-linked derivatives and total return swaps.

The Company uses derivatives principally to mitigate financial risks arising from its investment holdings, and monitors the derivatives for effectiveness in achieving their risk management objectives.

Derivatives are carried at fair value. The fair value of derivative contracts in a gain position is presented as derivative assets in the Consolidated Balance Sheets. The fair value of derivative contracts in a loss position is presented as derivative liabilities in the Consolidated Balance Sheets. The initial premium paid for a derivative contract, if any, would be recorded as a derivative asset and subsequently adjusted for changes in the fair value of the contract at each balance sheet date. Changes in fair value of a derivative are recorded in the Consolidated Statements of Comprehensive Income as net gains (losses) on derivatives, with a corresponding adjustment to the carrying value of the derivative asset or liability. Cash settlements related to fair value changes on derivative contracts are also recorded in the Consolidated Statements of Comprehensive Income as net gains (losses) on derivatives, and are recorded as an investing activity in the Consolidated Statements of Cash Flows.

Cash received from counterparties as collateral for derivative contracts is recorded as other assets in the Consolidated Balance Sheets, and a corresponding liability is recognized as other liabilities. Securities pledged by counterparties as collateral for derivatives in a gain position are not recorded as assets of the Company. Securities pledged to counterparties by the Company as collateral for derivative contracts in a loss position, as well as contractually required independent collateral, are reflected in the Consolidated Balance Sheets as assets pledged for derivative obligations.

Equity contracts

The Company's long equity total return swaps allow the Company to receive the total return on a notional amount of an individual equity (including dividends and capital gains or losses) in exchange for the payment of a floating rate of interest on the notional amount. Conversely, short equity index total return swaps purchased prior to December 31, 2016 allowed the Company to pay the total return on a notional amount of an equity index in exchange for the receipt of a floating rate of interest on the notional amount. The Company classifies dividends and interest paid or received related to its long equity and short equity index total return swaps on a net basis as investment income in the Consolidated Statements of Comprehensive Income. The Company's long equity and short equity index total return swaps may contain reset provisions requiring counterparties to cash-settle on a monthly or quarterly basis any fair value movements arising subsequent to the prior settlement date. Any cash amounts paid to settle unfavorable fair value changes and, conversely, any cash amounts received in settlement of favorable fair value changes, are recorded as net gains (losses) on derivatives recorded in the Consolidated Statements of Comprehensive Income. To the extent that a contractual reset date does not correspond to the balance sheet date, the Company records net gains (losses) on derivatives in the Consolidated Statements of Comprehensive Income to adjust the carrying value of the corresponding derivative asset or liability associated with each total return swap to reflect its fair value at the balance sheet date. Final cash settlements on total return swaps are recognized as net gains (losses) on derivatives net of any previously recorded unrealized fair value changes since the last reset date. Total return swaps require no initial net cash investment; and at inception the fair value is zero. At December 31, 2018 and 2017, the Company pledged securities with a fair value of $13.3 million and $2.5 million, respectively, as collateral to the counterparties to its long equity total return swaps derivative contracts. The Company terminated all of its short equity index total return swaps derivative contracts during the fourth quarter of 2016.

CPI-linked derivative contracts

The Company's derivative contracts referenced to the consumer price index in the United States and Europe ("CPI-linked derivatives") serve as an economic hedge against the potential adverse financial impact on the Company of decreasing price levels. These contracts may be structured to provide a payout at maturity if there is cumulative deflation over the life of the contract or if cumulative average inflation is below a specified floor rate over the life of the contract. As the average remaining life of a CPI-linked derivative declines, the fair value of the contract (excluding the impact of changes in the underlying CPI) will generally decline. The initial premium paid for each contract is recorded as a derivative asset and is subsequently adjusted for changes in the fair value of the contract at each balance sheet date with a corresponding offset to net gains (losses) on derivatives in the Consolidated Statements of Comprehensive Income. In the event of a sale, expiration or early settlement of any of these contracts, the Company will receive a cash settlement equal to the fair value of that contract on the date of the transaction. The Company's maximum potential loss on any contract is limited to the original cost of that contract. The Company's CPI-linked derivatives have a remaining weighted average life of 3 years as of December 31, 2018. At December 31, 2018 and 2017, the Company pledged securities with a fair value of $4.3 million and $5.3 million, respectively, as contractually required independent collateral to a counterparty for the CPI-linked derivatives.

U.S. Government bond forward contracts

Derivative forward contracts to sell long-dated U. S. Government bonds ("Treasury locks") are designed to hedge the exposure to interest rate risk in the Company's U.S. state and municipal bonds and long-dated U.S. Government bonds. Treasury locks derive their value primarily from changes in fair value of the underlying U.S. Treasury bond between the contract inception and expiration dates, require no initial net cash investment, and at inception the fair value is zero. These contracts have a term to maturity of less than one year and may be renewed at market rates. To the extent that the expiration date does not correspond to the balance sheet date, the Company adjusts the carrying value of the corresponding derivative asset or liability associated with each Treasury lock to reflect its fair value at the balance sheet date with the corresponding net gains (losses) on derivatives recorded in the Consolidated Statements of Comprehensive Income. At December 31, 2018 and 2017, the Company pledged securities with a fair value of $7.0 million and $4.1 million, respectively, as contractually required independent and mark-to-market collateral to the counterparty for the Treasury locks.

Foreign exchange forward contracts

Foreign exchange forward contracts ("foreign exchange forwards") denominated in the Euro are used to manage certain foreign currency exposures arising from foreign currency denominated investments. These foreign exchange forwards require no initial net cash investment and at inception the fair value is zero. These contracts have a term to maturity of less than one year and may be renewed at market rates. To the extent that the expiration date does not correspond to the balance sheet date, the Company adjusts the carrying value of the corresponding derivative asset or liability associated with each foreign exchange forward to reflect its fair value at the balance sheet date with the corresponding net gains (losses) on derivatives recorded in the Consolidated Statements of Comprehensive Income. At both December 31, 2018 and 2017, the Company had no pledged securities as collateral for any foreign exchange forward contract.

Counterparty risk

The Company endeavors to limit counterparty risk through the terms of master netting agreements negotiated with the counterparties to its derivative contracts. These agreements provide for a single net settlement of all financial instruments covered by the agreement in the event of default by the counterparty, thereby permitting obligations owed by the Company to a counterparty to be offset to the extent of the aggregate amount receivable by the Company from that counterparty ("net settlement arrangements"). Pursuant to these agreements, the counterparties to the derivative contracts are also contractually required to deposit eligible collateral in collateral accounts (subject to certain minimum thresholds) for the benefit of the Company depending on the then current fair value of the derivative contracts. The Company had not exercised its right to sell or repledge collateral at December 31, 2018.

See Note 4 for additional information related to derivative contracts.

Cash

Cash includes demand deposits with financial institutions.

Recognition of Property-Casualty Revenue and Expense

Revenue Recognition

The consideration paid for an insurance policy is generally known as a "premium." Premiums billed to the Company's policyholders are recorded as revenues in the Consolidated Statements of Comprehensive Income. Premiums are billed and collected according to policy terms, predominantly in the form of installments during the policy period. Premiums are earned pro-rata over the terms of the policies. Billed premiums applicable to the unexpired terms of policies in-force are recorded in the accompanying Consolidated Balance Sheets as a liability for unearned premiums.

Certain states in which the Company conducts business require that the Company bill additional amounts, or assessments, to policyholders in accordance with state statutes. In some cases, the Company is required to pay in advance estimated amounts of these assessments to the relevant regulatory agency. Premiums do not include these assessments and their collection does not have any impact on the Company's results of operations.

Any amounts receivable for billed premiums are charged-off upon initiating the legal collection process. An estimate of amounts that are likely to be charged-off is established as an allowance for doubtful accounts as of the balance sheet date. The estimate is comprised of any specific accounts that are past due and are considered probable to be charged-off and a provision against remaining accounts receivable based on historical bad debt expense. Premiums receivable is reported net of an allowance for estimated uncollectible amounts which was $0.8 million and $0.3 million at December 31, 2018 and 2017, respectively.

Workers' compensation premiums are determined based upon the payroll of the insured, the applicable premium rates and, where applicable, an experience-based modification factor and a debit or credit applied by the Company's underwriters based upon individual risk characteristics. Audits of policyholders' records are conducted after policy expiration to make a final determination of applicable premiums. Included with premiums earned is an estimate of the impact of final audit premiums. The Company can estimate this adjustment because it monitors, by policy, how much additional premium will be billed or refunded in final audit invoices as a percentage of the original estimated amount that was billed. The Company uses the historical percentage and current trends to estimate the probable amount to be billed or refunded as of the balance sheet date. When payrolls decline during policy periods (such as during a recession), the Company may bill more premium than is actually owed and will establish liability for the estimated amount to be refunded to its policyholders. When payrolls increase during policy periods, the Company may bill less premium than is actually owed and will establish a receivable for the estimated amount due from its policyholders. Included in premiums receivable was $4.8 million and $5.4 million at December 31, 2018 and 2017, respectively, for estimated additional amounts of premiums to be billed to the Company's policyholders.

The Company has written a relatively small number of workers' compensation policies that are retrospectively rated. Under this type of policy, subsequent to policy expiration, the policyholder may be entitled to a refund or owe additional premium based on the amount of losses sustained under the policy. These retrospective premium adjustments are limited in the amount by which they increase or decrease the standard amount of premium applicable to the policy. The Company can estimate these retrospective premium adjustments because it knows the underlying loss experience of the policies involved. At December 31, 2018 and 2017, the net premiums payable under retrospectively rated workers' compensation policies reflected in unearned premiums was $1.3 million and $0.9 million, respectively.

Losses and Loss Adjustment Expenses Incurred

Losses and loss adjustment expenses incurred in the accompanying Consolidated Statements of Comprehensive Income include provisions for the amount the Company expects to ultimately pay for all reported and unreported claims for the applicable periods. Loss adjustment expenses are the expenses applicable to the process of administering, settling and investigating claims, including related legal expenses.

Estimates of losses from environmental and asbestos related claims are included in overall loss reserves and to date have not been material.

Unpaid Losses and Loss Adjustment Expenses

The liabilities for unpaid losses and loss adjustment expenses ("loss reserves") in the accompanying Consolidated Balance Sheets are estimates of the unpaid amounts that the Company expects to pay for the ultimate cost of reported and unreported claims as of the balance sheet date. Loss reserves are estimates and are inherently uncertain; they do not and cannot represent an exact measure of ultimate liability. The Company's actuaries perform a comprehensive review of loss reserves at the end of every quarter, from which a point estimate of loss reserves is determined. The loss reserve estimates recorded in the financial statements reflect management's best estimate of loss reserves based on the actuarial point estimate as well as judgment regarding the inherent uncertainties of ultimate loss costs. There is no material difference between the actuarial point estimate and the loss reserve estimate recorded in the financial statements at December 31, 2018 and 2017. Workers' compensation, the Company's principle line of insurance, accounts for 92.4% of the net earned premium in 2018 and 94.7% of the outstanding liabilities for unpaid losses and loss adjustment expenses, net of reinsurance recoverable, at December 31, 2018. Given the long-tail nature of workers' compensation liabilities, the ultimate losses will not be known for many years and estimating loss reserves is a complex process which involves a combination of actuarial techniques and management judgment including the consideration of all relevant data.

The Company's actuaries produce a point estimate for workers' compensation loss reserves using the results of various methods of estimation. The actuaries prepare reserve estimates for all accident years using the Company's historical claims data and many of the common actuarial methodologies for estimating loss reserves, such as paid loss development methods, incurred loss development methods, the Bornhuetter-Ferguson methods and methods that utilize claim counts and average severity. The actuarial point estimate is based on a selection of the results of these various methods depending upon both the age of the accident year and the geographic state of the injury. For mature accident years, all of the methods produce very similar loss estimates; the actuarial point selections are primarily based upon incurred loss development methods because the actuaries believe this most accurately reflects the required reserves for the relatively few claims that remain open. For recent accident years, the Bornhuetter-Ferguson methods and methods that utilize claim counts and average severity are weighted with paid and incurred loss development methods.

When losses are reported to the Company, it establishes individual estimates of the ultimate cost of the claims, known as "case reserves." These case reserves are continually monitored and revised in response to new information and for amounts paid. The Company's actuaries use this information about reported claims in some of their estimation techniques. In estimating the Company's total loss reserves, the Company makes provision for two types of loss development. At the end of any calendar period, there are a number of claims that have not yet been reported but will arise out of accidents that have already occurred. These are referred to in the insurance industry as incurred but not reported ("IBNR") claims and the Company's loss reserves contain an estimate for IBNR claims. In addition to this provision for late reported claims, the Company also has to estimate, and make provision for, the extent to which the case reserves on known claims may also develop. These types of reserves are referred to in the insurance industry as "bulk" reserves. The Company's loss reserves make provision for both IBNR and bulk reserves in total, but not separately. The large majority of claims are reported promptly and therefore, as of the balance sheet date, the number of IBNR claims is relatively insignificant.

The principal uncertainty in the Company's workers' compensation loss reserve estimates is the risk of increasing claim costs, particularly medical. In estimating loss reserves, the Company's actuaries consider medical costs by evaluating long-term trends. The additional uncertainties considered in estimating ultimate loss costs include the ultimate number of expensive cases and the length of time required to settle long-term expensive cases. Expensive claims are those involving permanent disability of an injured worker and are paid over many years. The ultimate costs of expensive claims are difficult to estimate because of such factors as the on-going and possibly increasing need for medical care, complications from comorbidity, the duration of disability, life expectancy and benefits for dependents, as well as increased costs associated with obtaining settlement approval from Medicare.

The greater part of the challenge in estimating the loss reserves is associated with estimating the year-over-year increase (or decrease) in average claim severity for each accident year. Year-over-year rates of change of workers' compensation average claim severity (severity trends/inflation) vary considerably. The Company's initial workers' compensation loss reserve estimates for recent accident years provide for claim severity trends that contemplate the long-term trend observed in the Company's business. As loss experience emerges, actuarial estimates of ultimate losses and severity trends converge with those of the traditional dollar based loss development methods, resulting in net favorable or unfavorable development of the total loss reserve estimate.

Different assumptions about the claim severity inflation rates would change the workers' compensation loss reserve estimates; a material change is reasonably possible although management cannot predict if, when and to what extent such a change will occur. If the average annual inflation rate for each of the accident years 2016 through 2018 were increased or decreased by one percentage point in each year, the loss reserve estimates at December 31, 2018 would change accordingly by approximately $20 million.

The Company believes its loss reserve estimates are adequate. However, the ultimate losses will not be known with any certainty for several years. The Company evaluates its loss reserve estimates every quarter to reflect the most current data and judgments. Any resulting adjustments to loss reserves are reflected in the Company's Consolidated Statements of Comprehensive Income in the period in which the change is made.

Deferred Policy Acquisition Costs

Policy acquisition costs, consisting of agent commissions and premium taxes that vary with, and are primarily related to, the production of new or renewal business are deferred and amortized as the related premiums are earned.

A premium deficiency is recognized if the sum of expected losses and loss adjustment expenses, expected dividends to policyholders, unamortized acquisition costs and policy maintenance costs exceeds the remaining unearned premiums. A premium deficiency would first be recognized by charging any unamortized acquisition costs to expense to the extent required to eliminate the deficiency. If the premium deficiency were greater than unamortized acquisition costs, a liability would be accrued for the excess deficiency. The Company does not consider anticipated investment income when determining if a premium deficiency exists. There was no premium deficiency at December 31, 2018 or 2017.

Policyholders' Dividends

The Company issues certain policies in which the policyholder may qualify to receive a dividend. An estimated provision for workers' compensation policyholders' dividends is accrued as the related premiums are earned. Such dividends do not become a fixed liability unless and until declared by the respective Board of Directors of Zenith National's insurance subsidiaries. The dividend to which a policyholder may be entitled is set forth in the policy. Dividends are calculated after policy expiration. The Company is able to estimate any liability it may have because it knows the underlying loss experience of the policies it has written with dividend provisions and can estimate the future liability from the policy terms. Approximately 47% of the Company's workers' compensation net premiums were earned from participating policies with dividend provisions.

State Guaranty Fund Assessments

Guaranty funds ("Guaranty Funds") exist in several states to ensure that policyholders (holders of direct insurance policies but not of reinsurance policies) receive payment of their claims if insurance companies become insolvent. A Guaranty Fund is funded primarily by statutorily required assessments on insurance companies doing business in the state. Various mechanisms exist in some of these states for assessed insurance companies to recover these assessments. Upon the insolvency of an insurance company, the Guaranty Funds become primarily liable for the payment of the insolvent company's liabilities to policyholders. The declaration of an insolvency establishes the presumption that assessments by the Guaranty Funds are probable. The Company writes workers' compensation insurance in many states in which unpaid workers' compensation liabilities are the responsibility of the Guaranty Funds and has received, and expects to continue to receive, Guaranty Fund assessments, some of which may be based on a certain amount of the premiums it has already earned as of December 31, 2018.

The Company recorded an estimate of $1.4 million for the expected net liability at both December 31, 2018 and 2017, respectively, for Guaranty Fund assessments. The ultimate impact of such assessments will depend upon the amount and timing of actual assessments and of any recoveries to which the Company may be entitled.

Reinsurance Ceded

In the ordinary course of business and in accordance with general insurance industry practices, the Company purchases excess of loss reinsurance to protect it against the impact of large, irregularly occurring losses in the workers' compensation business. Such reinsurance reduces the magnitude of such losses on net income and the capital of the Company. Reinsurance makes the assuming reinsurer liable to the ceding company to the extent of the reinsurance. It does not, however, discharge the ceding company from its primary liability to its policyholders in the event the reinsurer is unable to meet its obligations under such reinsurance agreement. The Company monitors the financial condition of its reinsurers and does not believe that it is currently exposed to any material credit risk through its ceded reinsurance arrangements because most of its reinsurance is recoverable from large, well-capitalized reinsurance companies. As such, the Company did not record an allowance for uncollectible recoverables from its reinsurers. Historical write-offs have been infrequent and insignificant.

Premiums earned and losses and loss adjustment expenses incurred are stated in the accompanying Consolidated Statements of Comprehensive Income after deduction of amounts ceded to reinsurers. Balances due from reinsurers on unpaid losses, including an estimate of such recoverables related to reserves for IBNR losses, are reported as assets and are included in reinsurance recoverables even though amounts due on unpaid losses and loss adjustment expenses are not recoverable from the reinsurer until such losses are paid.

In 1998, Zenith Insurance acquired substantially all of the assets and certain liabilities of RISCORP, Inc. and certain of its subsidiaries (collectively, "RISCORP") related to its workers' compensation business. Also, in 1998, the Company entered into an aggregate excess of loss reinsurance agreement which provides ceded reinsurance for unpaid losses assumed by Zenith Insurance from RISCORP up to $50.0 million in excess of $182.0 million. In May 2018, the Company commuted this retroactive reinsurance agreement, received $3.0 million, eliminated a deferred gain of $0.4 million and recorded a total gain of $0.6 million. Reinsurance recoverables on unpaid losses and loss adjustment expenses at December 31, 2017 included recoverables under such agreement of $2.8 million, respectively, which was fully secured by an investment grade security held in a trust account. The deferred gain associated with such reinsurance was $0.5 million at December 31, 2017.

Properties and Equipment

Properties and equipment used in operations, including certain costs incurred to develop and obtain computer software, are capitalized and carried at cost less accumulated depreciation. Depreciation is calculated on a straight-line basis using the following useful lives: buildings — up to 40 years; and other property and equipment — 3 to 10 years. Expenditures for maintenance and repairs are charged to operations as incurred. Additions and improvements to buildings and other fixed assets are capitalized and depreciated over the useful lives of the properties and equipment. Upon disposition, the asset cost and related depreciation are removed from the accounts and the resulting gain or loss is included in the Company's results of operations.

Intangible Assets

At December 31, 2018 and 2017, goodwill from acquisitions was $21.0 million, of which $19.0 million is included in the assets of Zenith Insurance with the remaining $2.0 million included in Zenith National's assets. Other than goodwill, the Company had no intangible assets at December 31, 2018 or 2017. The Company tests goodwill for impairment annually and more frequently if an event occurs or circumstances change that management determines would more likely than not reduce the fair value of a reporting unit below its carrying amount. A reporting unit is an operating segment or a unit one level below the operating segment. The impairment tests include a comparison of the carrying amount of goodwill to the present value of future cash flows of both the Company's total workers' compensation business and the Southeast region workers' compensation business operation, a reporting unit. The fair value, estimated based on the present value of future cash flows of the reporting unit, exceeded its carrying amount as of December 31, 2018. Therefore, goodwill of the reporting unit is not considered impaired.

Restricted Stock

Under a restricted stock plan adopted by Fairfax in September 2010 ("Restricted Stock Plan"), certain Company officers are awarded shares of Fairfax Subordinate Voting Shares, no par value, with restricted ownership rights ("Restricted Stock"). Shares of Restricted Stock awarded during 2010 and 2011 vested in two equal installments on the third and fifth anniversary of the award date. Vesting of shares awarded in 2012 through November 2014 are conditioned upon the Company meeting a performance criterion in either the third, fourth or fifth year following the award date, with vesting to occur in three equal consecutive annual installments following the first year in which the condition is met. The Restricted Stock awarded after 2014 vests on the fifth anniversary of the award date and contains no performance conditions. The Restricted Stock vests in full upon the death or disability of the recipient of Restricted Stock. Restricted Stock is generally forfeited by employees who terminate employment prior to vesting. During the vesting period, the Restricted Stock Plan participants are entitled to voting rights and ordinary cash dividends paid by Fairfax from the date of the award. Restricted Stock awards under the Restricted Stock Plan are accounted for as equity awards based on the amount paid by the Company for the open market purchase of Fairfax Subordinate Voting Shares prior to each award. Compensation expense is recognized over the vesting period based on the grant date fair value with an offsetting entry to the initial charge to the Company's stockholders' equity.

Recent Accounting Guidance Not Yet Adopted

In May 2014, the Financial Accounting Standards Board ("FASB") issued new guidance on how an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This guidance does not apply to contracts within the scope of other standards (for example, insurance contracts or lease contracts). In August 2015, the FASB deferred the effective date of this new guidance by one year. This guidance is now effective for annual reporting periods beginning after December 15, 2018 and interim periods thereafter. Early adoption is not permitted. The guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In January 2016, the FASB issued updated guidance to address the recognition, measurement, presentation, and disclosure of certain financial instruments. The updated guidance requires equity investments, except those accounted for under the equity method of accounting, that have readily determinable fair value to be measured at fair value with changes in fair value recognized in net income. Equity investments that do not have readily determinable fair values may be remeasured at fair value either upon the occurrence of an observable price change or upon identification of impairment. A qualitative assessment for impairment is required for equity investments without readily determinable fair values. The updated guidance also eliminates the requirement to disclose the method and significant assumptions used to estimate the fair value of financial instruments measured at amortized cost on the balance sheet. The updated guidance is effective for annual periods beginning after December 15, 2018 and interim periods thereafter and will require recognition of a cumulative effect adjustment at adoption. In February 2018, the FASB issued technical corrections and improvements intended to clarify certain aspects of the guidance on recognizing and measuring financial assets and liabilities. The guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In February 2016, the FASB issued updated guidance to require lessees to recognize a right-to-use asset and a lease liability for leases with terms of more than 12 months. The updated guidance retains the two classifications of a lease as either an operating or finance lease (previously referred to as a capital lease). Both lease classifications require the lessee to record the right-to-use asset and the lease liability based upon the present value of cash flows. Finance leases will reflect the financial arrangement by recognizing interest expense on the lease liability separately from the amortization expense of the right-to-use asset. Operating leases will recognize lease expense (with no separate recognition of interest expense) on a straight-line basis over the term of the lease. The accounting by lessors is not significantly changed by the updated guidance. The updated guidance requires expanded qualitative and quantitative disclosures, including additional information about the amounts recorded in the financial statements. In July 2018, the FASB amended the updated guidance and provided an additional transition method with which to adopt the updated guidance. Under the additional transition method, entities may elect to recognize a cumulative-effect adjustment to the opening balance of retained earnings in the year of adoption. Consequently, if this transition method is elected, an entity's reporting for the comparative periods prior to adoption presented in the financial statements would continue to be in accordance with current lease guidance. This guidance is effective for annual periods beginning after December 15, 2019 and interim periods thereafter. Early adoption is permitted. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In June 2016, the FASB issued new guidance which requires a financial asset (or a group of financial assets) measured at amortized cost to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value of the amount expected to be collected on the financial asset. The guidance broadens the information that an entity must consider in developing its expected credit loss estimate for assets measured either collectively or individually; measurement of expected credit losses will be based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. Furthermore, the new guidance requires credit losses relating to available-for-sale securities to be recorded through an allowance for credit losses, and an entity will be able to record reversals of credit losses in current period net income. The effective date of the guidance was deferred until fiscal years beginning after December 15, 2021, including interim periods within the fiscal year. The guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In August 2016, the FASB issued new guidance which addresses how certain cash receipts and cash payments are presented and classified on the statement of cash flows. The guidance will be effective for annual periods beginning after December 15, 2018 and interim periods thereafter. Early adoption is permitted. This guidance is not expected to have a material impact on the Company's financial statements.

In October 2016, the FASB issued new guidance which requires recognition of current and deferred income taxes resulting from an intra-entity transfer of any asset (excluding inventory) when the transfer occurs. This is a change from existing GAAP which prohibits recognition of current and deferred income taxes until the asset is sold to a third party. The guidance will be effective for annual periods beginning after December 15, 2018 and interim periods thereafter. Early adoption is permitted. This guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In November 2016, the FASB issued new guidance on how entities should present restricted cash and restricted cash equivalents in the statement of cash flows. The guidance requires entities to present the changes in the total of cash, cash equivalents, restricted cash and restricted cash equivalents in the statement of cash flows. As a result, entities will no longer present transfers between cash and cash equivalents and restricted cash and restricted cash equivalents in the statement of cash flows. The guidance will be effective for annual periods beginning after December 15, 2018 and interim periods thereafter. Early adoption is permitted. The guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In January 2017, the FASB issued new guidance to simplify how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. Under the new guidance, entities will record an impairment charge based on the excess of a reporting unit's carrying amount over its fair value. The guidance will be effective for annual periods or any interim goodwill impairment tests beginning after December 15, 2021. Early adoption is permitted. The guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In March 2017, the FASB issued updated guidance to shorten the amortization period for certain callable debt securities held at a premium. The guidance requires the premium to be amortized to the earliest call date; however, securities held at a discount will continue to be amortized to maturity. The guidance will be effective for annual periods beginning after December 15, 2019, and interim periods thereafter. Early adoption is permitted. This guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In August 2018, the FASB issued updated guidance that modifies disclosure requirements related to fair value measurement. The amendments are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Implementation on a prospective or retrospective basis varies by specific disclosure requirement. Early adoption is permitted. The guidance also allows for early adoption of any removed or modified disclosures upon issuance of this guidance while delaying adoption of the additional disclosures until their effective date. The guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In August 2018, the FASB issued updated guidance to reduce complexity for the accounting for costs of implementing a cloud computing service arrangement. The new guidance aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. The updated guidance is effective for reporting periods beginning after December 15, 2020. Early adoption is permitted. The guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

In October 2018, the FASB issued new guidance that expands the application of a specific private company accounting alternative related to variable interest entities and changes how entities evaluate decision-making fees under the variable interest guidance. Entities will consider indirect interests held through related parties under common control on a proportionate basis rather than in their entirety. Entities are required to apply the amendments retrospectively. The guidance will be effective for reporting periods beginning after December 15, 2020 and interim periods thereafter. Early adoption is permitted. The guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

Note 3. Investments

The cost or amortized cost and fair value of fair value option and available-for-sale investments at December 31, 2018 and 2017 were as follows:

(In thousands)	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
December 31, 2018				
Fair value option investments:				
Fixed maturity securities:				
State and local government debt	$ 87,607	$ 17,363		$ 104,970
U.S. Government debt (a)	983,019	1,245	$ (785)	983,479
Corporate debt	52,817	825	(3,890)	49,752
Total fixed maturity securities	1,123,443	19,433	(4,675)	1,138,201
Equity securities	219,734	3,469	(30,620)	192,583
Short-term investments (b)	128,335			128,335
Other investments – affiliate corporate loans	6,110	255		6,365
Total fair value option investments	1,477,622	23,157	(35,295)	1,465,484
Available-for-sale investments:				
Equity securities	20,364	22	(4,271)	16,115
Total available-for-sale investments	20,364	22	(4,271)	16,115
Total fixed maturity, equity securities and short-term investments	**$ 1,497,986**	**$ 23,179**	**$ (39,566)**	**$ 1,481,599**
December 31, 2017				
Fair value option investments:				
Fixed maturity securities:				
State and local government debt	$ 388,034	$ 27,084	$ (46)	$ 415,072
U.S. Government debt	23,159	520	(91)	23,588
Corporate debt	21,998	2,869	(3,178)	21,689
Total fixed maturity securities	433,191	30,473	(3,315)	460,349
Equity securities	356,556	32,175	(78,137)	310,594
Short-term investments (b)	738,810			738,810
Total fair value option investments	1,528,557	62,648	(81,452)	1,509,753
Available-for-sale investments:				
Equity securities	20,364	16	(4,133)	16,247
Total available-for-sale investments	20,364	16	(4,133)	16,247
Total fixed maturity, equity securities and short-term investments	**$ 1,548,921**	**$ 62,664**	**$ (85,585)**	**$ 1,526,000**

(a) Includes investments of $2.6 million pledged for derivative obligations at December 31, 2018.

(b) Includes investments of $21.9 million and $11.9 million pledged for derivative obligations at December 31, 2018 and 2017, respectively.

Fixed maturity securities, including short-term investments, by contractual maturity at December 31, 2018 were as follows:

(In thousands)		Amortized Cost		Fair Value
Due in one year or less	$	613,460	$	612,835
Due after one year through five years		542,316		540,078
Due after five years through ten years		5,597		5,939
Due after ten years		90,405		107,684
Total	$	1,251,778	$	1,266,536

Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Total investments at December 31, 2018 also include other investments detailed below and derivative contracts described in Note 4.
Other investments consist of the following:

	December 31,			
(In thousands)		2018		2017
Equity-method common stock (a)	$	162,028	$	169,788
Equity-method partnerships (a)		13,502		26,369
Cost-method partnerships, at fair value (cost $21,756 in 2018 and $22,985 in 2017) (b)		22,049		24,220
Affiliate corporate loans (cost $6,110)		6,365		
Total other investments	$	203,944	$	220,377

(a) Investments in common stock, partnerships and limited liability companies accounted under the equity method are recorded at cost, adjusted for subsequent purchases, distributions, other-than-temporary impairments, if any, and the Company's share of the changes in the investee's NAV since the initial acquisition.

(b) Partnerships and limited liability company investments where the Company's ownership is minor and the Company does not have significant operating or financial influence are recorded at fair value.

At December 31, 2018, the Company had commitments to invest an additional $14.7 million in partnerships and limited liability companies.

Net realized gains (losses) on investments, excluding derivatives, were as follows:

	Year Ended December 31,					
(In thousands)		2018		2017		2016
Sales of equity securities (a)	$	(97,838)	$	(19,324)	$	(13,014)
Sales of fixed maturity securities, including short-term investments and other (b)		1,799		12,453		24,940
Gains (losses) from other investments (c)		(697)		6,848		860
Net realized gains (losses) on investments	$	(96,736)	$	(23)	$	12,786

(a) Net realized losses on sales of equity securities for the year ended December 31, 2018 include $1.2 million of gross realized gains and $99.0 million of gross realized losses on sales of fair value option equity securities, including $86.0 million of realized losses recognized upon transfer of certain equity securities to pay dividends to affiliates of Fairfax in December 2018 (see Note 12).

Net realized losses on sales of equity securities for the year ended December 31, 2017 include $5.0 million of gross realized gains and $24.3 million of gross realized losses on sales of fair value option equity securities. These gross realized losses included $15.3 million of losses on Exco Resources, Inc. ("Exco") that were reclassified from unrealized losses when the Company commenced applying the equity method of accounting upon increase in ownership interest in Exco during the second quarter of 2017. This reclassification had no impact on net income or total comprehensive income. The gross realized losses also included $8.8 million of realized losses recognized upon transfer of an equity security to pay dividends to affiliates of Fairfax in December 2017 (see Note 12).

Net realized losses on sales of equity securities for the year ended December 31, 2016 include $38.4 million of gross realized gains and $51.4 million of gross realized losses on sales of fair value option equity securities.

(b) Net realized gains on sales of fixed maturity securities, including short-term investments and other for the year ended December 31, 2018 include $1.9 million of gross realized gains and $0.1 million of gross realized losses on sales of fair value option fixed maturity securities.

Net realized gains on sales of fixed maturity securities, including short-term investments and other for the year ended December 31, 2017 include $13.5 million of gross realized gains and $1.0 million of gross realized losses on sales of fair value option fixed maturity securities. These gross realized gains included $4.5 million of realized gains recognized upon transfer of a fixed maturity security to pay dividends to affiliates of Fairfax in June 2017 (see Note 12).

Net realized gains on sales of fixed maturity securities, including short-term investments and other for the year ended December 31, 2016 primarily include $25.1 million of gross realized gains on sales of fair value option fixed maturity securities.

(c) Net gains from other investments for the year ended December 31, 2017 primarily include $2.4 million gain on sale of Agrigroupe LP to Fairfax Africa Holdings Corp. ("FAH"); $2.0 million gain on sale of a cost-method partnership investment; and realized gains of $1.2 million for Apple Bidco and $1.1 million for Boat Rocker Media Inc. ("Boat Rocker") on dilution resulting from additional shares issued (see Note 12).

The changes in net unrealized gains/losses on available-for-sale investments and investments in cost-method partnerships, as well as the Company's share of changes in unrealized gains/losses from its investments in equity-method common stocks and partnerships are recognized as a separate component of stockholders' equity and were as follows:

	Year Ended December 31,		
(In thousands)	2018	2017	2016
Equity securities	$ (132)	$ 2,192	$ (2,700)
Investments in equity-method partnerships	1,006	396	
Investments in equity-method common stocks	(85)	(1,434)	
Investments in cost-method partnerships	(942)	(276)	(1,930)
Total before tax	$ (153)	$ 878	$ (4,630)
After tax (see Note 13)	$ (670)	$ 571	$ (3,010)

The change in net unrealized gains/losses on fair value option investments still held was as follows:

	Year Ended December 31,		
(In thousands)	2018	2017	2016
Change in net unrealized gains/losses recognized on fair value option investments	$ 6,666	$ 90,321	$ (73,457)
Less: Net losses (gains) recognized on fair value option investments sold	51,606	8,753	(29,752)
Change in net unrealized gains/losses recognized on fair value option investments still held at the reporting date	$ (44,940)	$ 81,568	$ (43,705)

Net investment income was as follows:

	Year Ended December 31,		
(In thousands)	2018	2017	2016
Fixed maturity securities (a)	$ 23,022	$ 20,790	$ 39,595
Equity securities (b)	16,511	3,775	4,686
Short-term and other investments (a)	8,373	5,825	1,594
Derivatives	5,473	203	(8,139)
Income (losses) from equity-method investments (c)	(9,566)	6,652	(2,897)
Subtotal	43,813	37,245	34,839
Investment expenses	(7,994)	(7,151)	(7,764)
Net investment income	$ 35,819	$ 30,094	$ 27,075

(a) In 2017 and early part of 2018, a large portion of the long-dated taxable and tax-exempt municipal bonds was sold and redeemed, with the proceeds primarily reinvested in short-term and short-dated U.S. treasury bonds and high quality corporate bonds in the later part of 2018.

(b) Income from equity securities in the year ended December 31, 2018 includes a $12.4 million special dividend received from a common stock investment.

(c) Loss from equity-method investments in the year ended December 31, 2018 includes the Company's share of the net losses of $5.1 million from Farmers Edge Inc ("Farmers Edge"), $2.0 million from Astarta Holdings NV ("Astarta"), $1.5 million from FAH, $1.2 million from Davos Brands LLC ("Davos"), $1.0 million from Apple Bidco and $1.0 million from Peak Achievement Athletics Inc., partially offset by the Company's share of the net income of $1.3 million from Fairfax India Holdings Corp. ("FIH") and $1.1 million from Grivalia Properties S.A.

Income from equity-method investments for the year ended December 31, 2017 primarily included the Company's share of net income of $3.5 million from FIH, of $3.4 million from FAH, of $2.0 million from Boat Rocker and of $1.7 million from Astarta, partially offset by the Company's share of net losses of $2.3 million from Farmers Edge, of $1.7 million from Davos and of $1.2 million from Agrigroupe LP.

Net investment loss from equity-method investments for the year ended December 31, 2016 primarily included the Company's share of the net losses of $6.4 million from Apple Bidco, partially offset by the Company's share of the net income of $1.4 million from FIH and of $1.2 million from Boat Rocker.

See Note 12 for additional information on related party investment transactions.

At December 31, 2018 and 2017, investments with a fair value of $1.1 billion, respectively, were on deposit with regulatory authorities in compliance with insurance company regulations. At December 31, 2018, the Company had additional qualifying securities with a fair value of $83.3 million available for deposit.

Note 4. Derivative Contracts

See Note 2 for a description of the Company's accounting policies related to derivative contracts.

The following table summarizes the notional amount, cost and fair value of derivative contracts:

	Notional		Fair Value of Derivative		
(In thousands)	Amount	Cost	Assets	Liabilities	
December 31, 2018					
CPI-linked derivatives	$ 7,920,604	$ 41,058	$ 2,303		
Foreign currency options	437,500	7,519	7,431		
U.S. government bond forwards	94,000			$ 5,530	(a)
Long equity total return swaps	71,431			10,958	(a)
Foreign exchange forwards	13,146			16	(a)
Equity rights/warrants	921		20		
Total		$ 48,577	$ 9,754	$ 16,504	
December 31, 2017					
CPI-linked derivatives	$ 8,041,674	$ 41,058	$ 3,445		
U.S. government bond forwards	98,000			$ 1,686	(a)
Long equity total return swaps	58,265		2,077	1,917	(a)
Foreign exchange forwards	57,638			677	(a)
Equity rights/warrants	16,774	1,959	1,282		
Total		$ 43,017	$ 6,804	$ 4,280	

(a) Represents the change in fair value since the most recent cash settlement date prior to the reporting date.

The gains (losses) from settlements and changes in fair value of the derivative contracts are recorded as net gains (losses) on derivatives in the Consolidated Statements of Comprehensive Income (Loss) as follows:

	Year Ended December 31,		
(In thousands)	2018	2017	2016
Gains (losses) on settlements			
Equity derivatives:			
Equity total return swaps – long positions (a)	$ 3,115	$ 3,980	
Equity total return swaps – short positions (a)			$ (91,434)
Equity warrants	(1,234)		
Equity call options		1,357	
U.S. government bond forward contracts	7,135	(9,900)	
Foreign exchange forward contracts	4,149	(4,919)	573
Total	13,165	(9,482)	(90,861)
Change in fair value (b)			
Equity derivatives:			
Equity total return swaps – long positions (a)	(11,118)	160	
Equity total return swaps – short positions (a)			(15,528)
Equity warrants	697	(708)	(230)
CPI-linked derivative contracts	(1,142)	(3,696)	(15,889)
U.S. government bond forward contracts	(3,844)	1,403	(3,089)
Foreign exchange forward contracts	661	(1,023)	877
Foreign currency options	(88)		
Total	(14,834)	(3,864)	(33,859)
Net gains (losses) on derivatives			
Equity derivatives:			
Equity total return swaps – long positions (a)	(8,003)	4,140	
Equity total return swaps – short positions (a)			(106,962)
Equity warrants	(537)	(708)	(230)
Equity call options		1,357	
CPI-linked derivative contracts	(1,142)	(3,696)	(15,889)
U.S. government bond forward contracts	3,291	(8,497)	(3,089)
Foreign exchange forward contracts	4,810	(5,942)	1,450
Foreign currency options	(88)		
Total net losses on derivatives	$ (1,669)	$ (13,346)	$ (124,720)

(a) Amounts for total return swaps include net gains (losses) where the Company and its counterparties are required to cash-settle on a quarterly basis the fair value movement since the previous quarterly reset date notwithstanding that the total return swap positions remain open subsequent to the cash settlement.

(b) Change in fair value of total return swaps was measured from the contract inception or most recent cash settlement date prior to the reporting date. Change in fair value of all other derivative contracts is measured from the contract inception date or prior balance sheet date. Change in fair value of CPI-linked derivatives, foreign exchange forwards and foreign currency options include unrealized foreign exchange gains.

During the years ended December 31, 2018 and 2017, the Company recognized $5.5 million and $0.2 million, respectively, of net dividend and interest income earned on its total return swaps recorded in net investment income, compared to $8.1 million of net dividend and interest expense incurred for the year ended December 31, 2016, which was recorded as a reduction to net investment income.

CPI-Linked derivative contracts

The following table summarizes the notional amounts and underlying CPI Index price ("strike price") for the Company's CPI-linked derivative contracts at initiation and the index value at December 31, 2018 and December 31, 2017:

(Notional amount in thousands)	Notional Amount Original Currency	Notional Amount US Dollars	Weighted Average Strike Price In Original Currency	Index Value
Underlying CPI Index:				
December 31, 2018				
United States	5,520,000	$ 5,520,000	232.81	251.23
European Union	2,100,000	2,400,604	97.66	104.10
		$ 7,920,604		
December 31, 2017				
United States	5,520,000	$ 5,520,000	232.81	246.52
European Union	2,100,000	2,521,674	97.66	102.57
		$ 8,041,674		

Counterparty collateral and exposure

At December 31, 2018 and 2017, the Company pledged to its counterparties securities with a fair value of $24.6 million and $11.9 million, respectively, as independent and mark-to-market collateral for CPI-linked, U.S. Government bond forward and equity long total return swap derivative contracts and recorded these amounts as assets pledged for derivative obligations in the Company's Consolidated Balance Sheets.

At December 31, 2018, the counterparties pledged $0.3 million of cash compared to $0.8 million of cash and $2.9 million of securities, at fair value, at December 31, 2017. The Company recorded the cash collateral as other assets and recognized a corresponding liability in its Consolidated Balance Sheets. The Company does not record in its Consolidated Balance Sheets securities pledged by counterparties as collateral for derivatives in a gain position.

The following table sets out the Company's exposure to credit risk related to the counterparties to its derivative contracts:

(In thousands)	December 31, 2018	December 31, 2017
Total derivative assets (a)	$ 9,734	$ 5,522
Impact of net settlement arrangements	(9,469)	(3,603)
Fair value of collateral deposited for the benefit of the Company	(265)	(1,919)
Excess of collateral pledged by the Company in favor of counterparties	3,118	
Net derivative counterparty exposure after net settlement and collateral arrangements	$ 3,118	$

(a) Excludes warrants with a fair value of $20,000 and $1.3 million at December 31, 2018 and 2017, which are not subject to counterparty risk.

The net derivative counterparty exposure after net settlement and collateral arrangements relates principally to the timing of collateral placement.

Offsetting of Derivative Assets/Liabilities

The Company entered into master netting agreements with certain of its derivative counterparties whereby the collateral provided (held) is calculated on a net basis. In accordance with GAAP, the Company elected not to offset derivative assets and liabilities in the Consolidated Balance Sheets for the counterparties with the master netting agreement. The following table summarizes by counterparty (1) the gross and net amounts reflected as derivative assets (excluding warrants) and liabilities in the Consolidated Balance Sheets; (2) the gross amounts of the derivative instruments eligible for netting but not offset in the Consolidated Balance Sheets; and (3) financial collateral received and pledged which is contractually permitted to be offset upon an event of default, but is not allowed to be presented net under GAAP (net amount of exposure).

(In thousands)	Gross and net amounts reflected in the Consolidated Balance Sheets	Gross amounts not offset in the Consolidated Balance Sheets: Derivative asset (liability)	Gross amounts not offset in the Consolidated Balance Sheets: Collateral provided (held) - financial instruments (a)	Net amount of exposure
December 31, 2018				
Derivative assets:				
Citibank, N.A.	$ 9,469	$ (9,469)		
Deutsche Bank AG London	265		$ (265)	
Total derivative assets (b)	$ 9,734	$ (9,469)	$ (265)	
Derivative liabilities:				
Citibank, N.A.	$ (14,974)	$ 9,469	$ 5,505	
Bank of New York Mellon (c)	(16)			$ (16)
Bank of America	(1,514)		1,333	(181)
Total derivative liabilities	$ (16,504)	$ 9,469	$ 6,838	$ (197)
December 31, 2017				
Derivative assets:				
Citibank, N.A.	$ 2,814	$ (2,303)	$ (511)	
Deutsche Bank AG London	631		(631)	
Bank of America	2,077	(1,300)	(777)	
Total derivative assets (b)	$ 5,522	$ (3,603)	$ (1,919)	
Derivative liabilities:				
Citibank, N.A.	$ (2,303)	$ 2,303		
Bank of America	(1,300)	1,300		
Bank of New York Mellon (c)	(677)			$ (677)
Total derivative liabilities	$ (4,280)	$ 3,603		$ (677)

(a) Amounts of collateral pledged to the Company by the counterparties (collateral held) and pledged by the Company to the counterparties (collateral provided) reflected above are to the extent of the net counterparty exposure before collateral.

(b) Excludes warrants with a fair value of $20,000 and $1.3 million at December 31, 2018 and 2017, respectively, which are not subject to counterparty risk.

(c) Represents foreign currency forward contracts that are not subject to a master netting arrangement.

Note 5. Fair Value Measurements

Fair values for substantially all of the Company's financial instruments are measured using market or income approaches. Considerable judgment may be required in interpreting market data used to develop estimates of fair value. Accordingly, actual values realized in future market transactions may differ from the estimates presented in these consolidated financial statements. In determining fair value, the Company primarily uses prices and other relevant information generated by market transactions involving identical or comparable assets ("market approach"). The Company also considers the impact of a significant decrease in volume and level of activity for an asset or liability when compared with normal activity to identify transactions that are not orderly.

Fair value measurements are determined under a three level hierarchy that prioritizes the inputs to valuation techniques used to measure fair value, distinguishing between market participant assumptions developed based on market data obtained from sources independent of the reporting entity ("observable inputs") and the reporting entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances ("unobservable inputs"). The hierarchy level assigned to each security carried at fair value is based on the Company's assessment of the transparency and reliability of the inputs used in the valuation of each instrument at the measurement date. The highest priority is given to unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). Securities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Company recognizes transfers between levels at the end of each reporting period in which the transfer is identified. The three hierarchy levels are defined as follows:

Level 1— Inputs represent unadjusted quoted prices for identical instruments exchanged in active markets. The fair values of publicly traded equity securities, highly liquid cash management funds and short-term U.S. Government securities are based on published quotes in active markets.

Level 2— Inputs include directly or indirectly observable inputs (other than Level 1 inputs) such as quoted prices for similar financial instruments exchanged in active markets, quoted prices for identical or similar financial instruments exchanged in inactive markets and other market observable inputs. The fair value of the vast majority of the Company's investments in fixed maturity securities, along with most derivative contracts (including long equity total return swaps, foreign exchange forward contracts, options and U.S. Government bond forward contracts), are priced based on information provided by independent pricing service providers, while much of the remainder are based primarily on non-binding third party broker-dealer quotes that are prepared using Level 2 inputs. Where third party broker-dealer quotes are used, typically at least one quote is obtained from a broker-dealer with particular expertise in the instrument being priced. Certain common stock investments which are measured at fair value using the net asset value per share ("NAV") practical expedient have been excluded.

Level 3— Inputs include unobservable inputs used in the measurement of financial instruments. Management is required to use its own assumptions regarding unobservable inputs as there is little, if any, market activity in these instruments or related observable inputs that can be corroborated at the measurement date. Certain cost-method partnership investments which are measured at fair value using the NAV practical expedient have been excluded. Investments for which NAV is only a component of the fair value measurement continue to be included.

The following table presents the Company's investments measured at fair value on a recurring basis as of December 31, 2018 and December 31, 2017 classified by the valuation hierarchy discussed previously:

		Fair Value Measurement Using		
(In thousands)	Total	Level 1	Level 2	Level 3
December 31, 2018				
Fair value option securities:				
Fixed maturity securities:				
State and local government debt	$ 104,970		$ 104,970	
U.S. government debt	983,479		983,479	
Corporate debt	49,752		31,890	$ 17,862
Total fixed maturity securities	1,138,201		1,120,339	17,862
Equity securities (a)	192,583	$ 143,657		8,754
Short-term investments	128,335	123,397	4,938	
Other investments - affiliate corporate loans	6,365			6,365
Total fair value option investments	$ 1,465,484	$ 267,054	$ 1,125,277	$ 32,981
Available-for-sale investments:				
Equity securities	$ 16,115		$ 54	$ 16,061
Total available-for-sale investments	$ 16,115		$ 54	$ 16,061
Derivatives:				
Foreign currency options	$ 7,431		$ 7,431	
CPI-linked derivative contracts	2,303			$ 2,303
Equity warrants	20		20	
Total derivative assets	9,754		7,451	2,303
Equity total return swaps – long positions	(10,958)		(10,958)	
U.S. Government bond forward contracts	(5,530)		(5,530)	
Foreign exchange forward contracts	(16)		(16)	
Total derivative liabilities	(16,504)		(16,504)	
Net derivatives	$ (6,750)		$ (9,053)	$ 2,303
December 31, 2017				
Fair value option securities:				
Fixed maturity securities:				
State and local government debt	$ 415,072		$ 415,072	
U.S. Government debt	23,588		23,588	
Corporate debt	21,689			$ 21,689
Total fixed maturity securities	460,349		438,660	21,689
Equity securities (a)	310,594	$ 250,317		12,106
Short-term investments	738,810	738,810		
Total fair value option investments	$ 1,509,753	$ 989,127	$ 438,660	$ 33,795
Available-for-sale investments:				
Equity securities	$ 16,247		$ 48	$ 16,199
Total available-for-sale investments	$ 16,247		$ 48	$ 16,199
Derivatives:				
Equity total return swaps – long positions	$ 2,077		$ 2,077	
CPI-linked derivative contracts	3,445			$ 3,445
Equity warrants	1,282		18	1,264
Total derivative assets	6,804		2,095	4,709
Equity total return swaps – long positions	(1,917)		(1,917)	
U.S. Government bond forward contracts	(1,686)		(1,686)	
Foreign exchange forward contracts	(677)		(677)	
Total derivative liabilities	(4,280)		(4,280)	
Net derivatives	$ 2,524		$ (2,185)	$ 4,709

(a) Certain common stock investments with a fair value of $40.2 million and $48.2 million that are measured using the NAV practical expedient have not been classified in the fair value hierarchy at December 31, 2018 and December 31, 2017, respectively. The fair value amounts presented in the "Total" column are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the Consolidated Balance Sheets.

The following table presents changes in the Company's Level 3 fixed maturity, equity securities, and derivatives measured at fair value on a recurring basis:

(In thousands)	Corporate Debt	Equity Securities	Derivatives	Affiliate Corporate Loans
Balance at December 31, 2016	$ 19,603	$ 14,444	$ 7,141	
Purchases	6,819	11,812	1,959	
Sales	(19,484)	(250)		
Realized and unrealized gains/losses included in:				
Other comprehensive income (a)		2,185		
Change in net unrealized gains/losses on fair value option investments	2,899	294		
Net realized gains (losses) on investments	4,484	(180)		
Net losses on derivatives			(4,170)	
Transfers from Level 3 to Level 2 (b)			(221)	
Transfers from Level 2 to Level 3 (c)	7,368			
Balance at December 31, 2017	$ 21,689	$ 28,305	$ 4,709	
Purchases	9,395		563	$ 6,110
Sales	(7,075)		(1,645)	
Realized and unrealized gains/losses included in:				
Other comprehensive loss (a)		(138)		
Change in net unrealized gains/losses on fair value option investments	(2,853)	(3,352)		255
Accretion of discounts	81			
Net realized gains on investments	1,478			
Net losses on derivatives			(1,324)	
Transfers from Level 3 to Level 2 (d)	(4,853)			
Balance at December 31, 2018	$ 17,862	$ 24,815	$ 2,303	$ 6,365

(a) Changes in unrealized gain/losses for equity securities include changes in fair value and foreign currency fluctuation.

(b) In 2017, investments in warrants were transferred from Level 3 to Level 2 due to a change in a key valuation input.

(c) In 2017, two private placement corporate debt securities were transferred from Level 2 to Level 3 due to the modification of terms and a change in the observability of a key valuation input.

(d) In 2018, one private placement corporate debt security purchased in 2018 was transferred from Level 3 to Level 2 due to a change in observability of a key valuation input.

The following table provides information on the valuation techniques, significant unobservable inputs and ranges for each major category of Level 3 assets measured at fair value on a recurring basis at December 31, 2018:

(In thousands)		Balance at December 31, 2018	Valuation Techniques	Significant Unobservable Inputs
Corporate debt (a)	$	17,862	Market approach	Credit spread of issuer
Equity securities, available-for-sale (b)	$	16,061	Market approach	Estimated NAV multiple
Equity securities, fair value option (c)	$	8,754	Market approach	Credit spread of issuer
Derivatives (d)	$	2,303	Market approach	Broker quotes
Affiliate corporate loans (e)	$	6,365	Market approach	Credit spread of issuer

(a) The Level 3 corporate debt securities consist of three private placement debt securities with the fair values determined using an Expected Recoverability Model and two private placement debt securities with the fair value determined using a Black-Scholes Model. Prices for identical instruments are not available and significant subjectivity may be involved when fair value is determined using pricing data available for comparable instruments. Two of the private debt securities were previously classified as Level 2 investments and transferred into Level 3 in March 2017.

(b) The Level 3 equity securities, available-for-sale consist primarily of common stock of a company based in the United Kingdom with a fair value estimated as NAV multiple because a significant portion of its NAV, excluding cash balances, is comprised of real estate holdings supported by appraisals. The estimated fair value of this equity security also includes foreign currency fluctuations.

(c) The Level 3 equity securities, fair value option consist primarily of two preferred stocks purchased in 2017, with the fair value determined using a Black-Scholes Model. Prices for identical instruments are not available and significant subjectivity may be involved when fair value is determined using pricing data available for comparable instruments.

(d) The Level 3 derivatives consist primarily of CPI-linked derivatives that were valued using broker-dealer quotes which management has determined use market observable inputs except for the inflation volatility input which is not market observable.

(e) The Level 3 affiliate corporate loans consist of four loans, three of which relate to the same issuer and are valued using an expected Recoverability Model. The estimated fair value of one of the securities also includes foreign currency fluctuations.

Note 6. Properties and Equipment

Properties and equipment, included in other assets, consist of the following:

	December 31,			
(In thousands)		2018		2017
Land	$	15,208	$	15,208
Buildings		40,683		40,138
Other property and equipment		82,720		90,617
Subtotal		138,611		145,963
Accumulated depreciation		(105,511)		(110,631)
Total	$	33,100	$	35,332

Depreciation expense for the years ended December 31, 2018, 2017, and 2016 was $3.8 million, $3.4 million and $3.7 million, respectively.

Note 7. Income Tax

The Company is included in the consolidated federal income tax return of Fairfax (US) Inc. and its eligible subsidiaries and in various state combined or consolidated income tax returns. Zenith National and Fairfax (US) Inc. are parties to a tax allocation agreement whereby, in general, federal income taxes are allocated by Fairfax (US) Inc. to Zenith National equal to the taxes that would have been payable/refunded between the Company and the Internal Revenue Service ("IRS") if it had filed a stand-alone consolidated federal income tax return. The insurance subsidiaries pay premium taxes on direct premiums written in lieu of most state income or franchise taxes.

The Tax Cuts and Jobs Act of 2017 ("Act") was signed into law on December 22, 2017. The Act includes a reduction of the corporate tax rate from 35% to 21%; repeal of the AMT regime and changes to loss reserve discounting for taxable years beginning after December 31, 2017.

The deferred tax assets ("DTAs") and deferred tax liabilities ("DTLs") as of December 31, 2017, are measured using the new enacted tax rate of 21% that is expected to apply to taxable income in the periods in which the DTAs and DTLs are expected to be settled or realized. Changes in DTAs and DTLs, including changes attributable to changes in tax rates, are recognized as part of the current year tax expense in the Consolidated Statement of Comprehensive Income. The remeasurement of deferred taxes due to the change in tax rate is recorded as a discrete item in the income tax provision for the year ended December 31, 2017.

The difference between the statutory income tax rate and the Company's effective tax rate on income, as reflected in the Consolidated Statements of Comprehensive Income, was as follows:

	Year Ended December 31,		
(In thousands)	2018	2017	2016
Statutory tax rate	at 21%	at 35%	at 35%
Statutory income tax expense	$ 16,918	$ 77,118	$ 590
Increase (reduction) in tax:			
Tax-exempt interest and other investments	(2,778)	(5,749)	(6,623)
Foreign taxes paid	350	177	3,254
State taxes paid (refunded)		(434)	578
Non-deductible expenses and other	(2,044)	823	(701)
Income tax expense (benefit) before valuation allowance	12,446	71,935	(2,902)
Valuation allowance	21,600		
Change in tax rate		30,760	
Income tax expense (benefit)	$ 34,046	$ 102,695	$ (2,902)

Deferred tax is provided based upon temporary differences between the tax and book basis of assets and liabilities. The components of the deferred tax assets and liabilities were as follows:

	December 31,			
	2018		2017	
	Deferred Tax		Deferred Tax	
(In thousands)	Assets	Liabilities	Assets	Liabilities
Unpaid losses and loss adjustment expenses discount	$ 14,250		$ 14,007	
Limitation on deduction for unearned premiums	6,623		7,014	
Investments	37,241		15,303	
Policyholders' dividends accrued	9,080		8,819	
Compensation and benefits	4,253		3,814	
Deferred policy acquisition costs		$ 2,551		$ 2,677
Properties and equipment		282		540
Other	379		400	
Total before valuation allowance	$ 71,826	$ 2,833	$ 49,357	$ 3,217
Valuation allowance	(21,600)			
Net deferred tax asset	$ 47,393		$ 46,140	

GAAP requires the Company to evaluate the recoverability of its DTAs and establish a valuation allowance, if necessary, to reduce the DTA to an amount that is more likely than not to be realized (a likelihood of more than 50%). In making this evaluation, the Company is required to consider all available evidence, both positive and negative, including objectively verifiable evidence of taxable income in the immediate ensuing years. The discounting of loss reserves for tax purposes reverse over 10 to 25 years; and the limitation on deductions for unearned premiums reverse in the following year. Investments-related DTAs at December 31, 2018 are primarily attributable to deferred and unrealized tax losses on the Company's equity securities.

In assessing the recoverability of the Company's DTAs, management evaluates whether it is more likely than not that some portion or all of the deferred tax assets will not be realized by generating sufficient taxable income of the appropriate character. Management considers the reversal of deferred tax liabilities, carryback potential of an appropriate nature, and tax-planning strategies in making this assessment. At December 31, 2018, the Company recorded a $21.6 million non-cash charge to establish a valuation allowance on its investment-related DTAs. The valuation allowance does not adversely affect the Company's ability to use these tax deductions to reduce taxable income in the future.

At December 31, 2018 and 2017, there were no material unrecognized tax benefits.

The Company recognizes any interest and penalties related to uncertain tax positions in income tax expense; however, there were none during the years ended December 31, 2018, 2017 and 2016.

The IRS is examining taxable years 2017 and 2018. Taxable years 2014 through 2018 are subject to examination by state taxing authorities.

Note 8. Unpaid Losses and Loss Adjustment Expenses

See Note 2 for a description of the Company's accounting policies related to unpaid losses and loss adjustment expenses.

The Company's workers' compensation incurred and paid losses and allocated loss adjustment expenses, net of reinsurance, are presented in the following tables.

Workers' Compensation

(in thousands)

	Incurred Losses and Allocated Loss Adjustment Expenses, Net of Reinsurance Years Ended December 31,										As of December 31, 2018	
Accident Year	**2009 [1]**	**2010 [1]**	**2011 [1]**	**2012 [1]**	**2013 [1]**	**2014 [1]**	**2015 [1]**	**2016 [1]**	**2017 [1]**	**2018**	**Net IBNR Reserves**	**Cumulative Number of Reported Claims [2]**
2009	$ 262,953	$ 271,983	$ 287,896	$ 291,896	$ 291,896	$ 289,798	$ 284,548	$ 280,807	$ 280,226	$ 278,800	10,943	23,062
2010		266,698	278,900	276,900	276,900	271,971	268,359	264,538	261,909	260,357	12,470	23,224
2011			322,367	311,367	311,367	300,665	293,127	287,565	286,064	283,977	13,973	26,530
2012				385,899	350,993	332,441	321,499	312,301	309,930	307,331	15,470	30,083
2013					370,296	341,735	323,545	309,959	302,556	297,707	20,620	30,659
2014						358,819	331,551	307,190	294,755	286,855	21,536	30,411
2015							354,155	329,034	315,023	299,935	31,784	30,837
2016								360,638	340,182	323,750	33,930	31,467
2017									354,148	328,410	47,720	31,265
2018										337,529	79,406	30,282
									Total	$ 3,004,651		

(1) Data presented for these calendar years is required supplementary information, which is unaudited.
(2) The amounts reported for the cumulative number of reported claims include direct and assumed open and closed claims by accident year at the claimant level. The amounts do not include claim counts for business assumed through pools and associations. Claims reported are counted even if they eventually close with no loss or loss adjustment payment or if they are within a policy deductible where the insured is responsible for payment of losses in the deductible layer.

Workers' Compensation

(in thousands)

Accident Year	Cumulative Paid Losses and Allocated Loss Adjustment Expenses, Net of Reinsurance — Years Ended December 31, 2009 (1)	2010 (1)	2011 (1)	2012 (1)	2013 (1)	2014 (1)	2015 (1)	2016 (1)	2017 (1)	2018
2009	$ 68,237	$ 144,518	$ 195,593	$ 219,733	$ 234,874	$ 227,211	$ 249,715	$ 253,858	$ 256,086	$ 257,580
2010		65,279	140,100	179,572	203,228	241,113	227,010	232,877	235,602	237,354
2011			67,805	152,550	201,241	242,278	240,048	247,932	254,485	257,343
2012				77,738	168,162	212,470	241,385	256,922	266,111	272,125
2013					70,631	166,783	211,947	237,852	251,613	258,546
2014						73,323	160,065	203,881	229,189	240,337
2015							74,561	166,502	214,635	236,628
2016								81,103	177,908	225,456
2017									85,204	183,532
2018										85,461
									Total	$ 2,254,362

All outstanding liabilities for unpaid losses and allocated loss adjustment expenses beginning 2009, net of reinsurance	$ 750,289
All outstanding liabilities for unpaid losses and allocated loss adjustment expenses prior to 2009, net of reinsurance	189,564
Total outstanding liabilities for unpaid losses and allocated loss adjustment expenses, net of reinsurance	$ 939,853

(1) Data presented for these calendar years is required supplementary information, which is unaudited.

The reconciliation of the net incurred and paid loss development tables to the liability for unpaid losses and loss adjustment expenses is as follows:

(in thousands)		December 31, 2018
Workers' compensation	$	939,853
Other insurance operations		55,559
Liabilities for unpaid losses and allocated loss adjustment expenses, net of reinsurance		995,412
Liabilities for unpaid unallocated loss adjustment expenses		105,505
Liabilities for unpaid losses and loss adjustment expenses, net of reinsurance		1,100,917
Receivable from reinsurers for unpaid losses		46,949
Total gross liabilities for unpaid losses and loss adjustment expenses	$	1,147,866

The following table presents the average annual percentage payout of losses and loss adjustment expenses incurred by age, net of reinsurance, for an accident year as of December 31, 2018. The percentages show the average portion of the net losses and loss adjustment expenses paid in each succeeding year.

Average Annual Percentage Payout of Incurred Losses and Loss Adjustment Expenses by Age, Net of Reinsurance
(unaudited)

Years	1	2	3	4	5	6	7	8	9	10
	26.2%	30.8%	15.7%	8.4%	4.7%	2.8%	2.2%	1.2%	0.8%	0.6%

The following table represents a reconciliation of changes in the liability for unpaid losses and loss adjustment expenses:

	Year Ended December 31,		
	2018	2017	2016
Beginning of year, net of reinsurance	$ 1,139,373	$ 1,144,409	$ 1,173,287
Incurred claims:			
Current accident year	455,714	480,306	461,622
Prior accident years	(85,290)	(76,348)	(101,540)
Total incurred claims	370,424	403,958	360,082
Payments:			
Current accident year	(137,616)	(140,573)	(128,140)
Prior accident years	(271,264)	(268,421)	(260,820)
Total payments	(408,880)	(408,994)	(388,960)
End of year, net of reinsurance	1,100,917	1,139,373	1,144,409
Receivable from reinsurers for unpaid losses	46,949	52,158	64,163
End of year, gross of reinsurance	$ 1,147,866	$ 1,191,531	$ 1,208,572

The net favorable development of $85.3 million in 2018 was principally attributable to workers' compensation favorable loss development trends for 2015 through 2017 accident years. The net favorable development of $76.3 million in 2017 was principally attributable to workers' compensation favorable loss development trends for 2013 through 2016 accident years. The net favorable development of $101.5 million in 2016 was principally attributable to workers' compensation favorable loss development trends for 2012 through 2015 accident years.

Note 9. Long-Term Debt

At December 31, 2018 and 2017, the outstanding principal amount and fair value of the Company's Subordinated Deferrable Interest Debentures ("long-term debt") was $38.5 million. The long-term debt is due in 2028 and bears interest at the rate of 8.55% per annum.

The semi-annual interest payments on the long-term debt may be deferred by Zenith National for up to ten consecutive semi-annual periods. This debt is redeemable by Zenith National at 100% of the principal amount plus a "make-whole premium," if any, together with accrued and unpaid interest. The make-whole premium is the excess of the sum of the present value of the principal amount at maturity and the present value of the remaining scheduled payments of interest over 100% of the principal amount. The original issue costs and discount on the long-term debt of $1.7 million are being amortized over the term of the long-term debt. Interest, issue costs and discount expense were $3.3 million for each of the years ended December 31, 2018, 2017 and 2016.

Note 10. Reinsurance Ceded

2018-2019 Reinsurance ceded workers' compensation coverage

The Company maintains excess of loss and catastrophe reinsurance which provides protection up to $150 million for losses including catastrophe losses arising out of earthquakes and acts of terrorism including nuclear, biological and chemical attacks. For the California agriculture business, the Company retains the first $10 million and the layer from $20 million to $50 million of each loss arising from industrial accidents and the first $50 million of each loss arising out of earthquakes and acts of terrorism. For all other business classes, the Company retains the first $50 million of each loss.

2016-2017 Reinsurance ceded workers' compensation coverage

The Company maintained excess of loss and catastrophe reinsurance which provides protection up to $150 million for losses including catastrophe losses arising out of earthquakes and acts of terrorism including nuclear, biological and chemical attacks. For the California agriculture business, the Company retained the first $10 million and the layer from $20 million to $30 million of each loss arising from industrial accidents and the first $30 million of each loss arising out of earthquakes and acts of terrorism. For all other business classes, the Company retained the first $30 million of each loss.

Reinsurance transactions reflected in the accompanying Consolidated Statements of Comprehensive Income were as follows:

	Year Ended December 31,		
(In thousands)	2018	2017	2016
Direct premiums earned	$ 807,953	$ 816,985	$ 811,849
Assumed premiums earned	7,412	6,554	7,336
Ceded premiums earned	(11,066)	(11,935)	(11,927)
Net premiums earned	$ 804,299	$ 811,604	$ 807,258
Ceded losses and loss adjustment expenses incurred	$ (970)	$ 1,081	$ 2,323

Amounts recoverable for paid and unpaid losses from reinsurers at December 31, 2018 and 2017 and their respective A.M. Best ratings were as follows:

	December 31,				A.M. Best	A.M. Best
(In thousands)		2018 (a)		2017 (a)	Rating (b)	Rating Date
General Reinsurance Corp.	$	38,535	$	43,567	A++	1/2018
Lloyds Underwriters		1,528		1,025	A	7/2018
Factory Mutual Insurance Company		1,051		492	A+	2/2018
Inter-Ocean Re Ins Co. Ltd. (c)				2,799	NR	
All others (d)		6,771		6,548		
Total	$	47,885	$	54,431		

(a) Under insurance regulations in California, reinsurers placed securities on deposit equal to the California component of the Company's ceded workers' compensation loss reserves.

(b) A.M. Best, in assigning ratings, is primarily concerned with the ability of insurance and reinsurance companies to pay the claims of policyholders. In the A.M. Best ratings scheme, ratings of B+ to A++ are considered "Secure" and ratings of B and below are considered "Vulnerable." NR means A.M. Best does not rate the reinsurer.

(c) Reinsurance recoverable from the Inter-Ocean Re Ins Co. Ltd. at December 31, 2017 was fully secured by an investment grade security held in a bank trust account on the Company's behalf. In May 2018, the Company commuted this retroactive reinsurance agreement, received $3.0 million, eliminated a deferred gain of $0.4 million and recorded a total gain of $0.6 million.

(d) No individual reinsurer in excess of $1.0 million at December 31, 2018 and 2017.

Note 11. Stockholders' Equity and Statutory Financial Information

Dividend Restrictions

The California Insurance Holding Company System Regulatory Act limits the ability of Zenith Insurance to pay dividends to Zenith National and for Zenith Insurance to receive dividends from its insurance subsidiary by providing that the appropriate insurance regulatory authorities in the state of California must approve any dividend that, together with all other such dividends paid during the preceding twelve months, exceeds the greater of: (a) 10% of the paying company's statutory surplus as regards policyholders at the preceding December 31; or (b) 100% of the net income for the preceding year. In addition, any such dividend must be paid from policyholders' surplus attributable to accumulated earnings. Such restrictions on dividends are not cumulative. Dividend payments from Zenith Insurance to Zenith National must also be in compliance with the California Corporations Code that permit dividends to be paid only out of retained earnings and only if specified ratios between assets and liabilities and between current assets and current liabilities exist after payment.

In 2018, Zenith National paid $81.9 million in ordinary dividends to affiliates of Fairfax as follows: $39.0 million in equity securities, at fair value and $42.9 million in cash. In 2017, Zenith National paid $111.0 million in ordinary dividends to affiliates of Fairfax as follows: $30.9 million in equity securities, at fair value; $19.5 million in fixed maturity securities, at fair value including accrued interest; and $60.6 million in cash. In 2016, Zenith National paid cash dividends of $130.0 million to affiliates of Fairfax.

In 2018, Zenith Insurance paid $85.9 million in ordinary dividends to Zenith National as follows: $39.0 million in equity securities, at fair value and $46.9 million in cash. In 2017, Zenith Insurance paid a $115.0 million in ordinary dividends to Zenith National as follows: $30.9 million in equity securities, at fair value; $19.5 million in fixed maturity securities, at fair value including accrued interest; and $64.6 million in cash. In 2016, Zenith Insurance paid cash dividends of $80.0 to Zenith National. Zenith Insurance has the ability to pay up to $133.7 million of dividends to Zenith National without prior approval of the California Department of Insurance ("California DOI") during 2019.

In 2018, 2017 and 2016, ZNAT Insurance Company ("ZNAT"), a wholly-owned insurance subsidiary of Zenith Insurance, paid dividends of $2.5 million, $2.7 million and $2.6 million, respectively, to Zenith Insurance to reduce ZNAT's excess capital. ZNAT Insurance has the ability to pay up to $2.9 million to Zenith Insurance without prior approval of the California DOI during 2019.

Statutory Financial Data

The capital stock and surplus and net income of the Company's insurance subsidiaries, prepared in accordance with the statutory accounting practices of the National Association of Insurance Commissioners, were as follows:

	As of and for the Year Ended December 31,		
(In thousands)	2018	2017	2016
Capital stock and surplus	$ 541,085	$ 571,728	$ 563,563
Net income	$ 134,018	$ 85,664	$ 115,338

Statutory accounting net income differs from GAAP primarily due to the timing of the recognition of changes in fair value of investment securities.

The insurance business is subject to state-by-state regulation and legislation focused on solvency, pricing, market conduct, claims practices, underwriting, accounting, investment criteria, and other areas. Such regulation and legislation changes frequently. Compliance is essential and is an inherent risk and cost of the business. The Company believes it is in compliance with all material regulations.

Note 12. Related Party Transactions

Investments

Management of all of the Company's investments is centralized at Fairfax through investment management agreements entered into in 2010. The parties to these agreements are Zenith National's insurance subsidiaries, Fairfax and Hamblin Watsa Investment Counsel, Ltd. ("HWIC"), a Fairfax affiliate. Investment management expenses incurred under these agreements were $5.2 million, $4.8 million and $5.1 million for the years ended December 31, 2018, 2017 and 2016, respectively.

In December 2018, Zenith National paid an $81.9 million ordinary dividend to affiliates of Fairfax in the form of two equity securities and cash. As a result, the Company transferred its entire positions in Eurobank Ergasias and Blackberry Limited ("BBRY") common stock with a fair value of $25.0 million and $14.0 million, respectively, to Fairfax (US) Inc. and recognized realized losses of $63.0 million and $23.0 million, respectively.

In December 2017, Zenith National paid a $76.0 million ordinary dividend to affiliates of Fairfax in the form of an equity security and cash. As a result, the Company transferred a portion of its investment in Kennedy Wilson Inc. ("KWI") common stock with a fair value of $30.0 million to Fairfax (US) Inc. and recognized a realized loss of $8.8 million.

In June 2017, Zenith National paid a $35.0 million ordinary dividend to affiliates of Fairfax in the form of an equity security, a fixed maturity security and cash. As a result, the Company transferred a portion of its investments in KWI common stock with a fair value of $0.9 million and BBRY bonds with a fair value of $19.5 million, including accrued interest, to Fairfax (US) Inc. and recognized a realized loss of $0.2 million and a realized gain of $4.5 million on the transfer of KWI common stock and BBRY bonds, respectively.

In September 2016, the Company sold $10.0 million of common stock investments in each of BBRY and Bank of Ireland ("BOI"), at fair value, to U.S. Fire Insurance Company ("U.S. Fire"), a Fairfax affiliate and

Odyssey Reinsurance Company ("Odyssey Re"), a Fairfax affiliate, respectively. The Company recognized a realized loss of $15.4 million and a realized gain of $4.2 million, respectively, on these sales. The Company received approval from the California DOI prior to executing these transactions.

In August 2016, the Company sold $5.0 million and $10.0 million of common stock investments in BBRY and BOI, respectively, at fair value, to Brit Syndicates Limited, a Fairfax affiliate. The Company recognized a realized loss of $7.3 million and a realized gain of $4.3 million, respectively, on these sales. Approval from the California DOI was not required as the total amount was below the applicable regulatory threshold.

In May 2016, the Company purchased $52.0 million par value of a municipal bond at a fair value of $19.1 million from Northbridge General Insurance Corporation, a Fairfax affiliate. Approval from the California DOI was not required as the amount was below the applicable regulatory threshold.

The Company owns common stock shares in various mutual fund classes of HWIC Asia, which is a wholly-owned subsidiary of Fairfax. The Company elected the fair value option of accounting for its investment in HWIC Asia common stocks. At December 31, 2018 and 2017, the aggregate fair value of these investments was $40.2 million and $48.2 million, respectively. In 2016, the Company received proceeds of $49.9 million on the sale of a class of HWIC Asia and recognized a loss of $0.4 million. Changes in fair value for these investments are recorded in the change in net unrealized gains/losses on fair value option investments in the Consolidated Statements of Comprehensive Income (Loss). The Company recorded the changes in unrealized gains/losses of related to its investments in HWIC Asia of $8.0 million decrease, $3.2 million increase and $2.5 million decrease during the years ended December 31, 2018, 2017 and 2016, respectively. The Company recorded dividend income related to its investments in HWIC Asia of $1.0 million, $0.3 million, and $1.0 million for the years ended December 31, 2018, 2017, and 2016, respectively.

In February 2018, Fairfax and the Company invested in private placement non-rated debt securities issued by Seaspan Corporation ("Seaspan"), a publicly traded company domiciled in the Marshall Islands. Fairfax and the Company received warrants ("Seaspan Warrants") to purchase Seaspan common stock in connection with this investment. Seaspan became an affiliate of Fairfax and the Company simultaneously with this investment. The Company's share of this investment was $5.0 million, allocated between $4.4 million ($5.0 million par value) in Seaspan corporate bonds and $0.6 million in Seaspan Warrants. The Company sold its Seaspan Warrants, at fair value, to Wentworth Insurance Company Ltd. ("Wentworth"), a Fairfax affiliate, in April 2018 for $0.6 million. In July 2018, the Company purchased 0.8 million shares of Seaspan Warrants from Wentworth for $2.8 million and subsequently converted these warrants to purchase an equivalent number of Seaspan common stock shares for $5.2 million in cash paid to Seaspan. The Company recorded the acquisition of Seaspan affiliated common stock at a cost of $7.6 million and recognized a loss of $0.4 million on the conversion of Seaspan Warrants. The Company elected the fair value option of accounting for its investment in Seaspan affiliated common stock. The carrying value of this investment at December 31, 2018 was $6.2 million. The carrying value of the Company's affiliated investment in Seaspan fixed maturity securities was $4.9 million at December 31, 2018.

In February 2018, Fairfax completed the sale of its 51.0% ownership interest in the Keg Restaurants Ltd. ("Keg") to Cara Operations Limited ("Cara"), a publicly traded majority-owned subsidiary of Fairfax domiciled in Canada, for consideration that comprised of cash and Cara common stock. In 2014, the Company invested in FFHL LP, a wholly-owned limited partnership subsidiary of Fairfax formed to hold the Keg common stock. As a result of the sale of Keg to Cara, the Company received a $0.6 million cash dividend distribution from FFHL LP and the Company's remaining equity interest in the FFHL LP was redeemed in full in the form of $11.7 million of Cara common stock. The Company recorded its share of the FFHL LP realized loss on the sale of Keg to Cara of $0.3 million as part of equity in losses of FFHL LP in investment income. The Company recognized realized loss on foreign exchange of $1.2 million upon final redemption of its investment in FFHL LP that was reclassified from unrealized foreign currency translation adjustment previously recorded in equity. Cara was subsequently renamed Recipe Unlimited Corp. ("Recipe"). The

Company elected the fair value option of accounting for its investment in Recipe affiliated common stock. The carrying value of this investment was $11.2 million at December 31, 2018. In 2018, the Company received total dividends of $0.2 million from Recipe.

The Company owns common stock in publicly-traded and private companies and invests in limited partnerships which are affiliates of Fairfax (including but not limited to investments described in the following paragraphs). These investments are recorded using the equity method of accounting, unless a fair value option is elected for such securities; see Note 2 and Note 3 for additional information related to equity-method investments. The aggregate value of the Company's equity-method investments in Fairfax affiliates recorded in the Consolidated Balance Sheets was $175.5 million and $196.2 million at December 31, 2018 and 2017, respectively. The Company's share of net income/loss of the equity-method investees was recorded in net investment income. Net realized gains/losses on sales and on dilution resulting from additional shares issued or bought back by equity-method investees are recorded in net realized gains/losses on investments. The Company's share of other changes in investees' equity was recorded in net change in net unrealized gain/losses in Other Comprehensive Income (Loss). Net unrealized gains/losses on foreign currency translation adjustment related to the Company's equity-method investments are recorded in the change in unrealized foreign currency translation adjustment Other Comprehensive Income (Loss).

The following table summarizes impact from the Company's investments in equity-method common stocks and partnerships on various components of Comprehensive Income:

	Year Ended December 31,		
(In thousands)	2018	2017	2016
Equity-method common stocks and partnerships:			
Net investment income (loss)	$ (9,566)	$ 6,652	$ (2,897)
Net realized gains (losses) on investments	(547)	3,137	1,471
Net change in unrealized gains/losses on other investments, before tax	921	(1,038)	
Net change in unrealized foreign currency translation adjustment, before tax	(2,438)	3,766	(652)

In September 2018, the Company paid $4.3 million to purchase 5.6 million common stock shares of Toys "R" Us (Canada) Ltd. ("Toys R Us"), a wholly-owned subsidiary of Fairfax, from Allied World Assurance Company, Ltd. ("AWAC"), a wholly-owned subsidiary of Fairfax. The Company records this investment in affiliated common stock of Toys R Us using the equity method of accounting, on a one quarter lag. The carrying amount of this investment at December 31, 2018 equaled its cost.

At December 31, 2016, Fairfax and the Company owned common stock and debt issued by Exco Resources, Inc. ("Exco"). In March 2017, Exco completed its debt refinancing transaction. As a result, as of March 31, 2017, Fairfax and the Company owned common stock, two new debt instruments issued by Exco (1.75 and 1.5 Exco Bonds), as well as warrants to purchase Exco common stock ("Exco Warrants"). In the first quarter of 2017, the Company recorded $13.8 million of cumulative unrealized losses on this common stock investment in the Consolidated Statements of Comprehensive Income. In June 2017, Fairfax and the Company received additional shares of Exco common stock as payment in-kind for interest accrued on one of the new Exco bonds. Fairfax concluded that it obtained significant influence as a result of the additional investment; and both Fairfax and the Company commenced equity accounting for Exco common stock as of the day significant influence was obtained. In the second quarter of 2017, upon step up to equity method of accounting, the Company recorded $15.3 million of realized losses on the Exco common stock previously accounted at fair value, with changes in fair value recorded in the Consolidated Statements of Comprehensive Income. In the third quarter of 2017, the Company recorded $0.9 million of realized losses from other-than-temporary impairment for the Company's investment in Exco equity-method common stock. The Company's share of Exco's net losses since equity accounting commenced exceeded the Company's remaining investment in Exco equity-method common stock; and a result, the carrying value of Exco common stock was reduced to zero in 2017. In January 2018, Fairfax and the Company entered into an agreement with Exco to extend a private debtor-in-possession loan ("Exco DIP Loan") to Exco who is in the process of bankruptcy restructuring. The Company's share of this affiliated corporate loan was $2.7 million at December 31, 2018. As a result of the bankruptcy restructuring, the 1.75 Exco Bonds were valued at 60% of par and its related investment income was written down to 60% of coupon rate in the fourth quarter of 2017 and income accrual stopped as of March 20, 2018. Exco Warrants were canceled in 2018. The carrying value of Exco Bonds was $10.5 million at both December 31, 2017 and 2018.

In March 2017, the Company invested $21.0 million in Farmers Edge, Inc. ("Farmers Edge"), a private Canadian company that became an affiliate of Fairfax and the Company simultaneously with the Company's investment at which time the Company commenced equity-method accounting. In December 2017, the Company sold a portion of its investment in Farmers Edge to Allied World Insurance Company, a Fairfax affiliate, for $5.0 million and recognized $0.4 million of realized gain on the sale. In February 2018, Fairfax and the Company entered into a private loan agreement ("Farmers Edge Loan") with Farmers Edge. Fairfax and the Company also received warrants ("Farmers Edge Warrants") to purchase Farmers Edge common stock in connection with this loan. The Company's share of these investments was $4.1 million, allocated between $3.4 million (Canadian $5.0 million par value) in Farmers Edge Loan and $0.7 million in Farmers Edge Warrants, as estimated by HWIC. The Company sold its Farmers Edge Warrants to Wentworth on the same day they were acquired, substantially at cost. The carrying value of Farmers Edge common stock was $9.6 million and $14.7 million at December 31, 2018 and 2017, respectively. The carrying value of Farmers Edge corporate loan was $3.7 million at December 31, 2018.

The Company owned a common stock investment in APR Energy plc that was privatized through a consortium of investors, including Fairfax, during the first quarter of 2016. In connection with the terms of the privatization deal, the Company, along with other Fairfax affiliates, invested $35.0 million in the common stock shares of the newly formed entity. In February 2016, existing shares with a fair value of $7.9 million were converted into shares of the newly formed entity, Apple Bidco. Apple Bidco became an affiliate of Fairfax simultaneously with the privatization transaction. In December 2017, the Company sold a portion of Apple Bidco to AWAC for $10.0 million and recognized a realized gain of $1.0 million. The carrying value of Apple Bidco common stock was $28.4 million and $29.7 million as of December 31, 2018 and 2017, respectively.

In June 2016, the Company invested $15.0 million in Davos Brands LLC ("Davos"), a U.S. limited liability company involved in manufacturing and distributing luxury alcohol brands including sake, vodka and other spirits. Fairfax affiliates and the Company own approximately 35% and 11% of Davos, respectively. The Company's investment in Davos was previously classified as a non-affiliated partnership investment based on the uncertainty of obtaining regulatory approval from liquor licensing boards in Canada and the U.S. During first quarter of 2017, Fairfax received regulatory approval from most jurisdictions. Due to this change in circumstances, Fairfax and the Company began classifying its investment as an affiliated partnership and commenced equity method of accounting as of March 31, 2017. The carrying value of Davos was $13.5 million and $13.7 million at December 31, 2018 and 2017, respectively.

In February 2017, the Company invested $35.0 million in the newly issued common stock of Fairfax Africa Holdings Corp. ("FAH"), as part of the initial public offering ("Offering"). FAH became an affiliate of the Company simultaneously with the Company's investment at which time the Company commenced equity method accounting. Concurrent with the closing of the Offering, the Company's investment in Agrigroupe LP, an affiliate of Fairfax and the Company, with the carrying value of $8.8 million was acquired by FAH at its estimated fair value of $11.2 million. The carrying value of FAH was $47.8 million and $48.4 million at December 31, 2018 and 2017, respectively.

In January 2017, the Company invested $4.8 million in Astarta Holding NV ("Astarta"), a Netherlands company whose common stock is publicly traded on the Polish stock exchange. Astarta became an affiliate of Fairfax and the Company in March 2017 when Fairfax obtained significant influence as a result of additional investment. Fairfax and the Company commenced equity method accounting for Astarta in March

2017 and recorded a realized gain of $0.6 million to step up the Company's cost basis to the fair market value of its investment on the day significant influence was obtained. In May 2017, the Company exercised a call option to acquire additional shares of Astarta for $7.5 million and recorded a realized gain of $1.4 million on the call option exercise. The carrying value of Astarta was $13.6 million and $16.5 million at December 31, 2018 and 2017, respectively.

In January 2017, the Company invested $3.2 million in 2018296 Alberta ULC ("Alberta"), a private Canadian company wholly owned by Fairfax. Alberta was established for the purposes of investing in Mosaic Capital Corporation, a Canadian investment company. Alberta became an affiliate of Fairfax and the Company simultaneously with the Company's investment at which time the Company commenced equity method accounting. The carrying value of Alberta was $3.6 million and $3.3 million at December 31, 2018 and 2017, respectively.

In January 2017, the Company invested an additional $2.5 million in Fairfax India Holdings Corp. ("FIH"), an affiliate of Fairfax, as part of an additional share offering. The carrying value of FIH was $18.8 million and $19.5 million at December 31, 2018 and 2017, respectively.

In December 2016, the Company invested $10.0 million in 99388983 Canada Inc. ("Canada Inc."), a private Canadian company that became an affiliate of Fairfax simultaneous with the Company's investment. Canada Inc. provided a debtor-in-possession ("DIP") loan to Performance Sporting Goods ("PSG"), a Canadian company in the process of bankruptcy restructuring. In February 2017, the bankruptcy restructuring was resolved and the DIP loan was repaid, partially in cash and in assets of PSG, and Canada Inc. purchased the remaining assets and liabilities of PSG. The Company's original investment then converted into Class A common stock of Canada Inc.; and this entity was renamed Peak Achievements Athletics ("PAA"). The carrying value of PAA was $8.6 million and $9.6 million at December 31, 2018 and 2017, respectively.

Other

The Company continues to be a party to various reinsurance treaties with affiliates of Fairfax that were entered into in the ordinary course of business, primarily excess of loss reinsurance agreements with Odyssey Re for 2010 through 2018. In the fourth quarter 2016, the Company commuted a quota-share ceded reinsurance contract with Odyssey Re, received cash of $2.4 million in full and final settlement of the contract, and recorded a loss of $0.6 million. At December 31, 2018 and 2017, the Company recorded net reinsurance recoverables of $1.0 million and $0.7 million, respectively, related to the reinsurance transactions with the affiliates of Fairfax.

Zenith National paid Fairfax $5.4 million, $6.6 million and $4.5 million for the years ended December 31, 2018, 2017 and 2016, respectively, for the cost of the open market purchase made by Fairfax on Zenith National's behalf of Fairfax Subordinate Voting Shares granted to certain officers under the Restricted Stock Plan.

On November 2, 2016, the Company entered into loan agreements with Fairfax and ZNAT, to borrow $55.0 million and $40.0 million, respectively, to facilitate the sales of certain U.S. Government debt securities that were on deposit in accordance with California laws and regulations. The annual interest rate on both loans was 0.24%. The loans were funded primarily by short-term U.S. Government debt securities. On November 9, 2016 and November 29, 2016, the Company repaid in cash principal and interest, respectively, on both loans.

In April 2015, Zenith National entered into an agreement with MFXchange US, Inc., an indirect, wholly-owned subsidiary of Fairfax, to provide information technology services to Zenith National. The Company recorded expenses of $0.1 million, $0.1 million and $0.2 million for the years ended December 31, 2018, 2017 and 2016, respectively.

In November 2014, the Company entered into a Master Administrative Services Agreement with various affiliates of Fairfax. Under the agreement, the affiliated parties provide and receive administration services such as accounting, underwriting, claims, reinsurance, preparation of regulatory reports, and actuarial services. The Company began providing claims processing services for Seneca Insurance Company, Inc. ("Seneca") under this agreement in March 2016 and recorded service fee income of $0.4 million, $0.5 million and $0.4 million for the years ended December 31, 2018, 2017 and 2016, respectively, in the Consolidated Statements of Comprehensive Income (Loss) which was substantially offset by costs of dedicated staff and allocated shared services. Other liabilities at December 31, 2018 and 2017 include a loss fund of $0.6 million maintained by the Company to process future workers' compensation claim payments on behalf of Seneca.

In March 2013, the Company entered into an agreement with TIG Insurance Company ("TIG") to become their primary workers' compensation claims service provider. The Company recorded service fee income of $8.8 million, $9.1 million, and $8.7 million for the years ended December 31, 2018, 2017 and 2016, respectively, in the Consolidated Statements of Comprehensive Income (Loss) which is substantially offset by costs of dedicated staff and allocated shared services. Other liabilities at December 31, 2018 include a net liability of $3.2 million which included a net loss fund liability of $4.0 million reduced by a service fee income receivable of $0.8 million, compared to a net liability of $2.3 million which included a net loss fund liability of $3.3 million reduced by a service fee income receivable of $1.0 million at December 31, 2017.

Note 13. Other Comprehensive Income (Loss)

Other comprehensive income (loss) is comprised of changes in unrealized gains/losses on investments classified as available-for-sale, other investments in cost-method partnerships, other investments in equity-method common stocks and partnerships and foreign currency translation adjustments. The following table summarizes the components of the Company's other comprehensive income (loss):

(In thousands)	Pre-Tax	Income Tax Effect	After-Tax
Year ended December 31, 2018			
Net unrealized gains arising during the year	$ 629	$ 131	$ 498
Less: reclassification adjustment for net realized gains included in net income	(782)	(163)	(619)
Reclassification of certain tax effects to retained earnings at January 1, 2018 (a)		549	(549)
Net changes in unrealized gains/losses on available-for-sale and other investments	(153)	517	(670)
Change in unrealized foreign currency translation adjustment arising during the year	(3,593)	(755)	(2,838)
Less: reclassification adjustment for net realized foreign exchange losses included in net income	1,155	243	912
Reclassification of certain tax effects to retained earnings at January 1, 2018 (a)		280	(280)
Change in unrealized foreign currency translation adjustment	(2,438)	(232)	(2,206)
Total other comprehensive loss	$ (2,591)	$ 285	$ (2,876)
Year ended December 31, 2017			
Net unrealized gains arising during the year	$ 3,620	$ 1,267	$ 2,353
Less: reclassification adjustment for net realized gains included in net income	(2,742)	(960)	(1,782)
Net changes in unrealized gains/losses on available-for sale and other investments	878	307	571
Change in unrealized foreign currency translation adjustment	3,766	1,318	2,448
Total other comprehensive income	$ 4,644	$ 1,625	$ 3,019
Year ended December 31, 2016			
Net unrealized losses arising during the year	$ (4,270)	$ (1,494)	$ (2,776)
Less: reclassification adjustment for net realized gains included in net income	(360)	(126)	(234)
Net changes in unrealized gains/losses on available-for sale and other investments	(4,630)	(1,620)	(3,010)
Change in unrealized foreign currency translation adjustment	(652)	(228)	(424)
Total other comprehensive loss	$ (5,282)	$ (1,848)	$ (3,434)

(a) In February 2018, the FASB issued updated guidance that allows a reclassification from accumulated other comprehensive loss to retained earnings for the stranded tax effects resulting from the enactment of the Act. The Company early adopted this amended guidance on January 1, 2018, and as a result, elected to reclassify a total of $0.8 million in stranded tax effects from accumulated other comprehensive loss to retained earnings as of January 1, 2018.

The following table summarizes the net unrealized gains (losses) on available-for-sale securities, other investments in cost-method partnerships, other investments in equity-method common stocks and partnerships, and foreign currency translation adjustment recognized in accumulated other comprehensive loss:

(In thousands)	December 31, 2018	December 31, 2017
Available-for-sale equity securities	$ (4,249)	$ (4,117)
Other investments in equity-method common stocks	(1,519)	(1,434)
Other investments in cost-method partnerships	293	1,235
Other investments in equity-method partnerships	1,402	396
Net unrealized loss on investments, before tax	(4,073)	(3,920)
Deferred tax benefit	(855)	(1,372)
Net unrealized loss on investments, after tax	(3,218)	(2,548)
Net unrealized loss on foreign currency translation adjustment, before tax	(4,438)	(2,000)
Deferred tax benefit	(932)	(700)
Net unrealized loss on foreign currency translation adjustment, after tax	(3,506)	(1,300)
Total accumulated other comprehensive loss	$ (6,724)	$ (3,848)

Note 14. Employee Benefit and Retirement Plans

The Company offers a tax deferred savings plan created under Section 401(k) of the Internal Revenue Code for all eligible employees. The Company matches 50% of employee contributions that are 6% or less of salary on a current basis (subject to certain limits) and is not liable for any future payments under the plan. The Company contributed $3.4 million, $3.4 million and $3.1 million under the plan for the years ended December 31, 2018, 2017 and 2016, respectively.

In June 2010, an employee stock purchase plan was approved by Zenith National's Board of Directors providing for the purchase of up to 100,000 Fairfax Subordinate Voting Shares. The plan limits employee contributions to 10% of base salary or wages before tax for each payroll period. Under this stock purchase plan, the Company matches 30% of employee contributions and purchases Fairfax Subordinate Voting Shares at market value. If the Company achieves certain annual profitability conditions, it will provide an additional 20% match on the total contributions made during the year to employees who are employed on the date the additional match is made. The Company contributed $2.1 million, $1.8 million and $1.7 million in matching contributions under the plan for years ended December 31, 2018, 2017 and 2016, respectively.

Note 15. Commitments and Contingencies

Leases

The Company has office space and automobile leases expiring through 2028. The minimum lease payments on these non-cancelable operating leases at December 31, 2018 were as follows:

(In thousands)	Offices	Auto Fleet	Total
2019	$ 6,323	$ 772	$ 7,095
2020	6,702	455	7,157
2021	5,492	107	5,599
2022	3,565	4	3,569
2023	2,077		2,077
Thereafter	3,144		3,144
Total	$ 27,303	$ 1,338	$ 28,641

Rent expense for the years ended December 31, 2018, 2017 and 2016 was $8.6 million, $8.2 million, and $8.7 million, respectively.

Litigation

The Company is involved in various litigation proceedings that arise in the ordinary course of business. Disputes adjudicated in the workers' compensation administrative systems may be appealed to review boards or civil courts, depending on the issues and local jurisdictions involved. From time to time, plaintiffs also sue the Company on theories falling outside of the exclusive jurisdiction and remedies of the workers' compensation claims adjudication systems. Certain of these legal proceedings seek injunctive relief or substantial monetary damages, including claims for punitive damages, which may not be covered by reinsurance agreements. Historically, the Company has not experienced any material exposure or damages from any of these legal proceedings. In addition, in the opinion of management, after consultation with legal counsel, currently outstanding litigation is either without merit or the ultimate liability, if any, is not expected to have a material adverse effect on the Company's consolidated financial condition, results of operations or cash flows.

Note 16. Stock-Based Compensation

The following table provides information regarding the Fairfax Subordinate Voting Shares under the Restricted Stock Plan:

	Number of Shares
Authorized for purchases and grants at plan inception in 2010	200,000
Purchased and restricted	(56,243)
Vested	(39,432)
Purchased and available for future grants	(11,150)
Available for future purchases at December 31, 2018	93,175

The following represents open market purchases of Fairfax Subordinate Voting Shares under the Restricted Stock Plan which also resulted in charges to the Company's Stockholders' equity:

(Dollars in thousands, except share data)	Number of Shares	Weighted Average Purchase Price Per Share	Total Purchase Price
Purchased through December 31, 2011	29,970	$ 388.11	$ 11,632
Purchased in 2012	10,554	381.59	4,027
Purchased in 2013	6,145	390.86	2,402
Purchased in 2014	5,898	501.47	2,958
Purchased in 2015	19,844	486.34	9,651
Purchased in 2016	10,191	443.31	4,518
Purchased in 2017	12,908	509.28	6,574
Purchased in 2018	11,315	474.36	5,367
Total purchased since plan inception	106,825	441.17	$ 47,129

Changes in the restricted shares outstanding were as follows:

(Dollars in thousands, except share data)	Number of Shares	Weighted Average Grant Date Fair Value Per Share	Grant Date Fair Value
Restricted Shares at December 31, 2015	35,799	$ 443.01	$ 15,859
Granted during 2016	10,183	449.52	4,577
Forfeited during 2016	(240)	479.30	(115)
Vested during 2016	(4,296)	394.01	(1,692)
Restricted Shares at December 31, 2016	41,446	449.48	18,629
Granted during 2017	14,335	447.71	6,418
Forfeited during 2017	(2,267)	421.59	(956)
Vested during 2017	(3,227)	384.96	(1,242)
Restricted Shares at December 31, 2017	50,287	454.37	22,849
Granted during 2018	11,608	508.90	5,907
Forfeited during 2018	(305)	474.43	(144)
Vested during 2018	(5,347)	384.87	(2,058)
Restricted Shares at December 31, 2018	56,243	472.13	$ 26,554

Stock-based compensation expense before tax was $4.9 million, $4.1 million and $3.2 million for the years ended December 31, 2018, 2017 and 2016, respectively.

Unrecognized compensation expense before tax under the Restricted Stock Plan was $14.4 million and $13.5 million at December 31, 2018 and 2017, respectively.

Supplementary Consolidating Information

Report of Independent Auditors

To the Management of Zenith National Insurance Corp.

We have audited the consolidated financial statements of Zenith National Insurance Corp. and its subsidiaries (collectively, the "Company") as of December 31, 2018 and for the year then ended and our report thereon appears on pages 2 and 3 of this document. That audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The consolidating information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated, in all material respects, in relation to the consolidated financial statements taken as a whole. The consolidating information is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position, results of operations and cash flows of the individual companies and is not a required part of the consolidated financial statements. Accordingly, we do not express an opinion on the financial position, results of operations and cash flows of the individual companies.

PricewaterhouseCoopers LLP

February 22, 2019

ZENITH NATIONAL INSURANCE CORP. AND SUBSIDIARIES
SUPPLEMENTARY CONSOLIDATING BALANCE SHEET
DECEMBER 31, 2018

(In thousands)	Zenith Insurance Company	ZNAT Insurance Company	1390 Main Street LLC	Zenith of Nevada, Inc.	Zenith Insurance Company Eliminations	Note	**Zenith Insurance Company & Subsidiaries**	Zenith National Insurance Corp.	Zenith National Insurance Corp. Eliminations	Note	**Zenith National Insurance Corp. & Subsidiaries**
Assets:											
Investments	$ 1,618,651	$ 62,520					$ 1,681,171	$ 7,761			$ 1,688,932
Cash	23,478	2,554		$ 1,591			27,623	2,044			29,667
Accrued investment income	3,685	160					3,845	7			3,852
Premiums receivable	39,262	1,191					40,453				40,453
Reinsurance recoverables	70,642	166,196			$ (188,953)	(2a)	47,885				47,885
Deferred policy acquisition costs	10,140	2,007					12,147				12,147
Deferred tax asset	45,988	1,013	$ (25)				46,976	417			47,393
Investment in subsidiaries	34,533				(34,533)	(2b)		565,568	$ (565,568)	(2c)	
Goodwill	18,976						18,976	2,009			20,985
Other assets	48,740	480	8,569				57,789	86			57,875
Intercompany	14,416	(15,280)					(864)	864			
Total assets	$ 1,928,511	$ 220,841	$ 8,544	$ 1,591	$ (223,486)		$ 1,936,001	$ 578,756	$ (565,568)		$ 1,949,189
Liabilities:											
Unpaid losses and loss adjustment expenses	$ 1,146,806	$ 173,246			$ (172,186)	(2a)	$ 1,147,866				$ 1,147,866
Unearned premiums	86,710	16,767			(16,767)	(2a)	86,710				86,710
Policyholders' dividends accrued	38,408	4,829					43,237				43,237
Long-term debt								$ 38,225			38,225
Income tax payable	3,283	43					3,326	(26)			3,300
Derivative liabilities	16,504						16,504				16,504
Other liabilities	71,232	1,558					72,790	3,387			76,177
Total liabilities	1,362,943	196,443			(188,953)		1,370,433	41,586			1,412,019
Total stockholders' equity	565,568	24,398	$ 8,544	$ 1,591	(34,533)	(2b)	565,568	537,170	$ (565,568)	(2c)	537,170
Total liabilities and stockholders' equity	$ 1,928,511	$ 220,841	$ 8,544	$ 1,591	$ (223,486)		$ 1,936,001	$ 578,756	$ (565,568)		$ 1,949,189

This supplementary consolidating balance sheet should be read in connection with the accompanying notes to supplementary consolidating balance sheet, the consolidated financial statements and notes to the consolidated financial statements.

ZENITH NATIONAL INSURANCE CORP. AND SUBSIDIARIES
NOTES TO SUPPLEMENTARY CONSOLIDATING BALANCE SHEET

1. Basis of Presentation

The accompanying supplementary consolidating Balance Sheet has been prepared in accordance with GAAP and includes the accounts of Zenith Insurance, ZNAT, 1390 Main Street LLC, Zenith of Nevada, Inc. and Zenith National.

2. Consolidating Eliminations

The following eliminations are reflected in the accompanying supplementary consolidating Balance Sheet as of December 31, 2018:

(a) To eliminate intercompany reinsurance balances;

(b) To eliminate Zenith Insurance's investment in ZNAT, 1390 Main Street LLC and Zenith of Nevada, Inc.; and

(c) To eliminate Zenith National's investment in Zenith Insurance.