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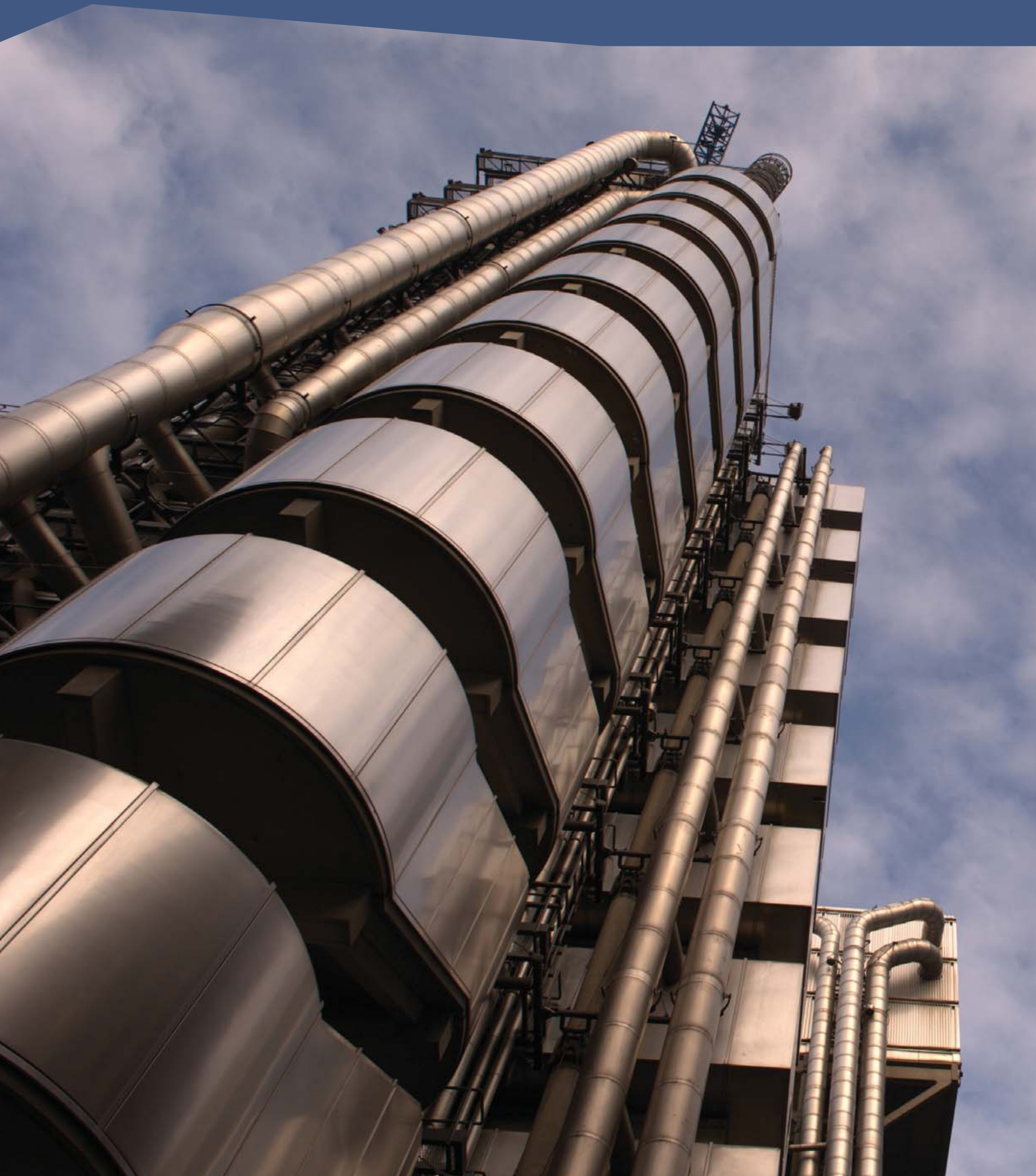
Argenta Syndicate Management Limited
Syndicate 2121

# Report, Annual Accounts and Underwriting Year Accounts

as at 31 December 2016



# Argenta Syndicate Management Limited
# Company Information

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## Managing Agent's Report

The directors of Argenta Syndicate Management Limited (ASML), a company registered in England and Wales, present their report for the year ended 31 December 2016.

The annual accounts are prepared using the annual basis of accounting as required by Statutory Instrument No. 1950 of 2008, the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 ("the 2008 Regulations").

A separate set of underwriting year accounts has been prepared on the traditional three year accounting basis in accordance with the Lloyd's Syndicate Accounting Byelaw (No. 8 of 2005). These relate to the 2014 year of account which has been reinsured to close with effect from 31 December 2016.

The financial reporting framework that has been applied is United Kingdom Generally Accepted Accounting Practice (UK GAAP) including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' (FRS 102) and Financial Reporting Standard 103 'Insurance Contracts' (FRS 103).

**Principal activity**

There has been no change during the year to the syndicate's principal activity which continues to be the transaction of general insurance and reinsurance business.

**Overview of business**

Syndicate 2121 continues to underwrite a predominantly direct and short tail account across a broad range of marine and non-marine classes of business with a worldwide geographical spread, although some long tail casualty business is also written. It operates within the Lloyd's of London (Lloyd's) insurance market in London and through a service company on the Lloyd's platform in Singapore, Argenta Underwriting Asia Pte Ltd (AUA). This service company has recently opened a branch office in the Central Business District of Sydney, Australia. In addition, at the beginning of 2016 the syndicate established a dedicated underwriting division of Lloyd's Insurance Company (China) Limited (LICCL) based in Shanghai, accessing Chinese domiciled reinsurance business. Finally, and in line with the stated aim for controlled growth, in 2016 AUA purchased the business of an established managing general agent in Australia writing a niche property account. This business had been written by the syndicate on a subscription basis since 2005 and in a lead capacity since 2011 with consistent results that have beaten the business plan average. For 2016 the syndicate assumed 100% of this account which is now fully integrated with the remainder of the book of business written.

The largest line of business continues to be the direct and facultative property book, built around a number of long standing relationships with managing general agents and supplemented with an open market book of predominantly small commercial and homeowners' business. The syndicate also writes onshore power and utility business and terrorism in the property sector. The marine book consists of the traditional classes including hull, cargo, specie, war and fine art. Energy, including exploration, production and distribution is underwritten, although refining risks are not. Marine and energy liabilities, both in conjunction with the physical damage lines and on a standalone basis, are also written. The syndicate has a small international (i.e. non-USA) treaty account split across catastrophe excess of loss and risk excess business. An international casualty book written via a Lloyd's approved consortium is written which also includes a small product recall account and is in its fourth year of development. An accident and health book was added to the syndicate's portfolio in 2014, and in 2015 the syndicate started to develop a UK commercial combined book for small to medium enterprises which packages property with both employers' and public liability risks. Finally, for 2016 the syndicate expanded its cyber book predominantly through participation on another Lloyd's approved consortium and quota share reinsurance of another larger Lloyd's syndicate, and introduced, during the latter part of the year, a new political risks account.

## Managing Agent's Report
*continued*

**Overview of business** *continued*

For the 2016 year the stamp capacity was increased to £270 million in line with the ASML strategic objective to grow Syndicate 2121 and to add new lines of business or aligned distribution sources that are able to deliver profit in a competitive market. This is expected to continue but will always be subject to market conditions and either the recruitment of high quality underwriters with a proven track record, or through the support of market consortia which have lead expertise.

**Review of underwriting activities for 2016**

On an annual accounting basis, the result of the syndicate for calendar year 2016 is a profit of £15.0 million (combined ratio 94%) with the 2014 and 2015 underwriting years producing profits of £15.4 million and £7.2 million respectively, and 2016 producing a first year loss of £7.6 million. On the traditional Lloyd's basis of reporting, the 2014 year of account has closed with a profit of £34.6 million or 14.4% of capacity, with a pure year profit of 9.4% and a release from the 2013 and prior years of 5.0%. The profit includes a foreign exchange gain of £14.7 million.

The table below summarises the capacity, premium volumes and performance of Syndicate 2121 for 2016 alongside comparative numbers for 2015. Other than in respect of capacity, the numbers shown are on an annually accounted basis. The table is followed by further detailed comments in relation to each of the years on an annually accounted basis and also on an underwriting year of account basis.

| *Key performance indicators* | *2016* | *2015* |
|---|---|---|
| Capacity (underwriting year) | £270 million | £240 million |
| Premiums written gross of commission | £281 million | £227 million |
| Net premiums earned | £217 million | £178 million |
| Profit for the year | £15 million | £14 million |
| Claims ratio (net) | 50% | 48% |
| Combined ratio | 94% | 93% |
| Cash and investments at 31 December | £262 million | £231 million |

The combined ratio is the ratio of net incurred claims plus net operating expenses, together with non-technical foreign exchange differences, to net earned premiums.

Terms and conditions during 2016 remained very challenging with continued overcapacity across most lines of business. This resulted in a distinct lack of new business opportunities, declining renewals due to rate reductions and the expansion of the number and size of broker-led whole account placements. Despite the loss of income, the syndicate maintained its stance of not supporting such broker facilities.

Activity in the energy market continued to decline with less exploration, drilling and construction taking place as a result of the sharp downturn in the price of oil. Whilst there is evidence of some recovery in this sector, energy companies are taking much longer to adjust their operating costs such that a profit can be made even with the currently depressed price of oil.

Premium rates in many areas of the portfolio continued to fall during the year, albeit very much in line with business plan expectations at a whole account level. The overall rate reduction on business that was not renewed in 2016 was 3.8% compared to an expected reduction of 3.7% for the syndicate as a whole. This reduction in rates was slightly below the 5.4% witnessed in 2015 and, importantly, was at a level that had been anticipated during the 2016 business planning process.

**Review of underwriting activities for 2016** *continued*

The 2016 calendar year saw an increase in natural catastrophes when compared to recent years, with earthquakes in Japan, wildfires in Canada and Hurricane Matthew threatening, but ultimately skimming, the US coast in October 2016. Man-made losses during the period included the bearing failure on the Jubilee oilfield in Ghana and a large warehouse fire in New York State. According to Swiss Re's insurance research arm Sigma, natural catastrophe and man-made losses in 2016 totalled US$49 billion. This is up from US$37 billion in 2015 and US$36 billion in 2014.

The syndicate's largest natural catastrophe losses were in respect of flood damage to an energy plant in the utility class, Hurricane Matthew and floods in Louisiana. On the man-made side the largest losses were a cable fire on a Colombian power account and the bearing failure on the Jubilee oilfield in Ghana mentioned above.

*2014 year of account*

As previously reported, from a catastrophe perspective 2014 was a benign year; it also continued to experience a very low level of attritional losses across all classes and developed ahead of expectation. The largest losses to impact this year remain the Guam Power loss, the Australian hailstorms, and a fire loss to Quilliq Energy in Canada.

Reserves in respect of the 2013 and prior years of account continue to improve and develop satisfactorily, generating a surplus of £12 million as at 31 December 2016.

As a result of all of the above, the 2014 and prior years of account have produced a profit of 14.4% of stamp capacity.

*2015 year of account*

From a catastrophe perspective 2015 was also a benign year, although there was some increase in the level of attritional and large loss experience. The largest losses on the 2015 year of account are those that occurred in 2016 and discussed above, namely the cable fire on a Colombian power account, bearing failure on the Jubilee oilfield in Ghana and flood damage to an energy plant in the utility class. These are in addition to those large losses previously reported, being the over-voltage loss on Dynergy, the Californian wildfires and the explosion at Tianjin Port.

Overall the 2015 forecast result is currently developing behind the business plan target. Taking these factors into consideration and in the absence of any further adverse developments, the current forecast is a profit on the 2015 account of up to 5% of capacity.

*2016 year of account*

The 2016 year witnessed an increase in losses from a catastrophe perspective, although reduced attritional and large loss experience on the year to date compared with 2015 at the same stage. The largest loss to impact this year so far is Hurricane Matthew, with two pipeline losses emanating from the casualty account coming in distant second and third places.

Overall premium income was lower than planned with pure rate reductions continuing to impact all classes, particularly the treaty, marine cargo and specie, marine liability, energy and terrorism accounts. The loss of business to broker facilities slowed during the year as the risks that were going to be subsumed into these placements had significantly done so in 2015.

**Review of underwriting activities for 2016** *continued*

The new UK commercial combined account continued to develop more slowly than planned as coverholders are requiring proven service levels before they commit to updating their in-house systems to accommodate the syndicate’s underwriting guidelines.

The cyber, casualty, accident and health and the new political risks accounts showed growth in 2016, with the property, utility and marine hull and war classes, maintaining income levels year on year.

During the year the syndicate took advantage of market conditions to purchase additional facultative reinsurance cover, particularly in relation to the utility book of business. Such further cover was purchased on an opportunistic basis to enhance the performance of this class.

Overall the 2016 forecast result is currently developing slightly behind the business plan target. There is, however, a significant element of the business attaching to this year of account still on risk and the final result will depend on how this develops.

*Trading conditions for 2017*

When developing the 2017 business plan a further weakening in rates across all classes of business was factored in to the projections, however the rate reductions anticipated were at lower levels than those seen in 2015 and 2016. The January 2017 renewal season has supported this view with rates on average down by 2.7% across all classes, which is very much in line with the business plan assumptions.

Development of the UK commercial combined account is expected to continue to be measured, largely as a result of the underwriting discipline the syndicate applies. The syndicate’s involvement in Singapore and China for 2017 is expected to reduce as some large January renewals have been declined due to adverse renewal terms. The Australian platform, however, is expected to show strong signs of growth as domestic companies apply small rate increases on renewals along with some second year momentum for this operation.

The property and casualty accounts have suffered from lower renewal retentions and a general lack of new business when compared to the levels in the business plan.

The new political risks account is developing satisfactorily with its first full year being 2017. Some new auto physical damage business has been written through a London based managing general agent with exposures predominantly in the USA. Rates for this class sit at levels above the medium term average as liability losses in domestic package policies are beginning to bite causing the packages to break up which allows a true rate to be charged for the exposures.

Notwithstanding the above, new classes of business will be considered but only where they complement the syndicate’s existing portfolio and provide for either the recruitment of individuals or teams who offer experience, expertise and a proven track record, or through the further support of leading market practitioners on consortia.

Finally, the advantage of a softening reinsurance market is that a more effective programme can be purchased for all classes at a whole account level with further savings being achieved without a reduction in the protection afforded.

**ASML business structure**

ASML is the Lloyd's managing agency subsidiary of Argenta Holdings plc (AHP), an unquoted holding company with diversified interests in the Lloyd's insurance market.

ASML has been the managing agent of Syndicate 2121 since its inception in 2000. Since then the syndicate's capacity has steadily been increased to its current level, for the 2017 year of account, of £300 million. The company's strategy is to continue growing the syndicate, subject to market conditions, by selectively adding new business to current classes and diversifying into new classes when appropriate.

The syndicate underwrites a broad cross-section of mainly short tail classes encompassing marine, property, energy and utilities as well as small terrorism, accident and health and treaty books of business. The syndicate also commenced writing a small political risks account towards the end of 2016. Syndicate 2121 operates in Singapore via a service company, AUA, which is authorised by the Monetary Authority of Singapore (MAS) and Lloyd's Asia. AUA has a branch office in Sydney, and Syndicate 2121 also participates on the Lloyd's China Platform in Shanghai through a division of LICCL.

**Directors**

John LP Whiter – *Non-executive Chairman*
Andrew J Annandale – *Managing Director*
Graham K Allen – *Finance Director*
Peter J Bruin – *Operations Director and Company Secretary (resigned 31 October 2016)*
Paul Hunt – *Non-executive Director*
Ian M Maguire – *Active Underwriter Syndicate 2121*
Nicholas J Moore – *Chief Actuary*
John E Mumford – *Non-executive Director*
Trevor P Newbery – *Non-executive Director (resigned 25 June 2016)*
Gary A Powell – *Non-executive Director*
Matthew P Rowan – *Risk Management and Compliance Director*
– *Company Secretary (appointed 1 November 2016)*
David J Thompson – *Claims and Operations Director*

**Risk management**

As an underwriting business Syndicate 2121 is exposed to a variety of financial and non-financial risks. These risks, which shape the risk management strategy adopted by ASML, are integral to the capital setting process that is undertaken to ensure that there is an appropriate level of capital held in respect of the insurance liabilities to which Syndicate 2121 is exposed. The Own Risk and Solvency Assessment (ORSA) undertaken in respect of Syndicate 2121 reflects the risk profile of the business as well as the business strategy. Risks are managed through the risk management framework in order to ensure that the risk profile of the business is fully understood and can be monitored against the agreed risk appetite.

ASML is committed to risk management as an integral part of management and governance best practice, and has developed a risk management strategy to protect the material assets of Syndicate 2121 and to minimise its losses and liabilities.

**Risk management** *continued*

The risks to the business are grouped under various categories, each of which is the subject of a risk policy which sets out ASML's approach to the management of the risk in conjunction with the overarching risk management framework and risk strategy. ASML groups risks into the following key categories:

*Insurance risk*

Insurance risk is the risk that arises from the inherent uncertainties in the occurrence, amount and timing of insurance liabilities. The underwriting profile of Syndicate 2121 is such that it is likely that claims will arise on the business underwritten. An expected level of claims in relation to attritional, large and catastrophe type losses has, therefore, been included in the business planning process. Other precautionary measures, in the form of internal controls, are used to preserve the syndicate's performance by limiting the exposure to wider underwriting, claims and reserving risks, such as:

- Adverse catastrophe loss experience;
- Adverse large and attritional loss experience;
- Poor or inappropriate risk selection;
- Inadequate reinsurance placement; and
- Final claims costs deviating materially from estimated earned reserves due to the inherent variability of the business.

ASML manages these risks against an agreed risk appetite. The framework of systems and controls is designed to reduce the likelihood of such risks occurring and to mitigate their impact on the overall business of the syndicate.

*Operational risk*

Operational risk spans all risk categories. Control procedures are used to proactively address the risks associated with ASML's business processes, systems and other resources which might otherwise be detrimental to overall performance. Business continuity is considered key and ASML has developed a plan that provides for the syndicate to be operational within a 48 hour period in the event that its current offices are no longer available.

The retention of key staff is also fundamental to the success of the business and the strategy adopted by ASML is designed to ensure that the terms and conditions offered to employees, as part of their overall remuneration package, remain competitive with the rest of the London market insurance industry.

As a regulated business, ASML is fully aware of its regulatory obligations to the UK Financial Conduct Authority (FCA), the Prudential Regulation Authority (PRA), Lloyd's, the MAS and other overseas regulators. The procedures adopted by ASML in this regard rigorously monitor compliance with the regulatory standards and, through continuous assessment, highlight any developments that might impact the business.

*Capital risk*

Capital risk is defined as the risk to the syndicate of losses arising from inappropriate levels or sources of capital. Syndicate 2121 is supported by third party capital providers whose ongoing support is crucial to the syndicate continuing to trade forward. ASML is committed to the controlled growth of the syndicate and discussions with current and prospective capital providers are an ongoing process.

**Risk management** *continued*

*Liquidity risk*

This is the risk that the syndicate will not have sufficient available cash resources to be able to meet its liabilities as they fall due. The liquidity of the syndicate is influenced by a number of factors that have the potential to arise from across the business. Management information is used to enable the effective monitoring of the liquidity risk framework in line with the agreed procedures and governance arrangements. Robust procedures are in place for the monitoring of cash flow and effective credit control. Claims activity is closely scrutinised and the movement of existing claims is reported at regular intervals.

*Credit risk*

Credit risk is inherent to the business conducted with brokers, reinsurers and other counterparties. The potential for losses arising from a counterparty failing to fulfil its contracted payment obligations is managed by strict control procedures. Aged debt in respect of the payment of premiums and reinsurance recoveries is closely monitored and actively managed. The ASML finance and investment committee approves the brokers, coverholders and reinsurers with which the syndicate may conduct its business. There is no appetite to deal with counterparties who have not been approved.

*Financial market risk*

Financial market risk is partly mitigated by following a predominantly fixed income investment strategy designed to mitigate exposure to potential losses from movement in exchange rates, interest rates or inflation. The business has a low appetite for market risk and as such there is a requirement to hold only high grade fixed income investments with a minimum average portfolio credit quality of 'AA-', cash and high quality short term instruments. ASML may also invest in listed, highly diversified collective investment schemes, absolute return funds and funds of hedge funds, which serve to mitigate the impact of movements in the wider investment market. Allocations to the absolute returns funds are currently restricted to a maximum of 20% of the syndicate's assets under management and are reviewed regularly to ensure the syndicate's risk appetite budget is not exceeded. ASML also periodically seeks to match assets with liabilities in the syndicate's principal reporting currencies to the extent that funds permit.

*Emerging risk*

In addition to monitoring the individual risk categories outlined above, ASML has in place an emerging risks process to review risks that may impact on the business in the future, and to ensure that any such risks are understood and mitigated where possible.

*Conduct risk*

ASML defines conduct risk as being the risk that its customers are not treated fairly at all times and has in place a mechanism for identifying, monitoring, reporting and mitigating any conduct issues. This includes monitoring and reporting on a wide range of conduct management information and risk appetite metrics to the ASML board, risk framework and compliance committee and product oversight group.

**Investment managers and policy**

During 2016 Insight Investment Management (Global) Limited ('Insight') have been responsible for investing the majority of the syndicate's US dollar, euro and sterling assets within a fixed income portfolio. Lloyd's treasury manages the syndicate's Canadian dollar assets in the regulated trust funds within a fixed income portfolio. The performances of these assets are measured with reference to an appropriate benchmark.

In addition to the fixed income portfolios, Insight managed approximately 18% of the syndicate's assets in a selection of multi asset absolute return funds within a UCITS structure. The objectives of these funds are to optimise investment returns consistent with capital preservation and liquidity, within regulatory constraints, whilst using assets that would give diversification from the fixed income portfolio.

The assets under management within the Insight absolute return mandate consisted primarily of allocations to the euro BNY Mellon absolute return bond fund, from October 2016, and both the euro and US dollar denominated Emerging Market Debt, Currency, Credit and Equity Market Neutral funds. Performance targets of achieving 300 to 325 basis points in excess of three month LIBID were set with a related value at risk budget over a one month period under normal market conditions. The target and risk budgets were set with reference to the level of funds invested with Insight and the other assets within the overall portfolio for the syndicate.

Surplus funds that are held in addition to these portfolios are invested in a combination of unitised liquidity funds and bank deposits.

*Insight*

The fixed income portfolios returned 1.2%, 1.4% and 0.7% on the combined US, sterling and euro portfolios respectively. The fixed income portfolios outperformed their relative benchmarks by 0.02% in US dollars and by 0.5% in both sterling and euros.

Due to the constraints of managing a relatively small euro fixed income portfolio (€5m), this was liquidated with the majority of the funds being invested in the BNY Mellon absolute return bond fund in early October 2016. The fund returned 0.9% and outperformed the benchmark return of 0.7% during the short period to the end of the year.

The US dollar and the balance of the euro absolute return funds made losses of 0.9% and 2.1% respectively during the year versus a targeted return of 3.9% and 2.9% respectively. The overall performance of the absolute return funds was disappointing as the losses in the Credit and Currency funds outweighed the overall positive returns from the Emerging Market Debt and Equity Market Neutral funds. Insight report on 2016 as follows:

> "US Dollar Portfolio
> The USD portfolio outperformed the benchmark target in 2016.
>
> Interest rate strategy was positive during the year. The portfolio has been managed with a relatively low US Treasury duration exposure; the portfolio had 0.87 years interest rate duration at the start of the period and was modestly increased to 1.04 by the end of the period. Inflation market positioning was also positive, with allocations to short-dated Treasury Inflation Protected Securities during a period when realised inflation printed higher than what had been implied in the inflation breakeven at purchase.

**Investment managers and policy** *continued*

Global growth fears early in the period led to credit markets underperforming. However, an accommodative central bank response resulted in credit spreads narrowing for the rest of the period. This also benefitted government bonds, although yields increased towards the end of the period as reflation themes emerged, particularly in the US.

The portfolio kept its corporate bond exposure near its maximum permitted level with a preference towards the banking sector, major oil companies and asset-backed securities. The credit strategy added value during the year as credit markets performed well in 2016 as a whole.

Euro portfolio

The euro portfolio outperformed the benchmark target up until the portfolio was liquidated in August 2016.

The portfolio began the period with an interest rate duration of 1.59 years, focusing on 0-3 year maturities, and duration exposure was maintained at around this level. The interest rate strategy contributed positively over the period as European government bonds performed strongly during the first half of the year in particular on increased monetary central bank accommodation by the European Central Bank. Favoured sectors in credit were senior banks, supranationals and energy with the portfolio allocation close to its maximum permitted percentage exposure to credit markets. The credit strategy contributed positively over the period, and volatility was relatively low in the euro credit market, due to direct support from the European Central Bank's corporate purchase programme.

Sterling portfolio

The GBP portfolio outperformed the benchmark target in 2016.

For much of the year the portfolio had a duration of 0.91 years and this was increased towards the end of the year to 1.34 years and focused on 0-3 year maturities. Interest rate strategy was positive overall. UK gilt markets outperformed German bunds and US treasuries, partly on concerns surrounding 'Brexit' and the aggressive monetary policy response from the Bank of England during the summer. Credit strategy was also positive with a preference towards corporate sectors including senior banks, supranationals and autos.

Insight BNY Mellon Absolute Return Bond Fund

The euro portfolio outperformed the benchmark target from the initial investment in October 2016 to the end of December 2016.

In the fund, market allocation was positive, having detracted from performance towards the start of the year. The two other main contributors to performance were duration, which was managed actively throughout the year ending in a marginally short position, and asset-backed securities (ABS) which were fuelled primarily by increasing demand for income in a low interest rate environment. Negative contributions came from currency exposure management, and the high yield bonds and loans segment. The main events during the year were the UK vote on EU membership and the US presidential election. The fund navigated both with a small gain.

Absolute Insight Emerging Market Debt

Portfolio performance was positive over the period under review. The greatest contributors to returns were external government debt, local government debt and external corporate debt positions while currency exposures proved to be a drag on performance. Emerging market assets were negatively impacted by expectations of increased

**Investment managers and policy** *continued*

protectionism under a Trump presidency which would likely weigh on the long-term economic prospects of and sentiment towards emerging markets, following his surprise victory in the US November elections. In this environment, portfolio returns were negatively affected over the final four months of the year, led by losses in local quasi-government bonds, currency positions, external government debt and external corporate bonds.

Absolute Insight Credit

The fund recorded a negative return over 2016. The primary detractors from performance were high yield asset-backed securities (ABS) and credit default swap (CDS) index positions. On the positive side, investment grade bonds offset some of the losses elsewhere in the portfolio. The negative return over the year was largely a result of negative returns in the first quarter, when a weak period for risk assets had an impact on the portfolio through the ABS allocation, and the timing of short exposure to European high yield via a CDS index which detracted from returns when the index rallied strongly. The fund also recorded a negative return in the wake of the surprise UK referendum result as ABS holdings detracted from performance, in part due to UK assets comprising a significant proportion of the European ABS market. However, later gains elsewhere in the portfolio more than offset this loss as credit markets went through a positive, though volatile, period.

Absolute Insight Equity Market Neutral

Performance was positive over the year as gains across a range of stock-specific positions drove returns. It was a year of two extremes in 2016. In the first half, growth scares, deflationary fears, and central bank policy dominated market mind-sets, whilst from the summer a politically driven sense of hope and expectation emerged – centring on the emergence of a new, more pro-growth, pro-inflation economic policy regime in the US. While bond yields took a further leg down in the immediate aftermath of the Brexit vote, the investment environment started to change from early July as US treasury yields moved higher, with Donald Trump's election win confirming the emerging shift. The environment moved from one dominated by unconventional monetary policy, austerity and financial repression, towards one more focused on stimulatory fiscal rhetoric, combined with nationalist and protectionist policy agendas in mainstream politics.

Absolute Insight Currency

The fund generated a negative return over the year. The largest detractors over this period were short positions in commodity-related and emerging market currencies, and the euro held against the US dollar, while short Japanese yen and sterling positions were the strongest positive contributors."

*Lloyd's treasury*

The Canadian dollar portfolio returned 0.9% over the year which was in line with the benchmark for the calendar year. Canadian front-end yield levels increased along with US Treasuries post-US elections ending the quarter plus 20 to 40bps and pushing the 3-year yield to 0.8% at the year-end. The Bank of Canada left rates unchanged at 0.5% with Governor Poloz commenting that they expect inflation back to 2% by mid-2018 and would have to see something significantly different to change policy.

**Investment managers and policy** *continued*

*Custodians*

Citibank and RBC Investor & Treasury Services have acted as the syndicate's custodians in relation to the fixed income portfolios held with Insight and Lloyd's treasury. State Street and BNY Mellon are the administrators for the syndicate's investments in the absolute return funds.

*Investment objectives*

The overall objective is to target a return, over the long term, of 3 months LIBOR plus 1% and remain 99.5% confident of not underperforming LIBOR by more than 5%. The return for 2016 is consistent with ASML's risk appetite but below the overall long term target return of 1.8% primarily due to the desire not to take more investment risk at the present time coupled with continuing volatility in investment markets and the global low interest rate environment.

*Investment performance*

Funds for investment were primarily held in US dollars. The investment return for the year and the average funds available for investment were as follows:

*Average amount of syndicate funds available for investment during the year:*

| | *2016* | *2015* |
|---|---|---|
| | *'000* | *'000* |
| United States dollars | 245,031 | 225,636 |
| Sterling | 34,702 | 39,666 |
| Canadian dollars | 22,684 | 17,480 |
| Euro | 13,473 | 13,846 |
| Combined in sterling | 239,923 | 206,145 |
| Net aggregate investment return for the calendar year in sterling | 1,770 | 1,081 |

| *Net calendar year investment yield:* | *2016* | *2015* |
|---|---|---|
| United States dollars | 0.7% | 0.4% |
| Sterling | 1.6% | 1.0% |
| Canadian dollars | 0.7% | 1.1% |
| Euro | (0.4%) | 0.2% |
| Combined in sterling | 0.7% | 0.5% |

**Research and development**

The syndicate has not participated in any research and development activity during the year.

### Important events since the end of the financial year

We have reviewed the impact of the revision to the Ogden rate governing the discount rates applicable to lump sum bodily injury compensation awards announced on 27 February 2017, and have concluded that the impact on the business of the syndicate will be immaterial. Accordingly, there has been no adjustment to the claims reserves figures as at 31 December 2016 as a result of the revision of the Ogden rate.

On 18 March 2017 a transaction was entered into for AHP, the parent company of the managing agent for Syndicate 2121, to be acquired by Hannover Rück SE. The transaction is expected to close in the third quarter of 2017 subject to all necessary approvals.

### Disclosure of information to the auditor

In the case of each of the persons who are directors of the managing agent at the time the report is approved:

- So far as the director is aware, there is no relevant audit information, being information needed by the syndicate auditor in connection with the auditor's report, of which the auditor is unaware; and
- Having made enquiries of fellow directors of the agency and the syndicate's auditor, each director has taken all the steps that he or she ought to have taken as a director to become aware of any relevant audit information and to establish that the syndicate's auditor is aware of that information.

### Auditor

Ernst & Young LLP continues to act as the auditor of the syndicate annual accounts and underwriting year accounts, and also as the auditor of ASML. Lloyd's approval for this arrangement under the relevant provisions of the Audit Arrangements Byelaw (No. 7 of 1988) was granted following notification to syndicate members and their non-objection to the arrangement. Notice is hereby given that it is intended to continue with this arrangement unless objections to this proposal are received from syndicate members. Any such objection should be made in writing to the registered office of ASML, within 21 days of receipt of this statement.

Under the 2008 Regulations, the auditor is deemed reappointed in subsequent years if there is no objection. Ernst & Young LLP has signified its willingness to continue in office as the independent auditor to the syndicate and it is proposed that the appointment remains in force.

### Annual general meeting of syndicate members

In accordance with the provisions of the 2008 Regulations, it is not intended to hold an annual general meeting of the members of Syndicate 2121, unless objections to this proposal or to the deemed reappointment of the auditor are received from syndicate members. Any such objection should be made in writing to the registered office of ASML, within 21 days of receipt of this statement.

**Andrew J Annandale**
*Managing Director*

*Approved by the board of Argenta Syndicate Management Limited on 20 March 2017.*

SYNDICATE

# 2121

ANNUAL ACCOUNTS 2016

## Statement of Managing Agent's Responsibilities

The managing agent is responsible for preparing the syndicate annual accounts in accordance with applicable law and regulations.

The 2008 Regulations require the managing agent to prepare syndicate annual accounts at 31 December each year in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The syndicate annual accounts are required by law to give a true and fair view of the state of affairs of the syndicate as at that date and of its profit or loss for that year.

In preparing the syndicate annual accounts, the managing agent is required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the notes to the syndicate annual accounts; and
- prepare the syndicate annual accounts on the basis that the syndicate will continue to write future business unless it is inappropriate to presume that the syndicate will do so.

The managing agent is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the syndicate and enable it to ensure that the syndicate annual accounts comply with the 2008 Regulations. It is also responsible for safeguarding the assets of the syndicate and hence for taking reasonable steps for prevention and detection of fraud and other irregularities.

The managing agent is responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of annual accounts may differ from legislation in other jurisdictions.

## Independent Auditor's Report to the Members of Syndicate 2121

We have audited the syndicate annual accounts of Syndicate 2121 ('the syndicate') for the year ended 31 December 2016 which comprise the Income Statement, the Statement of Changes in Members' Balances, the Statement of Financial Position, the Statement of Cash Flows and the related notes 1 to 21. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' and Financial Reporting Standard 103 'Insurance Contracts'.

This report is made solely to the syndicate's members, as a body, in accordance with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008. Our audit work has been undertaken so that we might state to the syndicate's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the syndicate's members as a body, for our audit work, for this report, or for the opinions we have formed.

**Respective responsibilities of the managing agent and the auditor**

As explained more fully in the Statement of Managing Agent's Responsibilities set out on page 16, the managing agent is responsible for the preparation of syndicate annual accounts which give a true and fair view. Our responsibility is to audit and express an opinion on the syndicate annual accounts in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

**Scope of the audit of the syndicate annual accounts**

An audit involves obtaining evidence about the amounts and disclosures in the syndicate annual accounts sufficient to give reasonable assurance that the syndicate annual accounts are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the syndicate's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the managing agent; and the overall presentation of the syndicate annual accounts. In addition, we read all the financial and non-financial information in the Report and Annual Accounts to identify material inconsistencies with the audited syndicate annual accounts and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

**Opinion on syndicate annual accounts**

In our opinion the syndicate annual accounts:

- give a true and fair view of the syndicate's affairs as at 31 December 2016 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' and Financial Reporting Standard 103 'Insurance Contracts'; and
- have been prepared in accordance with the requirements of the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008.

# Independent Auditor's Report to the Members of Syndicate 2121

*continued*

**Opinion on other matter prescribed by the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008**

In our opinion the information given in the Managing Agent's Report for the financial year in which the syndicate annual accounts are prepared is consistent with the syndicate annual accounts.

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 requires us to report to you, if in our opinion:

- the managing agent in respect of the syndicate has not kept adequate accounting records; or
- the syndicate annual accounts are not in agreement with the accounting records; or
- we have not received all the information and explanations we require for our audit.

Michael Purrington (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London

20 March 2017

## Income Statement

*for the year ended 31 December 2016*

**Technical account – general business**

| | Notes | 2016 £'000 | 2016 £'000 | 2015 £'000 | 2015 £'000 |
|---|---|---|---|---|---|
| **Earned premiums, net of reinsurance** | | | | | |
| Gross premiums written | 2 | 280,715 | | 226,542 | |
| Outward reinsurance premiums | | (52,580) | | (47,621) | |
| Net premiums written | | 228,135 | | 178,921 | |
| *Change in the provision for unearned premiums* | | | | | |
| Gross amount | | (15,987) | | (6,234) | |
| Reinsurers' share | | 4,452 | | 5,229 | |
| Change in the net provision for unearned premiums | | (11,535) | | (1,005) | |
| *Earned premiums, net of reinsurance* | | | 216,600 | | 177,916 |
| Allocated investment return transferred from the non-technical account | 8 | | 1,770 | | 1,081 |
| **Claims incurred, net of reinsurance** | | | | | |
| *Claims paid* | | | | | |
| Gross amount | | (112,968) | | (114,939) | |
| Reinsurers' share | | 14,556 | | 25,987 | |
| Net claims paid | | (98,412) | | (88,952) | |
| *Change in the provision for claims* | | | | | |
| Gross amount | | (12,692) | | 12,011 | |
| Reinsurers' share | | 2,972 | | (8,253) | |
| Change in the net provisions for claims | | (9,720) | | 3,758 | |
| *Claims incurred, net of reinsurance* | | | (108,132) | | (85,194) |
| Net operating expenses | 4 | | (98,438) | | (79,755) |
| Balance on the technical account for general business | | | 11,800 | | 14,048 |

All items relate only to continuing operations.

# Income Statement

*for the year ended 31 December 2016 continued*

**Non-technical account**

| | Notes | *2016* *£'000* | *2015* *£'000* |
|---|---|---|---|
| Balance on the general business technical account | | 11,800 | 14,048 |
| Investment income | 8 | 2,100 | 1,579 |
| Net unrealised gains/(losses) on investments | 8 | (243) | (434) |
| Investment expenses and charges | 8 | (87) | (64) |
| Allocated investment return transferred to the general business technical account | | (1,770) | (1,081) |
| Exchange gains/(losses) | | 3,230 | (386) |
| Profit for the financial year | | 15,030 | 13,662 |

There are no recognised gains or losses in the accounting period other than those dealt with in the technical and non-technical accounts. Accordingly, a separate statement of comprehensive income has not been presented.

## Statement of Changes in Members' Balances

*for the year ended 31 December 2016*

| | Notes | 2016 £'000 | 2015 £'000 |
|---|---|---|---|
| **At 1 January** | | 26,779 | 39,122 |
| Profit for the financial year | | 15,030 | 13,662 |
| Members' agents' fees | | (1,345) | (1,096) |
| Payments of profit to members' personal reserve funds | 14 | (22,165) | (24,909) |
| **At 31 December** | | 18,299 | 26,779 |

## Statement of Financial Position

*as at 31 December 2016*

| | Notes | 2016 £'000 | 2016 £'000 | 2015 £'000 | 2015 £'000 |
|---|---|---|---|---|---|
| **ASSETS** | | | | | |
| **Investments** | | | | | |
| Financial investments | 9 | | 235,775 | | 215,053 |
| Deposits with ceding undertakings | | | 17 | | 83 |
| **Reinsurers' share of technical provisions** | | | | | |
| Provision for unearned premiums | 10 | 17,564 | | 11,074 | |
| Claims outstanding | 10 | 57,471 | | 46,311 | |
| | | | 75,035 | | 57,385 |
| **Debtors** | | | | | |
| Debtors arising out of direct insurance operations | 11 | 66,846 | | 40,155 | |
| Debtors arising out of reinsurance operations | 12 | 25,232 | | 21,700 | |
| Other debtors | | 944 | | 1,258 | |
| | | | 93,022 | | 63,113 |
| **Cash and other assets** | | | | | |
| Cash at bank and in hand | | 11,367 | | 2,241 | |
| Other assets | 13 | 15,082 | | 13,686 | |
| | | | 26,449 | | 15,927 |
| **Prepayments and accrued income** | | | | | |
| Accrued interest | | 36 | | 45 | |
| Deferred acquisition costs | 10 | 42,664 | | 32,357 | |
| Other prepayments and accrued income | | 1,543 | | 1,747 | |
| | | | 44,243 | | 34,149 |
| **TOTAL ASSETS** | | | 474,541 | | 385,710 |

## Statement of Financial Position

*as at 31 December 2016 continued*

| | Notes | 2016 £'000 | 2016 £'000 | 2015 £'000 | 2015 £'000 |
|---|---|---|---|---|---|
| **MEMBERS' BALANCES AND LIABILITIES** | | | | | |
| Members' balances | | | 18,299 | | 26,779 |
| **Technical provisions** | | | | | |
| Provision for unearned premiums | 10 | 148,737 | | 113,187 | |
| Claims outstanding | 10 | 264,389 | | 215,546 | |
| | | | 413,126 | | 328,733 |
| **Creditors** | | | | | |
| Creditors arising out of direct insurance operations | 15 | 10,595 | | 2,494 | |
| Creditors arising out of reinsurance operations | 16 | 21,421 | | 15,660 | |
| Other creditors | | 8,746 | | 9,924 | |
| | | | 40,762 | | 28,078 |
| Accruals and deferred income | | | 2,354 | | 2,120 |
| **TOTAL MEMBERS' BALANCES AND LIABILITIES** | | | 474,541 | | 385,710 |

The syndicate annual accounts on pages 19 to 63 were approved by the board of Argenta Syndicate Management Limited on 20 March 2017 and were signed on its behalf by

**Andrew J Annandale**
*Managing Director*

## Statement of Cash Flows

*for the year ended 31 December 2016*

| | Notes | *2016* *£'000* | *2015* *£'000* |
|---|---|---|---|
| **Profit on ordinary activities** | | 15,030 | 13,662 |
| Increase/(decrease) in unearned premiums and outstanding claims | | 29,625 | 8,150 |
| (Increase)/decrease in reinsurers' share of unearned premiums and outstanding claims | | (7,990) | 21 |
| (Increase)/decrease in debtors | | (19,068) | (10,903) |
| Increase/(decrease) in creditors | | 16,727 | 455 |
| Investment return | | (1,770) | (1,081) |
| Movements in other assets/liabilities | | (43) | (6) |
| **Net cash inflow from operating activities** | | 32,511 | 10,298 |
| **Investing activities** | | | |
| Investment income received | | 1,922 | 1,319 |
| Purchases of debt and equity instruments | | (91,407) | (130,312) |
| Sales of debt and equity instruments | | 111,292 | 119,803 |
| Purchases of derivatives | | (1,553) | (15,488) |
| Sales of derivatives | | 1,553 | 15,410 |
| (Increase)/decrease in overseas deposits | | (902) | (385) |
| (Increase)/decrease in deposits with ceding undertakings | | 81 | (1) |
| Changes to market values and currencies | | (14,576) | (2,206) |
| **Net cash inflow/(outflow) from investing activities** | | 6,410 | (11,860) |
| **Financing activities** | | | |
| Payments of profit to members' personal reserve funds | | (22,165) | (24,909) |
| Members' agents' fee advances | | (1,345) | (1,096) |
| **Net cash outflow from financing activities** | | (23,510) | (26,005) |
| Increase/(decrease) in cash and cash equivalents | | 15,411 | (27,567) |
| Cash and cash equivalents at 1 January | | 77,389 | 107,672 |
| Exchange differences on opening cash and cash equivalents | | 10,767 | (2,716) |
| **Cash and cash equivalents at 31 December** | 17 | 103,567 | 77,389 |

# Notes to the Accounts

## 1. Accounting policies

### 1.1 *Statement of compliance*

The financial statements have been prepared in compliance with the 2008 Regulations and FRS 102 and FRS 103, being applicable UK GAAP accounting standards, and in accordance with the provisions of Schedule 3 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations relating to insurance companies.

The financial statements are prepared under the historical cost convention except for certain financial instruments which are measured at fair value.

### 1.2 *Basis of preparation*

The financial statements for the year ended 31 December 2016 were approved for issue by the board of directors on 20 March 2017.

The financial statements are prepared in sterling which is the functional and presentational currency of the syndicate and rounded to the nearest £'000.

As permitted by FRS 103 the syndicate continues to apply the existing accounting policies that were applied prior to this standard for its insurance contracts.

The syndicate has elected to apply early the March 2016 amendments to FRS 102, *Fair value hierarchy disclosures*. As a result the fair value hierarchy disclosures, including comparatives, shown in note 9 are prepared on a basis consistent with the measurement of the financial instruments.

### 1.3 *Judgements and key sources of estimation uncertainty*

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the amounts reported for assets and liabilities as at the year-end date and the amounts reported for revenues and expenses during the year. However, the nature of estimation means that actual outcomes could differ from those estimates. The syndicate's key sources of estimation uncertainty are as follows:

*Insurance contract technical provisions*

For insurance contracts, estimates have to be made both for the expected ultimate cost of claims reported at the reporting date and for the expected ultimate cost of claims incurred but not yet reported (IBNR) at the reporting date. It can take a significant period of time before the ultimate claims cost can be established with certainty and for some types of policies, claims IBNR form the majority of the liability in the statement of financial position.

The ultimate cost of outstanding claims is estimated by using a range of standard actuarial claims projection techniques, such as Chain Ladder and Bornhuetter-Ferguson methods.

The main assumption underlying these techniques is that past claims development experience can be used to project future claims development and hence ultimate claims costs. The provision for claims outstanding is based on the estimated ultimate cost of all claims notified but not settled by the year-end date assessed on an individual case basis, together with the provision for related claims handling costs. The provision also includes the estimated cost of claims IBNR at the year-end date based on statistical methods.

**1. Accounting policies** *continued*

These methods generally involve projecting from past experience the development of claims over time to form a view of the likely ultimate claims to be experienced for more recent underwriting, having regard to variations in the business accepted and the underlying terms and conditions. For the most recent years, where a high degree of volatility arises from projections, estimates may be based in part on output from rating and other models of the business accepted and assessments of underwriting conditions. The amount of salvage and subrogation recoveries is separately identified and, where material, reported as an asset.

Similar judgements, estimates and assumptions are employed in the assessment of adequacy of provisions for unearned premiums. Judgement is also required in determining whether the pattern of insurance service provided by a contract requires amortisation of unearned premiums on a basis other than time apportionment.

*Estimates of future premiums*

For certain insurance contracts, premium is initially recognised based on estimates of ultimate premiums. These estimates are judgemental and could result in misstatements of revenue recorded in the financial statements.

The main assumption underlying these estimates is that past premium development can be used to project future premium development.

*Fair value of financial assets and derivatives determined using valuation techniques*

Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of discounted cash flow models and/or mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgement is required to establish fair values. The judgements include considerations of liquidity risk, credit risk and model inputs such as estimated future cash flows based on management's best estimates and discount rates.

For discounted cash flow analysis, estimated future cash flows and discount rates are based on current market information and rates applicable to financial instruments with similar yields, credit quality and maturity characteristics. Estimated future cash flows are influenced by factors such as economic conditions (including country specific risks), concentrations in specific industries, types of instruments or currencies, market liquidity and financial conditions of counterparties. Discount rates are influenced by risk free interest rates and credit risk.

Changes in assumptions about these factors could affect the reported fair value of financial instruments.

Further details are given in note 21.

*1.4 Significant accounting policies*

*Financial investments*

As permitted by FRS 102, the syndicate has elected to apply the recognition and measurement provisions of sections 11 and 12 in full to account for all of its financial instruments.

Financial assets and financial liabilities are recognised when the syndicate becomes a party to the contractual provisions of the instrument.

**1. Accounting policies** *continued*

All financial assets and liabilities are initially measured at transaction price (including transaction costs), except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value (which is normally the transaction price excluding transaction costs), unless the arrangement constitutes a financing transaction. If an arrangement constitutes a financing transaction, the financial asset or financial liability is measured at the present value of the future payments discounted at a market rate of interest for a similar debt instrument.

Financial liabilities are derecognised only when the obligation specified in the contract is discharged, cancelled or expires.

*Derivative financial instruments*

The syndicate uses derivative financial instruments to reduce exposure to foreign exchange risk and interest rate movements. The syndicate does not hold or issue derivative financial instruments for speculative purposes. Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each reporting date. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit or loss depends on the nature of the hedge relationship.

*Cash and cash equivalents*

For the purpose of the cash flow statement, cash and cash equivalents comprise cash at banks and in hand and short term deposits with an original maturity date of three months or less, net of outstanding bank overdrafts.

*Fair value of financial assets*

The syndicate uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

- Level 1: The unadjusted quoted price in an active market for identical assets or liabilities that the entity can access at the measurement date.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable (i.e. developed using market data) for the asset or liability, either directly or indirectly.
- Level 3: Inputs are unobservable (i.e. for which market data is unavailable) for the asset or liability.

See note 9 for details of financial instruments classified by fair value hierarchy.

*Impairment of financial assets*

For financial assets not held at fair value through profit or loss, the syndicate assesses at each reporting date whether the financial asset or group of financial assets is impaired. The syndicate first assesses whether objective evidence of impairment exists for financial assets. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in the collective assessment of impairment.

**1. Accounting policies** *continued*

*Derecognition of financial assets*

A financial asset or, when applicable, a part of a financial asset is derecognised when:

- The rights to the cash flows from the asset have expired; or
- The syndicate retains the right to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass–through' arrangement and either (a) the syndicate has transferred substantially all the risks and rewards of the asset; or (b) the syndicate has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the syndicate has transferred its right to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards nor transferred control of the asset, the asset is recognised to the extent of the syndicate's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the syndicate could be required to repay. In that case, the syndicate also recognises an associated liability.

*Offsetting of financial instruments*

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if, and only if:

- There is a currently enforceable legal right to offset the recognised amounts; and
- There is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

*Financial liabilities*

The syndicate's financial liabilities include trade and other payables, borrowings, insurance payables and derivative financial instruments, where applicable. All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings, net of directly attributable transaction costs.

Trade and other payables and loans and borrowings are subsequently measured at amortised cost using the effective interest rate (EIR) method. Gains and losses are recognised in the income statement when the liabilities are derecognised as well as through the EIR method amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fee or costs that are an integral part of the EIR. The EIR amortisation is included in investment return in the profit or loss.

Derivative financial liabilities are subsequently measured at fair value through profit or loss. A financial liability is derecognised when the obligation under the liability is discharged or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of the existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective amounts is recognised in profit or loss.

**1. Accounting policies** *continued*

*Investment return*

Dividends are recognised when the investments to which they relate are declared 'ex-dividend'. Interest income is recognised on a time proportionate basis taking into account effective interest yield.

Unrealised and realised gains and losses on financial investments are recognised based on the appropriate classification of financial investments and are covered in detail under the accounting policy for financial investments.

An allocation of actual investment return on investments supporting the general insurance technical provisions and associated members' balance is made from the non-technical account to the technical account. Investment return related to non-insurance business and members' balance is attributed to the non-technical account. Investment return has been wholly allocated to the technical account as all investments relate to the technical account.

*Insurance contracts – product classification*

Insurance contracts are those contracts when the syndicate (the insurer/reinsurer) has accepted significant insurance risk from another party (the policyholder/reinsured) by agreeing to compensate the policyholder if a specified uncertain future event (the re/insured event) adversely affects the policyholder. As a general guideline, the syndicate determines whether it has significant insurance risk, by comparing benefits paid with benefits payable if the insured event did not occur. Insurance contracts can also transfer financial risk.

Once a contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly during this period, unless all rights and obligations are extinguished or expire.

Any separable embedded derivatives within an insurance contract are separated and accounted for in accordance with sections 11 and 12 of FRS102 unless the embedded derivative is itself an insurance contract (i.e. the derivative is not separated if the policyholder benefits from the derivative only when the insured event occurs).

*Gross premiums*

Gross written premiums comprise the total premiums receivable for the whole period of cover provided by the contracts entered into during the reporting period, regardless of whether these are wholly due for payment in the reporting period, together with any adjustments arising in the reporting period to such premiums receivable in respect of business written in prior reporting periods. They are recognised on the date on which the policy commences. Additional or return premiums are treated as a remeasurement of the initial premium. Gross written premiums are stated gross of brokerage payable and exclude taxes and duties levied on them.

Written premiums include an estimate for pipeline premiums (i.e. premiums written but not reported to the syndicate by the reporting date) relating only to those underlying contracts of insurance where the period of cover has commenced prior to the reporting date. The most significant assumption in this estimate is that current experience will be consistent with prior year experience.

**1. Accounting policies** *continued*

Under some policies, written premiums are adjusted retrospectively in the light of claims experience or where the risk covered cannot be assessed accurately at the commencement of cover. Where written premiums are subject to an increase retrospectively, recognition of any potential increase is deferred until the additional amount can be ascertained with reasonable certainty. Where written premiums are subject to a reduction, a remeasurement taking account of such a reduction is made as soon as there is an obligation to the policyholder.

*Reinsurance premiums*

Reinsurance written premiums comprise the total premiums payable for all of the cover provided by contracts entered into in the period, including portfolio premiums payable, and are recognised on the date on which the policy incepts. Premiums include any adjustments arising in the accounting period in respect of reinsurance contracts incepting in prior accounting periods.

Under some policies, reinsurance premiums payable are adjusted retrospectively in the light of claims experience or where the risk covered cannot be assessed accurately at the commencement of cover. Where written premiums are subject to an increase retrospectively, recognition of any potential increase is recognised as soon as there is an obligation to the policyholder.

Outwards reinsurance premiums are accounted for and earned in the same accounting period as the premiums for the related direct or inwards business being reinsured.

*Profit commission*

Profit commission is charged by the managing agent at a rate of 15% of the profit on a year of account basis subject to the operation of a deficit clause; the profit commission rate increases from 15% to 17.5% if an average profit measure exceeds 7.5% of capacity. This is charged to the syndicate as incurred but does not become payable until after the appropriate year of account closes, normally at 36 months, although the managing agent may receive payments on account of anticipated profit commissions in line with interim profits released to members.

*Claims*

Claims include all claims occurring during the year, whether reported or not, related internal and external claims handling costs that are directly related to the processing and settlement of claims, a reduction for the value of salvage and other recoveries, and any adjustments to claims outstanding from previous years.

Reinsurance claims are recognised when the related gross insurance claim is recognised according to the terms of the relevant contract.

*Technical provisions*

Technical provisions comprise claims outstanding, provisions for unearned premiums and provisions for unexpired risks.

*Claims outstanding*

The outstanding claims provision is based on the estimated ultimate cost of all claims incurred but not settled at the reporting date, whether reported or not, together with related claims handling costs and reduction for the

**1. Accounting policies** *continued*

expected value of salvage and other recoveries. Delays can be experienced in the notification and settlement of certain types of claims, therefore, the ultimate cost of these cannot be known with certainty at the reporting date. The liability is calculated at the reporting date using a range of standard actuarial claim projection techniques, based on empirical data and current assumptions that may include a margin for adverse deviation. The liability is not discounted for the time value of money.

*Provisions for unearned premiums*

Unearned premiums are those proportions of premiums written in a year that relate to periods of risk after the reporting date. In respect of general insurance business, written premiums are recognised as earned over the period of the policy on a time apportionment basis having regard, where appropriate, to the incidence of risk. The proportion attributable to subsequent periods is deferred as a provision for unearned premiums.

Unearned reinsurance premiums are those proportions of premiums written in a year that relate to periods of risk after the reporting date. Unearned reinsurance premiums are deferred over the term of the underlying direct insurance policies for risks attaching contracts and over the term of the reinsurance contract for losses occurring contracts.

*Unexpired risks*

A liability adequacy provision (the unexpired risks provision) is made where the cost of claims and expenses arising after the end of the financial year from contracts concluded before that date, is expected to exceed the provision for unearned premiums, net of deferred acquisition costs.

The assessment of whether a provision is necessary is made by considering separately each category of business on the basis of information available at the reporting date, after offsetting surpluses and deficits arising on products which are managed together. Investment income is taken into account in calculating the provision.

At 31 December 2016 and 31 December 2015 the syndicate did not have an unexpired risks provision.

*Deferred acquisition costs*

Acquisition costs comprise costs arising from the conclusion of insurance contracts. They include both direct costs, such as intermediary commissions or the cost of drawing up the insurance document or including the insurance contract in the portfolio, and indirect costs, such as the advertising costs or the administrative expenses connected with the processing of proposals and the issuing of policies.

Deferred acquisition costs are costs arising from the conclusion of insurance contracts that are incurred during the reporting period but which relate to a subsequent reporting period and which are carried forward to subsequent reporting periods.

Deferred acquisition costs are amortised over the period in which the related premiums are earned.

The reinsurers' share of deferred acquisition costs is amortised in the same manner as the underlying asset amortisation is recorded in the income statement.

Commissions receivable on outwards reinsurance contracts are deferred and amortised on a straight line basis over the term of the expected premiums payable.

**1. Accounting policies** *continued*

*Reinsurance assets*

The syndicate cedes insurance risk in the normal course of business for all of its areas of operation. Reinsurance assets represent balances due from reinsurance companies. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision or settled claims associated with the reinsurer's policies and are in accordance with the related reinsurance contract.

Reinsurance assets are reviewed for impairment at each reporting date, or more frequently, when an indication of impairment arises during the reporting year. Impairment occurs when there is objective evidence as a result of an event that occurred after initial recognition of the reinsurance asset that the syndicate may not receive all outstanding amounts due under the terms of the contract and the event has a reliably measurable impact on the amounts that the syndicate will receive from the reinsurer. The impairment loss is recorded in the income statement.

Gains or losses on buying reinsurance are recognised in the income statement immediately at the date of purchase and are not amortised. There were no such gains recognised in 2016 or 2015.

Ceded reinsurance arrangements do not relieve the syndicate from its obligations to policyholders.

*Insurance receivables*

Insurance receivables are recognised when due and measured on initial recognition at the fair value of the consideration received or receivable. Subsequent to initial recognition, insurance receivables are measured at amortised cost, using the EIR method. The carrying value of insurance receivables is reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable, with the impairment loss recorded in the income statement.

Insurance receivables are derecognised when the derecognition criteria for financial assets have been met.

*Insurance payables*

Insurance payables are recognised when due and measured on initial recognition at the fair value of the consideration received less directly attributable transaction costs. Subsequent to initial recognition, they are measured at amortised cost using the EIR method. Insurance payables are derecognised when the obligation under the liability is settled, cancelled or expired.

*Foreign currencies*

The syndicate's functional currency and presentational currency is sterling. Transactions denominated in currencies other than the functional currency are initially recorded in the functional currency at the exchange rate ruling at the date of the transactions or at an approximate average rate.

Monetary assets and liabilities (which include all assets and liabilities arising from insurance contracts including unearned premiums and deferred acquisition costs) denominated in foreign currencies are retranslated into the functional currency at the exchange rate ruling on the reporting date.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction and are not subsequently restated. Non-monetary items denominated in a foreign currency, measured at fair value, are translated into the functional currency using the exchange rate ruling at the date when the fair value was determined.

Exchange differences are recorded in the non-technical account.

**1. Accounting policies** *continued*

*Taxation*

Under Schedule 19 of the Finance Act 1993 managing agents are not required to deduct basic rate income tax from trading income. In addition, all UK basic rate income tax deducted from syndicate investment income is recoverable by managing agents and consequently the distribution made to members or their members' agents is gross of tax. Capital appreciation falls within trading income and is also distributed gross of tax.

No provision has been made for any United States Federal Income Tax payable on underwriting results or investment earnings. Any payments on account made by the syndicate are included in the statement of financial position under the heading 'other debtors'.

No provision has been made for any overseas tax payable by members on underwriting results.

*Pension costs*

The underwriting agency operates a defined contribution scheme. Pension contributions relating to syndicate staff are charged to the syndicate and included within net operating expenses.

**2. Particulars of business written**

*Type of business*

An analysis of the technical account balance before investment return is set out below:

| **2016** | *Gross premiums written £'000* | *Gross premiums earned £'000* | *Gross claims incurred £'000* | *Gross operating expenses* £'000* | *Reinsurance balance £'000* | *Total £'000* |
|---|---|---|---|---|---|---|
| **Direct insurance:** | | | | | | |
| Accident and health | 5,927 | 4,509 | (2,304) | (1,965) | (397) | (157) |
| Motor (other classes) | 1,233 | 1,260 | (994) | (467) | (108) | (309) |
| Marine, aviation and transport | 25,354 | 25,721 | (9,926) | (11,331) | (2,439) | 2,025 |
| Energy | 25,970 | 28,239 | (5,272) | (11,920) | (4,230) | 6,817 |
| Fire and other damage to property | 110,060 | 109,794 | (64,950) | (39,661) | (9,443) | (4,260) |
| Third party liability | 12,198 | 7,495 | (4,827) | (3,235) | (247) | (814) |
| Pecuniary loss | 6,240 | 1,223 | (579) | (561) | (157) | (74) |
| | 186,982 | 178,241 | (88,852) | (69,140) | (17,021) | 3,228 |
| **Reinsurance acceptances:** | | | | | | |
| Fire and other damage to property | 28,835 | 28,468 | (11,151) | (8,325) | (4,713) | 4,279 |
| Marine, aviation and transport | 23,824 | 21,442 | (5,336) | (8,667) | (6,692) | 747 |
| Energy | 10,862 | 10,569 | (3,939) | (4,270) | (754) | 1,606 |
| Casualty | 30,212 | 26,008 | (16,382) | (8,036) | (1,420) | 170 |
| | 93,733 | 86,487 | (36,808) | (29,298) | (13,579) | 6,802 |
| | 280,715 | 264,728 | (125,660) | (98,438) | (30,600) | 10,030 |

# Notes to the Accounts

*continued*

**2. Particulars of business written** *continued*

**2015**

| | Gross premiums written £'000 | Gross premiums earned £'000 | Gross claims incurred £'000 | Gross operating expenses* £'000 | Reinsurance balance £'000 | Total £'000 |
|---|---|---|---|---|---|---|
| **Direct insurance:** | | | | | | |
| Accident and health | 2,797 | 2,283 | (1,502) | (1,035) | 37 | (217) |
| Motor (other classes) | 1,248 | 1,119 | (640) | (388) | (124) | (33) |
| Marine, aviation and transport | 23,929 | 25,616 | (10,828) | (11,062) | (182) | 3,544 |
| Energy | 24,466 | 29,643 | (6,419) | (11,816) | (4,959) | 6,449 |
| Fire and other damage to property | 98,092 | 96,210 | (43,919) | (33,848) | (15,826) | 2,617 |
| Third party liability | 2,859 | 1,481 | (2,057) | (533) | 189 | (920) |
| Pecuniary loss | 131 | 127 | (8) | (63) | (4) | 52 |
| | 153,522 | 156,479 | (65,373) | (58,745) | (20,869) | 11,492 |
| **Reinsurance acceptances:** | | | | | | |
| Fire and other damage to property | 26,152 | 24,502 | (4,795) | (7,149) | (2,748) | 9,810 |
| Marine, aviation and transport | 15,804 | 14,808 | (21,617) | (4,921) | 2,013 | (9,717) |
| Energy | 10,653 | 10,748 | (3,630) | (3,843) | (1,857) | 1,418 |
| Casualty | 20,411 | 13,771 | (7,513) | (5,097) | (1,197) | (36) |
| | 73,020 | 63,829 | (37,555) | (21,010) | (3,789) | 1,475 |
| | 226,542 | 220,308 | (102,928) | (79,755) | (24,658) | 12,967 |

All premiums were concluded in the UK.

The reinsurance balance includes reinsurance commission receivable.

*Gross operating expenses are the same as net operating expenses shown in the income statement, as no commissions in respect of outward reinsurance were set off in arriving at the net operating expenses.

*Geographical analysis by destination*

| | *Gross written premiums* 2016 £'000 | 2015 £'000 |
|---|---|---|
| UK | 91,544 | 58,257 |
| EU | 16,106 | 12,636 |
| Other | 173,065 | 155,649 |
| | 280,715 | 226,542 |

**3. Movement in prior year's provision for claims outstanding**

An overall improvement of £14,679,000 on prior years' provisions was experienced during the year. Improvements of £4,992,000 on fire and other damage to property, £5,979,000 on marine, aviation and transport and £4,044,000 on energy were partially offset by a deterioration of £248,000 on reinsurance acceptances.

(2015: An overall deterioration of £1,776,000 on prior years' provisions was experienced during the year. A deterioration of £3,356,000 on fire and other damage to property was partially offset by improvements of £1,275,000 on marine, aviation and transport and £344,000 on reinsurance acceptances.)

**4. Net operating expenses**

| | 2016 £'000 | 2015 £'000 |
|---|---|---|
| Acquisition costs | 85,488 | 67,537 |
| Change in deferred acquisition costs | (5,138) | (2,489) |
| Administrative expenses | 18,088 | 14,707 |
| | 98,438 | 79,755 |

Administrative expenses include:

| | 2016 £'000 | 2015 £'000 |
|---|---|---|
| Auditor's remuneration – audit of the syndicate accounts | 210 | 188 |
| – other services pursuant to regulations and Lloyd's byelaws | 127 | 116 |
| Operating lease rentals – office equipment | 43 | 62 |
| – other | – | 3 |
| Members' standard personal expenses | 8,084 | 6,463 |
| Other remuneration paid to auditors: | | |
| Audit of the managing agent's annual accounts | 15 | 14 |

Total commissions for direct insurance accounted for in the year amounted to £53.4 million (2015: £42.0 million).

Members' standard personal expenses include Lloyd's subscriptions, New Central Fund contributions, managing agent's fees and profit commission.

**5. Staff numbers and costs**

All staff are employed by the managing agency. The following amounts were recharged to the syndicate in respect of staff costs:

| | 2016 £'000 | 2015 £'000 |
|---|---|---|
| Wages and salaries | 8,649 | 8,056 |
| Social security costs | 1,172 | 1,048 |
| Other pension costs | 639 | 591 |
| | 10,460 | 9,695 |

The average number of employees employed by the managing agency but working for the syndicate during the year was as follows:

| | 2016 Number | 2015 Number |
|---|---|---|
| Administration and finance | 21 | 20 |
| Underwriting | 22 | 22 |
| Underwriting support | 24 | 22 |
| Claims | 8 | 7 |
| | 75 | 71 |

### 6. Emoluments of the directors of ASML and the active underwriter

ASML charged the syndicate the following amounts in respect of emoluments paid to its directors, including the active underwriter of the syndicate:

| | *2016* | *2015* |
|---|---|---|
| | *£'000* | *£'000* |
| Emoluments | 1,889 | 1,702 |

No advances or credits granted by ASML to any of its directors subsisted during the year.

### 7. Active underwriter's emoluments

The following aggregate remuneration was charged to the syndicate in respect of the active underwriter:

| | *2016* | *2015* |
|---|---|---|
| | *£'000* | *£'000* |
| Emoluments | 316 | 316 |

### 8. Investment return

| | *2016* | *2015* |
|---|---|---|
| | *£'000* | *£'000* |
| Income from other financial investments | 2,343 | 2,012 |
| Net losses on realisation of investments | | |
| – designated at fair value through profit or loss | (243) | (433) |
| Total investment income | 2,100 | 1,579 |
| Net unrealised gains/(losses) on investments | | |
| – designated at fair value through profit and loss | (243) | (434) |
| Investment expenses and charges | (87) | (64) |
| Total investment return | 1,770 | 1,081 |

## 9. Financial investments

| | 31 December 2016 | | |
|---|---|---|---|
| | *Carrying value £'000* | *Purchase price £'000* | *Listed £'000* |
| Shares and other variable yield securities and units in unit trusts | | | |
| – designated at fair value through profit or loss | 89,452 | 89,749 | 57,800 |
| Debt securities and other fixed income securities | | | |
| – designated at fair value through profit or loss | 140,187 | 139,922 | – |
| Derivative assets held at fair value through profit and loss | – | – | – |
| Deposits with credit institutions held at fair value | 1,854 | 1,854 | – |
| Loans secured by mortgages held at fair value | 4,282 | 4,290 | – |
| | 235,775 | 235,815 | 57,800 |

| | 31 December 2015 | | |
|---|---|---|---|
| | *Carrying value £'000* | *Purchase price £'000* | *Listed £'000* |
| Shares and other variable yield securities and units in unit trusts | | | |
| – designated at fair value through profit or loss | 73,216 | 73,110 | 65,162 |
| Debt securities and other fixed income securities | | | |
| – designated at fair value through profit or loss | 135,211 | 135,584 | – |
| Derivative assets held at fair value through profit and loss | – | – | – |
| Deposits with credit institutions held at fair value | 438 | 438 | – |
| Loans secured by mortgages held at fair value | 6,188 | 6,178 | – |
| | 215,053 | 215,310 | 65,162 |

The shares and other variable yield securities and units in unit trusts relate to holdings in highly diversified collective investment schemes, which include an element of low volatility absolute return funds managed in accordance with the UCITS regulations.

There was no material change in fair value for financial instruments held at fair value attributable to own credit risk in the current or comparative period.

There have been no day 1 profits recognised in respect of financial instruments designated at fair value through profit or loss.

The syndicate's investment managers are permitted to directly purchase derivative financial instruments (interest rate futures) to hedge its interest rate risks. These derivatives are classified as trading instruments.

**9. Financial investments** *continued*

The following table shows financial investments including overseas deposits (note 13) recorded at fair value analysed between the three levels in the fair value hierarchy.

| 31 December 2016 | *Level 1* *£'000* | *Level 2* *£'000* | *Level 3* *£'000* | *Total* *£'000* |
|---|---|---|---|---|
| Shares and other variable yield securities and units in unit trusts | 31,872 | 57,580 | – | 89,452 |
| Debt securities and other fixed income securities | 73,195 | 66,992 | – | 140,187 |
| Loans and deposits with credit institutions | 1,854 | 4,282 | – | 6,136 |
| Overseas deposits | 3,624 | 11,458 | – | 15,082 |
| | 110,545 | 140,312 | – | 250,857 |

| 31 December 2015 | *Level 1* *£'000* | *Level 2* *£'000* | *Level 3* *£'000* | *Total* *£'000* |
|---|---|---|---|---|
| Shares and other variable yield securities and units in unit trusts | 32,625 | 40,589 | 2 | 73,216 |
| Debt securities and other fixed income securities | 74,152 | 61,059 | – | 135,211 |
| Loans and deposits with credit institutions | 438 | 6,188 | – | 6,626 |
| Overseas deposits | 10,245 | 3,441 | – | 13,686 |
| | 117,460 | 111,277 | 2 | 228,739 |

Included in the level 1 category are financial assets that are measured by reference to published quotes in an active market. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry syndicate, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Included in the level 2 category are financial assets measured using a valuation technique based on assumptions that are supported by prices from observable current market transactions. For example, assets for which pricing is obtained via pricing services but where prices have not been determined in an active market, financial assets with fair values based on broker quotes, investments in private equity funds with fair values obtained via fund managers and assets that are valued using the syndicate's own models whereby the significant inputs into the assumptions are market observable.

**9. Financial investments** *continued*

Included in the level 3 category, are financial assets measured using a valuation technique (model) based on assumptions that are neither supported by prices from observable current market transactions in the same instrument nor are they based on available market data. Therefore, unobservable inputs reflect the syndicate's own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). These inputs are developed based on the best information available, which might include the syndicate's own data.

The asset class in the level 3 category is hedge funds. For these there is not a liquid market for the investments and as a result the valuations received from the investment manager, modelled on the values of the underlying assets, have been impaired by 90% as an illiquidity adjustment. The amounts involved were immaterial at both year ends.

**10. Technical provisions**

*Claims outstanding*

| | | *2016* | |
|---|---|---|---|
| | *Gross* | *Reinsurers' share* | *Net* |
| | *£'000* | *£'000* | *£'000* |
| At 1 January | 215,546 | (46,311) | 169,235 |
| Claims incurred in current underwriting year | 66,048 | (11,599) | 54,449 |
| Claims incurred in prior underwriting years | 59,612 | (5,929) | 53,683 |
| Claims paid during the year | (112,968) | 14,556 | (98,412) |
| Foreign exchange | 36,151 | (8,188) | 27,963 |
| At 31 December | 264,389 | (57,471) | 206,918 |

| | | *2015* | |
|---|---|---|---|
| | *Gross* | *Reinsurers' share* | *Net* |
| | *£'000* | *£'000* | *£'000* |
| At 1 January | 218,224 | (51,978) | 166,246 |
| Claims incurred in current underwriting year | 54,461 | (12,947) | 41,514 |
| Claims incurred in prior underwriting years | 48,467 | (4,787) | 43,680 |
| Claims paid during the year | (114,939) | 25,987 | (88,952) |
| Foreign exchange | 9,333 | (2,586) | 6,747 |
| At 31 December | 215,546 | (46,311) | 169,235 |

**10. Technical provisions** *continued*

*Provision for unearned premiums*

| | 2016 Gross £'000 | 2016 Reinsurers' share £'000 | 2016 Net £'000 |
|---|---|---|---|
| At 1 January | 113,187 | (11,074) | 102,113 |
| Premiums written in the year | 280,715 | (52,580) | 228,135 |
| Premiums earned in the year | (264,728) | 48,128 | (216,600) |
| Foreign exchange | 19,563 | (2,038) | 17,525 |
| At 31 December | 148,737 | (17,564) | 131,173 |

| | 2015 Gross £'000 | 2015 Reinsurers' share £'000 | 2015 Net £'000 |
|---|---|---|---|
| At 1 January | 102,359 | (5,428) | 96,931 |
| Premiums written in the year | 226,542 | (47,621) | 178,921 |
| Premiums earned in the year | (220,308) | 42,392 | (177,916) |
| Foreign exchange | 4,594 | (417) | 4,177 |
| At 31 December | 113,187 | (11,074) | 102,113 |

*Deferred acquisition costs*

| | 2016 £'000 | 2015 £'000 |
|---|---|---|
| At 1 January | 32,357 | 28,700 |
| Change in deferred acquisition costs | 5,138 | 2,489 |
| Foreign exchange | 5,169 | 1,168 |
| At 31 December | 42,664 | 32,357 |

**11. Debtors arising out of direct insurance operations**

| | 2016 £'000 | 2015 £'000 |
|---|---|---|
| Amounts falling due within one year – intermediaries | 66,789 | 40,097 |
| Amounts falling due after one year – intermediaries | 57 | 58 |
| | 66,846 | 40,155 |

**12. Debtors arising out of reinsurance operations**

| | 2016 £'000 | 2015 £'000 |
|---|---|---|
| Amounts falling due within one year | 25,131 | 21,628 |
| Amounts falling due after one year | 101 | 72 |
| | 25,232 | 21,700 |

**13. Other assets**

| | 2016 £'000 | 2015 £'000 |
|---|---|---|
| **Overseas deposits** | | |
| Amounts advanced in Illinois, USA as a condition of carrying on business there | 1,295 | 924 |
| Amounts advanced in Australia, South Africa and other countries as a condition of carrying on business there | 13,787 | 12,762 |
| | 15,082 | 13,686 |

**14. Reconciliation of members' balances**

Members participate on syndicates by reference to years of account and their ultimate result, assets and liabilities are assessed with reference to policies incepting in that year of account in respect of their membership of a particular year.

Transfers to members' personal reserve funds relate to transfers of £13,765,000 in respect of the 2013 year of account and £8,400,000 in respect of the 2014 year of account. (2015: transfers to members' personal reserve funds of £16,918,000 in respect of the 2012 year of account and £7,991,000 in respect of the 2013 year of account).

**15. Creditors arising out of direct insurance operations**

| | 2016 £'000 | 2015 £'000 |
|---|---|---|
| Amounts falling due within one year | 10,595 | 2,490 |
| Amounts falling due after one year | – | 4 |
| | 10,595 | 2,494 |

**16. Creditors arising out of reinsurance operations**

| | 2016 £'000 | 2015 £'000 |
|---|---|---|
| Amounts falling due within one year | 21,369 | 15,660 |
| Amounts falling due after one year | 52 | – |
| | 21,421 | 15,660 |

### 17. Cash and cash equivalents

| | 2016 | 2015 |
|---|---|---|
| | £'000 | £'000 |
| Cash at bank and in hand | 11,367 | 2,241 |
| Short-term deposits with financial institutions | 92,200 | 75,148 |
| | 103,567 | 77,389 |

### 18. Off balance sheet items

The syndicate has not been party to an arrangement which is not reflected in its statement of financial position, where material risks or benefits arise for the syndicate.

### 19. Related parties

**Argenta Holdings plc**

ASML is a wholly owned subsidiary of AHP which owns 100% of the voting and economic rights of ASML. AHP is regarded by ASML as its ultimate parent and is also the parent undertaking of the smallest and largest group to consolidate the financial statements of ASML. Copies of the accounts for AHP can be obtained from Companies House.

AHP is controlled by Glenrinnes Farms Ltd, RBC cees Trustee Ltd as trustee of the Argenta Employee Benefit Trust and Wren Properties Ltd, who own 44.75%, 25% and 25% of the economic and voting rights in the company respectively. Mr Alasdair Locke is a 99% controller of Glenrinnes Farms Ltd and up until 2014 owned this shareholding directly. Wren Properties Ltd is owned and controlled by members of the Robinson family.

AHP and its related parties provide certain underwriting, administrative, accounting, human resource, information technology and risk management and compliance services to ASML. These services are provided on a non-profit making basis by way of inter-group cross charges and direct salary charges.

Argenta Tax & Corporate Services Ltd (ATCSL), an AHP group company, provides taxation services to the syndicate. Fees are agreed on a commercial basis and the profit to ATCSL generated from providing these services is, as in 2015, less than £1,000.

AUA, a subsidiary of AHP, is a service company approved by Lloyd's and the MAS to operate on the Lloyd's Asia platform. AUA also holds a licence granted by the Australian Securities and Investments Commission and has a branch office approved by Lloyd's in Sydney, Australia. Syndicate 2121 uses this service company as a coverholder to bind risks on its behalf. Such services relating to business written in Singapore are provided at cost plus a small profit margin of 5% mainly for tax purposes. The total value of the margin is less than £80,000 for 2016 (2015: £70,000). The commission retained by AUA for business underwritten by the Australian branch is 27.5% of gross premium, which is in line with other Australian facilities currently supported by the syndicate. This commission charged in Australia covers original acquisition costs, branch office expenses and processing costs.

Other than by virtue of directorship fees, salaries and other related remuneration in respect of their employment by AHP or its related parties, and any potential future investment earnings or growth in capital value arising from their shareholding, none of the directors, officers, shareholders or related parties concerned, derive any personal benefit from the arrangements that exist.

**19. Related parties** *continued*

**Business transactions**

Mr Mumford was a director of another Lloyd's managing agency, Neon Underwriting Ltd (formerly Marketform Managing Agency Ltd), until his resignation on 10 February 2017.

Mr Whiter is chairman of Lloyd's broker Ed Broking (London) Ltd (formerly CGNMB LLP) and a director of its parent company, Ed Broking Group Ltd (formerly Cooper Gay Swett & Crawford Ltd).

Mr Graham White, who was a director of ASML until his resignation on 31 March 2015, is a director of Lloyd's broker Marine Aviation & General (London) Ltd.

Mr Newbery was a director of Lloyd's broker Tyser & Co Ltd, a member of the board of underwriting agency Aquila Underwriting LLP, and a director of Hawkes Bay Holdings Ltd, the parent company of both entities, until his resignation from all of the companies on 31 October 2015. Mr Newbery became a non-executive director of Arthur J. Gallagher Holdings (UK) Limited, the holding company of a number of Lloyd's brokers, and the non-executive chairman of Pen Underwriting Limited, a managing general agent, on 11 November 2015 and 8 December 2015 respectively.

The above entities may in the past have transacted business with syndicates managed by ASML and may do so in the future. Any such business, however, has been and will continue to be, conducted on an arm's length commercial basis with no involvement, either directly or indirectly, from the individuals above.

Other than directorship fees, salaries and other related remuneration, no personal benefit is derived by the individuals concerned from these arrangements.

Messrs Hunt and Mumford both benefit from fees paid in respect of independent review services that they carry out on sections of Syndicate 2121's book of business. It is a regulatory requirement that such reviews are performed by individuals who are separate from the day to day underwriting of the specific classes of business under review and have the necessary skill and experience to fulfil their independent review obligations.

Total fees payable to ASML in respect of services provided to the syndicate amounted to £2.0 million (2015: £1.8 million). Profit commission is only due on closure of the year of account though managing agents may receive payments on account of anticipated profit commissions in line with interim profits released to members. During 2016, profit commission of £4,856,000 (2015: £5,732,000) was due to ASML. Creditors at the year-end include amounts in respect of profit commission due to ASML of £8,042,000 (2015: £8,915,000).

In addition to this, £13,352,000 (2015: £12,458,000) was recharged by ASML for expenses paid on behalf of the syndicate. Creditors at the year-end include amounts due to ASML of £560,000 (2015: £719,000).

Mr Annandale and Mr Maguire are directors of AUA, which receives a commission on business accepted under binding authorities granted to it by Syndicate 2121. The total commissions payable were £2,664,000 (2015: £1,377,000). Creditors at the year-end include amounts due to AUA of £110,000 (2015: £207,000).

**Capital support for Syndicate 2121**

Mr Annandale is a director of Argenta Private Capital Limited (APCL), a subsidiary of AHP. Messrs Graham White and David Williams were directors of APCL until their resignations on 31 July 2015 and 29 July 2015 respectively, and were also directors of ASML until their resignations on 31 March 2015.

Mr Alan Tucker, who was a director of ASML until his resignation on 31 March 2015, is a director of Cantril Investments Ltd, Kemah Lime Street Capital Ltd, Kling Investment Ltd, Nidarich Ltd and Rechter Underwriting Ltd, all corporate members.

**19. Related parties** *continued*

APCL allocates capacity to Syndicate 2121 for the 2014 to 2017 years of account. Cantril Investments Ltd, Rechter Underwriting Ltd, Kling Investment Ltd and Kemah Lime Street Capital Ltd all allocate capacity to Syndicate 2121 for the 2014 to 2017 years of account.

Nidarich Ltd allocates capacity to Syndicate 2121 for the 2014 and 2015 years of account.

Mr Tucker is also a director of Fifteen B Limited, which is a member of Alizadeh Underwriting LLP that allocates capacity to Syndicate 2121 for the 2014 to 2017 years of account, and also a director of Inswin Ltd, which is a member of Winins LLP that allocates capacity to Syndicate 2121 for the 2017 year of account only.

Mr Annandale is or was a director of the following corporate members:

Argenta Underwriting No. 2 Limited (AU2)
Argenta Underwriting No. 3 Limited (AU3)
Argenta Underwriting No. 8 Limited (AU8)
Argenta Underwriting No. 9 Limited (AU9)
Argenta Underwriting No. 10 Limited (AU10)
Argenta Underwriting No. 11 Limited (AU11)
Argenta Underwriting No. 12 Limited (AU12) (resigned 15 December 2016)

AU12 was sold to a third party in December 2016. The other Argenta underwriting corporate members above remain subsidiaries of AHP. In relation to Syndicate 2121, all of these corporate members participate on the 2014 to 2017 years of account.

Other than directorship fees, salaries and other related remuneration and any potential future investment earnings or growth in capital value arising from shareholdings in the Lloyd's corporate members, no personal benefit is derived by the individuals concerned from these arrangements.

Mr Alasdair Locke is a director of and, via his company Glenrinnes Farms Ltd, a shareholder in AHP. Glenrinnes Farms Ltd provides capital to AU2, AU3 and AU9 for the 2014 to 2017 years of account on an excess basis through Funds at Lloyd's Provider's Agreements. Glenrinnes Farms Ltd also participates on AU3 on a pro-rata basis for each of the 2014 and 2015 years of account. Each corporate member in turn provides capital to Syndicate 2121 for each of the 2014 to 2017 years of account. Mr Locke derives no personal benefit from these arrangements other than a fee or a proportionate share of the underwriting result of the corporate members to which he is contractually entitled through his Glenrinnes Farms Ltd participation.

As part of the consideration for the provision of all such capital by Glenrinnes Farms Ltd, it was granted an option by AHP and its shareholders to acquire £98.5 million of Syndicate 2121 capacity. The option was closed out during 2015 following a payment to compensate for this.

All capital providers who underwrite on Syndicate 2121 are charged managing agency fees and profit commission on a standard basis, apart from one where the charges are less advantageous, as disclosed in the Register of Underwriting Agency Charges.

On 18 March 2017 a transaction was entered into for AHP, the parent company of the managing agent for Syndicate 2121, to be acquired by Hannover Rück SE. The transaction is expected to close in the third quarter of 2017 subject to all necessary approvals.

There are no other transactions or arrangements to be disclosed.

**20. Funds at Lloyd's**

In case syndicate assets prove insufficient to meet members' underwriting liabilities, every member is required to hold additional capital at Lloyd's which is held in trust and known as Funds at Lloyd's (FAL).

The level of FAL that Lloyd's requires a member to maintain is determined by Lloyd's based on PRA requirements and resource criteria according to the nature and the amount of risk to be underwritten by the member and the assessment of the reserving risk in respect of business that has been underwritten. FAL is not hypothecated to any specific syndicate participation by a member and therefore there are no specific funds available to a syndicate which can be precisely identified as its capital. As such, no amount has been shown in these annual accounts by way of FAL. However, the managing agent is able to make a call on the members' FAL to meet liquidity requirements or to settle losses.

**21. Risk management**

**(a) Governance framework**

The primary objective of the syndicate's risk management framework is to protect the syndicate's members from events that hinder the sustainable achievement of financial performance objectives, including failing to exploit opportunities. ASML recognises the critical importance of having efficient and effective risk management systems in place.

The managing agent has established a risk management function for the syndicate with clear terms of reference from the board of directors and its sub-committees. This is supplemented with a clear organisational structure with documented delegated authorities and responsibilities from the board of directors to executive management committees and senior managers. Lastly, a syndicate policy framework which sets out the risk profiles for the syndicate, risk management, control and business conduct standards for the syndicate's operations has been put in place. Each policy has a member of senior management charged with overseeing compliance with the policy throughout the syndicate.

The board of directors approves the risk management policies and meets regularly to approve any commercial, regulatory and organisational requirements of such policies. These policies define the identification of risk and its interpretation to ensure the appropriate quality and diversification of assets, align underwriting and reinsurance strategy to the syndicate goals, and specify reporting requirements. Significant emphasis is placed on assessment and documentation of risks and controls, including the articulation of 'risk appetite'.

**(b) Capital management objectives**

*Capital framework at Lloyd's*

Lloyd's is a regulated undertaking and subject to the supervision of the PRA under the Financial Services and Markets Act 2000.

Effective 1 January 2016, Lloyd's is subject to the Solvency II capital regime and the Solvency I figures are no longer applicable from that date. Although the capital regime has changed, this has not significantly impacted the solvency capital requirement (SCR) of the syndicate, since this has been previously calculated based on Solvency II principles, as described below.

**21. Risk management** *continued*

Within the supervisory framework, Lloyd's applies capital requirements at member level and centrally to ensure that Lloyd's complies with Solvency II capital requirements, and beyond that to meet its own financial strength, licence and ratings objectives.

Although Lloyd's capital setting processes use a capital requirement set at syndicate level as a starting point, the requirement to meet Solvency II and Lloyd's capital requirements apply at overall and member level only respectively, not at syndicate level. Accordingly the capital requirement in respect of Syndicate 2121 is not disclosed in these financial statements.

*Lloyd's capital setting process*

In order to meet Lloyd's requirements, each syndicate is required to calculate its SCR for the prospective underwriting year. This amount must be sufficient to cover a 1 in 200 year loss, reflecting uncertainty in the ultimate run-off of underwriting liabilities (SCR 'to ultimate'). The syndicate must also calculate its SCR at the same confidence level but reflecting uncertainty over a one year time horizon (one year SCR) for Lloyd's to use in meeting Solvency II requirements. The SCRs of each syndicate are subject to review by Lloyd's and approval by the Lloyd's Capital and Planning Group.

A syndicate may be comprised of one or more underwriting members of Lloyd's. Each member is liable for its own share of underwriting liabilities on the syndicate on which it participates but not other members' shares. Accordingly, the capital requirement that Lloyd's sets for each member operates on a similar basis. For a member participating on a single syndicate, its SCR is determined by the member's share of the syndicate SCR 'to ultimate'. Where a member participates on more than one syndicate a credit for diversification is included to reflect the spread of risk. The credit given is consistent with determining an SCR which reflects the capital requirement to cover a 1 in 200 year loss 'to ultimate' for that member. Over and above this, Lloyd's applies an uplift to the member's SCR to determine the overall level of capital required. This is known as the member's Economic Capital Assessment (ECA). The purpose of this uplift, which is a Lloyd's not a Solvency II requirement, is to meet Lloyd's financial strength, licence and ratings objectives. The capital uplift applied for 2016 was 35% (2015: 35%) of the member's SCR 'to ultimate'.

*Provision of capital by members*

Each member may provide capital to meet its ECA either by assets held in trust by Lloyd's specifically for that member (FAL), held within and managed within a syndicate (funds in syndicate) or as the member's share of the members' balances on each syndicate on which it participates.

Accordingly all of the assets less liabilities of the syndicate, as represented in the members' balances reported on the statement of financial position on page 23, represent resources available to meet members' and Lloyd's capital requirements.

**(c) Insurance risk**

The principal risk the syndicate faces under insurance contracts is that the actual claims and benefit payments or the timing thereof, differ from expectations. This is influenced by the frequency of claims, severity of claims, actual benefits paid and subsequent development of long–term claims. Therefore, the objective of the syndicate is to ensure that sufficient reserves are available to cover these liabilities. References to insurance business should, as appropriate, be understood to include the equivalent reinsurance business underwritten by the syndicate.

**21. Risk management** *continued*

The risk exposure is mitigated by diversification across a large portfolio of insurance contracts and geographical areas. The variability of risks is also improved by careful selection and implementation of underwriting strategy guidelines, as well as the use of reinsurance arrangements.

The syndicate purchases reinsurance as part of its risks mitigation programme. Reinsurance ceded is placed on both a proportional and non–proportional basis. The majority of proportional reinsurance is quota share reinsurance which is taken out to reduce the overall exposure to certain classes of business. Non–proportional reinsurance is primarily excess of loss reinsurance designed to mitigate the syndicate’s net exposure to catastrophe losses and large individual risk losses. Retention limits for the excess of loss reinsurance vary by product line and territory.

Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision and are in accordance with the reinsurance contracts. Although the syndicate has reinsurance arrangements, it is not relieved of its direct obligations to its policyholders and thus a credit exposure exists with respect to ceded insurance, to the extent that any reinsurer is unable to meet its obligations assumed under such reinsurance agreements. The syndicate’s placement of reinsurance is diversified such that it is neither dependent on a single reinsurer nor are the operations substantially dependent upon any single reinsurance contract.

The syndicate principally issues the following types of general insurance contracts: fire and other damage to property; marine, aviation and transport; energy; and third party liability. Risks usually cover twelve months duration.

The most significant risks arise from natural disasters, terrorist activities, cyber attacks, large risk losses and adverse attritional claims experience. For longer tail claims that take some years to settle, there is also inflation risk.

The above risk exposure is mitigated by diversification across a large portfolio of insurance contracts and geographical areas. The variability of risks is improved by careful selection and implementation of underwriting strategies, which are designed to ensure that risks are diversified in terms of type of risk and level of insured benefits. This is largely achieved through diversification across industry sectors and geography. Furthermore, strict claim review policies to assess all new and ongoing claims, regular detailed review of claims handling procedures and frequent investigation of possible fraudulent claims are all policies and procedures put in place to reduce the risk exposure of the syndicate. The syndicate further enforces a policy of actively managing and promptly pursuing claims, in order to reduce its exposure to unpredictable future developments that can negatively impact the business. Inflation risk is mitigated by taking expected inflation into account where appropriate when estimating insurance contract liabilities.

The syndicate has also limited its exposure by imposing maximum claim amounts on certain contracts as well as the use of reinsurance arrangements in order to limit exposure to catastrophic events (e.g. hurricanes, earthquakes and flood damage).

The purpose of these underwriting and reinsurance strategies is to limit exposure to catastrophes based on the syndicate’s risk appetite as decided by management. The overall aim is currently to restrict the impact of a single Realistic Disaster Scenario (RDS) on a gross of reinsurance basis to less than 80% of the ECA, and less than 30% on a net of reinsurance basis. The reinsurance counterparty exposure is managed such that the exposure to, for instance, a single ‘A’ rated reinsurer is estimated not to exceed 10% of the total recoverable amount for the programme. The board may decide to increase or decrease the maximum tolerances based on market conditions and other factors.

**21. Risk management** *continued*

The syndicate uses both its own and commercially available proprietary risk management software to assess catastrophe exposure. However, there is always a risk that the assumptions and techniques used in these models are unreliable or that claims arising from an unmodelled event are greater than those arising from a modelled event.

As a further guide to the level of catastrophe exposure written by the syndicate, the following table shows hypothetical claims arising for various RDS's based on the syndicate's expected risk exposures estimated for the 2017 Syndicate Business Forecast.

| *RDS event* | *Industry loss £m* | *Estimated gross loss £m* | *Estimated final net loss £m* |
|---|---|---|---|
| Carolinas windstorm (second event) | 26,866 | 96 | 60 |
| US Florida windstorm | 93,284 | 119 | 35 |
| European windstorm | 19,008 | 56 | 25 |
| US Gulf windstorm | 83,209 | 108 | 25 |
| Los Angeles earthquake | 58,209 | 120 | 24 |

The table below sets out the concentration of outstanding claim liabilities and unearned premiums by type of contract:

| | *31 December 2016* | | *31 December 2015* | |
|---|---|---|---|---|
| | *Gross liabilities £'000* | *Net liabilities £'000* | *Gross liabilities £'000* | *Net liabilities £'000* |
| **Direct insurance:** | | | | |
| Accident and health | 4,583 | 4,318 | 2,007 | 1,755 |
| Motor (other classes) | 977 | 973 | 824 | 823 |
| Marine, aviation and transport | 52,642 | 46,866 | 50,460 | 44,457 |
| Energy | 42,718 | 37,707 | 43,108 | 37,930 |
| Fire and other damage to property | 125,891 | 110,275 | 101,214 | 88,230 |
| Third party liability | 13,035 | 11,665 | 3,887 | 3,180 |
| Pecuniary loss | 6,147 | 3,759 | 48 | 41 |
| | 245,993 | 215,563 | 201,548 | 176,416 |
| **Reinsurance acceptances:** | | | | |
| Fire and other damage to property | 55,317 | 37,019 | 44,874 | 33,250 |
| Marine, aviation and transport | 39,314 | 32,563 | 38,640 | 27,222 |
| Energy | 22,708 | 20,296 | 18,536 | 17,649 |
| Casualty | 49,794 | 32,650 | 25,135 | 16,811 |
| | 167,133 | 122,528 | 127,185 | 94,932 |
| | 413,126 | 338,091 | 328,733 | 271,348 |

**21. Risk management** *continued*

The geographical concentration of the outstanding claim liabilities and unearned premiums is noted below. The disclosure is based on the domicile of counterparties. The analysis is not expected to be materially different if based on the countries in which the risks are situated.

| | *31 December 2016* | | *31 December 2015* | |
|---|---|---|---|---|
| | *Gross liabilities £'000* | *Net liabilities £'000* | *Gross liabilities £'000* | *Net liabilities £'000* |
| United Kingdom | 116,283 | 86,142 | 79,514 | 58,882 |
| EU | 18,424 | 15,870 | 16,423 | 14,660 |
| USA | 142,489 | 118,455 | 124,309 | 103,180 |
| Canada | 13,365 | 11,967 | 13,050 | 11,576 |
| Other | 122,565 | 105,657 | 95,437 | 83,050 |
| | 413,126 | 338,091 | 328,733 | 271,348 |

*Key assumptions*

The principal assumption underlying the liability estimates is that the future claims development will follow a similar pattern to past claims development experience. This includes assumptions in respect of claim indemnity costs, claim handling costs and claims inflation for each underwriting year. For more recent years of account, 'a priori' loss ratio selections are also key assumptions in determining the reserves, which are themselves based on historical experience as well as judgements to reflect current underwriting conditions.

Additional qualitative judgements are used to assess the extent to which past trends may not apply in the future, for example: one–off occurrence; changes in market factors; economic conditions; as well as internal factors such as portfolio mix, policy conditions and claims handling procedures. Judgement is further used to assess the extent to which external factors such as judicial decisions and government legislation affect the estimates.

Other key circumstances affecting the reliability of assumptions include the occurrence of large losses, delays in settlement and changes in foreign currency rates.

*Sensitivities*

The claim liabilities are sensitive to the key assumptions that follow. It has not been possible to quantify the sensitivity of certain assumptions such as legislative changes or uncertainty in the estimation process.

The following analysis is performed for reasonably possible movements in key assumptions with all other assumptions held constant, showing the impact on gross and net liabilities, profit and members' balances. The correlation of assumptions will have a significant effect in determining the ultimate claims liabilities, but to demonstrate the impact due to changes in each assumption, assumptions had to be changed on an individual basis. It should be noted that movements in these assumptions are non–linear.

**21. Risk management** *continued*

| *31 December 2016* | *Change in assumptions* | *Impact on gross liabilities £'000* | *Impact on net liabilities £'000* | *Impact on profit £'000* | *Impact on members' balance £'000* |
|---|---|---|---|---|---|
| 'A priori' loss ratios | +5% | 5,212 | 4,327 | (3,941) | (3,941) |
| Incurred claims development patterns | Recede development by 1 month | 9,293 | 8,219 | (7,624) | (7,624) |

| *31 December 2015* | *Change in assumptions* | *Impact on gross liabilities £'000* | *Impact on net liabilities £'000* | *Impact on profit £'000* | *Impact on members' balance £'000* |
|---|---|---|---|---|---|
| 'A priori' loss ratios | +5% | 4,469 | 3,994 | (3,088) | (3,088) |
| Incurred claims development patterns | Recede development by 1 month | 8,187 | 7,486 | (6,883) | (6,883) |

The method used for deriving sensitivity information and the significant assumptions are the same for both periods.

*Claims development table*

The following tables show the estimates of cumulative incurred claims, including both claims notified and IBNR for each successive underwriting year at each reporting date, together with cumulative payments to date. The cumulative claims estimates and cumulative payments are translated to sterling at the rate of exchange that applied at 31 December 2016.

The syndicate has taken advantage of the transitional rules of FRS 103 that permit only five years of information to be disclosed upon adoption. The claims development information disclosed is being increased from five years to ten years over the period 2016 to 2020.

In setting claims provisions the syndicate gives consideration to the probability and magnitude of future adverse experience. Due to the uncertainty inherent in the estimation process, the actual overall claim provision may not always be in surplus.

**21. Risk management** *continued*

*Gross insurance contract outstanding claims provision as at 31 December 2016:*

| *Underwriting year* | *Before 2011* | *2011* | *2012* | *2013* | *2014* | *2015* | *2016* | *Total* |
|---|---|---|---|---|---|---|---|---|
| | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* |
| Estimate of cumulative claims incurred | | | | | | | | |
| At end of underwriting year | | 65,032 | 99,728 | 61,696 | 49,155 | 66,044 | 71,050 | |
| 12 months later | | 186,419 | 160,684 | 121,738 | 109,669 | 142,185 | | |
| 24 months later | | 197,018 | 162,660 | 123,980 | 109,828 | | | |
| 36 months later | | 208,500 | 160,513 | 119,940 | | | | |
| 48 months later | | 210,461 | 156,305 | | | | | |
| 60 months later | | 209,147 | | | | | | |
| Current estimate of cumulative claims incurred | | 209,147 | 156,305 | 119,940 | 109,828 | 142,185 | 71,050 | |
| Cumulative payments to date | | 190,030 | 141,042 | 93,571 | 74,412 | 66,631 | 10,381 | |
| Gross outstanding claims provision at 31 December 2016 per the statement of financial position | 32,001 | 19,117 | 15,263 | 26,369 | 35,416 | 75,554 | 60,669 | 264,389 |

# Notes to the Accounts

*continued*

**21. Risk management** *continued*

*Net insurance contract outstanding claims provision as at 31 December 2016:*

| *Underwriting year* | *Before 2011* | *2011* | *2012* | *2013* | *2014* | *2015* | *2016* | *Total* |
|---|---|---|---|---|---|---|---|---|
| | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* |
| Estimate of cumulative claims incurred | | | | | | | | |
| At end of underwriting year | | 58,469 | 62,736 | 56,828 | 45,534 | 50,144 | 58,517 | |
| 12 months later | | 137,395 | 123,923 | 114,028 | 101,311 | 118,801 | | |
| 24 months later | | 140,687 | 124,328 | 115,516 | 102,257 | | | |
| 36 months later | | 142,562 | 122,291 | 111,747 | | | | |
| 48 months later | | 144,145 | 119,191 | | | | | |
| 60 months later | | 141,911 | | | | | | |
| Current estimate of cumulative claims incurred | | 141,911 | 119,191 | 111,747 | 102,257 | 118,801 | 58,517 | |
| Cumulative payments to date | | 134,384 | 106,252 | 88,167 | 70,924 | 55,124 | 10,225 | |
| Net outstanding claims provision at 31 December 2016 per the statement of financial position | 19,570 | 7,527 | 12,939 | 23,580 | 31,333 | 63,677 | 48,292 | 206,918 |

The estimate of cumulative claims incurred on an underwriting year will increase whilst premium continues to be earned. This will naturally give rise to an increase in incurred claims in the period up to 24 months beyond the underwriting year.

**21. Risk management** *continued*

**(d) Financial risk**

*(1) Credit risk*

Credit risk is the risk that one party to a financial instrument will cause a financial loss to the other party by failing to discharge an obligation.

The following policies and procedures are in place to mitigate the exposure to credit risk:

- A credit risk policy setting out the assessment and determination of what constitutes credit risk for the syndicate. Compliance with the policy is monitored and exposures and breaches are reported to the risk framework and compliance committee. The policy is regularly reviewed for pertinence and for changes in the risk environment.

- Net exposure limits are set for each investment counterparty or syndicate of counterparties, with minimum credit quality requirements at a portfolio level.

- Reinsurance is placed with counterparties that have a good credit rating and concentration of risk is avoided by following policy guidelines in respect of counterparties' limits that are set by the finance and investment committee and are subject to regular reviews. At each reporting date management performs an assessment of creditworthiness of reinsurers, ascertaining a suitable allowance for impairment.

- Guidelines determine when to obtain collateral and guarantees.

- The syndicate sets the maximum amounts and limits that may be advanced to corporate counterparties by reference to their long term credit ratings.

- The credit risk in respect of customer balances, incurred on non-payment of premiums or contributions, will only persist during the grace period specified in the policy document or trust deed until expiry, when the policy is either paid up or terminated. Commission paid to intermediaries is netted off against amounts receivable from them to reduce the risk of doubtful debts.

The tables below show the maximum exposure to credit risk (including an analysis of financial assets exposed to credit risk) for the components of the statement of financial position. The maximum exposure is shown gross, before the effect of mitigation through collateral agreements and the use of credit derivatives.

**21. Risk management** *continued*

| *31 December 2016* | *Neither past due nor impaired £'000* | *Past due £'000* | *Impaired £'000* | *Total £'000* |
|---|---|---|---|---|
| Financial investments | | | | |
| – Debt securities and other fixed income securities | 140,187 | – | – | 140,187 |
| – Shares and other variable yield securities and units in unit trusts | 89,452 | – | – | 89,452 |
| – Loans secured by mortgages | 4,282 | – | – | 4,282 |
| – Derivative assets | – | – | – | – |
| – Deposits with credit institutions | 1,854 | – | – | 1,854 |
| Deposits with ceding undertakings | 17 | – | – | 17 |
| Reinsurers' share of claims outstanding | 57,471 | – | – | 57,471 |
| Debtors arising out of insurance operations | 81,663 | 10,415 | – | 92,078 |
| Other debtors | 944 | – | – | 944 |
| Cash at bank and in hand | 11,367 | – | – | 11,367 |
| Overseas deposits | 15,082 | – | – | 15,082 |
| | 402,319 | 10,415 | – | 412,734 |

**21. Risk management** *continued*

| *31 December 2015* | *Neither past due nor impaired £'000* | *Past due £'000* | *Impaired £'000* | *Total £'000* |
|---|---|---|---|---|
| Financial investments | | | | |
| – Debt securities and other fixed income securities | 135,211 | – | – | 135,211 |
| – Shares and other variable yield securities and units in unit trusts | 73,214 | – | 2 | 73,216 |
| – Loans secured by mortgages | 6,188 | – | – | 6,188 |
| – Derivative assets | – | – | – | – |
| – Deposits with credit institutions | 438 | – | – | 438 |
| Deposits with ceding undertakings | 83 | – | – | 83 |
| Reinsurers' share of claims outstanding | 46,311 | – | – | 46,311 |
| Debtors arising out of insurance operations | 54,516 | 7,339 | – | 61,855 |
| Other debtors | 1,258 | – | – | 1,258 |
| Cash at bank and in hand | 2,241 | – | – | 2,241 |
| Overseas deposits | 13,686 | – | – | 13,686 |
| | 333,146 | 7,339 | 2 | 340,487 |

Assets which are past due but not impaired have principally been in arrears for less than 3 months from the reporting date.

**21. Risk management** *continued*

The table below provides information regarding the credit risk exposure of the syndicate at 31 December 2016 by classifying assets according to Standard & Poor's credit ratings of the counterparties. AAA is the highest possible rating. Assets that fall outside the range of AAA to BBB are classified as speculative grade and have not been rated. Insurance and other debtors have been excluded from the table as these are generally not rated.

| | *AAA* | *AA* | *A* | *BBB* | *<BBB* | *Not rated* | *Total* |
|---|---|---|---|---|---|---|---|
| *31 December 2016* | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* | *£'000* |
| Shares and other variable yield securities and units in unit trusts | 31,831 | 10,450 | – | – | – | 47,171 | 89,452 |
| Debt securities and other fixed income securities | 80,143 | 26,738 | 28,501 | 4,805 | – | – | 140,187 |
| Loans secured by mortgages | 4,282 | – | – | – | – | – | 4,282 |
| Deposits with credit institutions | – | – | 1,854 | – | – | – | 1,854 |
| Overseas deposits | 9,109 | 2,327 | 1,904 | 849 | – | 893 | 15,082 |
| Deposits with ceding undertakings | – | – | – | – | – | 17 | 17 |
| Reinsurers' share of claims outstanding | – | 5,576 | 50,029 | – | – | 1,866 | 57,471 |
| Cash at bank and in hand | – | – | 11,367 | – | – | – | 11,367 |
| Total credit risk | 125,365 | 45,091 | 93,655 | 5,654 | – | 49,947 | 319,712 |

**21. Risk management** *continued*

| *31 December 2015* | *AAA* £'000 | *AA* £'000 | *A* £'000 | *BBB* £'000 | *<BBB* £'000 | *Not rated* £'000 | *Total* £'000 |
|---|---|---|---|---|---|---|---|
| Shares and other variable yield securities and units in unit trusts | 32,624 | – | – | – | – | 40,592 | 73,216 |
| Debt securities and other fixed income securities | 72,067 | 35,641 | 20,754 | 6,749 | – | – | 135,211 |
| Loans secured by mortgages | 5,553 | – | 635 | – | – | – | 6,188 |
| Deposits with credit institutions | – | – | 438 | – | – | – | 438 |
| Overseas deposits | 8,106 | 2,301 | 1,668 | 1,524 | 45 | 42 | 13,686 |
| Deposits with ceding undertakings | – | – | – | – | – | 83 | 83 |
| Reinsurers' share of claims outstanding | – | 5,945 | 38,135 | – | – | 2,231 | 46,311 |
| Cash at bank and in hand | – | – | 2,241 | – | – | – | 2,241 |
| Total credit risk | 118,350 | 43,887 | 63,871 | 8,273 | 45 | 42,948 | 277,374 |

*Maximum credit exposure*

It is the syndicate's policy to maintain accurate credit ratings across its portfolio of investments and reinsurance counterparties.

Credit ratings are provided regularly by the syndicate's investment managers and are subject to regular review to ensure any counterparty risk is in line with the syndicate's risk appetite and complies with the specified investment guidelines. The management of the syndicate's investments is largely outsourced to professional investment managers who are given clearly defined credit, concentration and asset parameters within which they can operate. Specific provisions are included within the investment guidelines around notification of any credit breaches which would result in action being taken to rectify the position, subject to materiality.

**21. Risk management** *continued*

*(2) Liquidity risk*

Liquidity risk is the risk that the syndicate will encounter difficulty in meeting obligations associated with financial instruments. In respect of catastrophic events there is also a liquidity risk associated with the timing differences between gross cash out flows and expected reinsurance recoveries.

The following policies and procedures are in place to mitigate the syndicate's exposure to liquidity risk:

- A liquidity risk policy exists that sets out the assessment and determination of what constitutes liquidity risk. Compliance with the policy is monitored and exposures and breaches are reported to the risk framework and compliance committee. The policy is regularly reviewed for pertinence and for changes in the risk environment.
- Guidelines on asset allocation, portfolio limit structures and maturity profiles of assets are set, in order to ensure that sufficient funding is available to meet insurance and investment contracts obligations.

*Maturity profiles*

The table below summarises the maturity profile of the syndicate's financial liabilities based on remaining undiscounted contractual obligations, including interest payable, and gross outstanding claim liabilities based on the estimated timing of claim payments resulting from recognised insurance liabilities. Repayments which are subject to notice are treated as if notice were to be given immediately.

| | *0–1 year £'000* | *1–3 years £'000* | *3–5 years £'000* | *Over 5 years £'000* | *Total £'000* |
|---|---|---|---|---|---|
| **31 December 2016** | | | | | |
| Outstanding claim liabilities | 111,466 | 96,106 | 33,807 | 23,010 | 264,389 |
| Other | 40,007 | 755 | – | – | 40,762 |

| | *0–1 year £'000* | *1–3 years £'000* | *3–5 years £'000* | *Over 5 years £'000* | *Total £'000* |
|---|---|---|---|---|---|
| **31 December 2015** | | | | | |
| Outstanding claim liabilities | 97,827 | 79,580 | 23,679 | 14,460 | 215,546 |
| Other | 24,016 | 4,062 | – | – | 28,078 |

The profile periods used as at 31 December 2015 have been adjusted to align them with those used as at 31 December 2016. The above outstanding claims liability figures are shown gross; this is a change from last year, when they were shown net, and the comparatives have been restated accordingly.

**21. Risk management** *continued*

*(3) Financial market risk*

Financial market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Financial market risk comprises three types of risk:

a. Currency risk;

b. Interest rate risk; and

c. Equity price risk.

The following policies and procedures are in place to mitigate the exposure to financial market risk:

- A financial market risk policy exists that sets out the assessment and determination of what constitutes financial market risk for the syndicate. Compliance with the policy is monitored and exposures and breaches are reported to the risk framework and compliance committee. The policy is reviewed regularly for pertinence and for changes in the risk environment.
- Strict control over derivative instruments (e.g. equity derivatives are only permitted to be held to facilitate portfolio management or to reduce investment risk).
- For assets backing outstanding claims provisions, financial market risk is managed by ensuring the duration and profile of assets are aligned to the technical provisions they are backing. This helps manage financial market risk to the extent that changes in the values of assets are matched by a corresponding movement in the values of the technical provisions.

*(a) Currency risk*

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The syndicate's functional currency is sterling and its exposure to foreign exchange risk arises primarily with respect to transactions in euros, US dollars and Canadian dollars. The syndicate seeks to mitigate the risk by regularly seeking to match the estimated foreign currency denominated liabilities with assets denominated in the same currency.

**21. Risk management** *continued*

The table below summarises the exposure of the financial assets and liabilities by settlement currency to foreign exchange risk at the reporting date, as follows:

| *Converted £'000* | *UK £* | *US $* | *CAD $* | *EUR €* | *OTH* | *Total* |
|---|---|---|---|---|---|---|
| **As at 31 December 2016** | | | | | | |
| Total assets | 58,279 | 358,650 | 20,948 | 18,887 | 17,777 | 474,541 |
| Total liabilities | (60,076) | (353,376) | (14,208) | (17,330) | (11,252) | (456,242) |
| **Net assets** | (1,797) | 5,274 | 6,740 | 1,557 | 6,525 | 18,299 |

| *Converted £'000* | *UK £* | *US $* | *CAD $* | *EUR €* | *OTH* | *Total* |
|---|---|---|---|---|---|---|
| **As at 31 December 2015** | | | | | | |
| Total assets | 58,176 | 293,140 | 13,360 | 12,481 | 8,553 | 385,710 |
| Total liabilities | (48,247) | (289,231) | (9,330) | (11,785) | (338) | (358,931) |
| **Net assets** | 9,929 | 3,909 | 4,030 | 696 | 8,215 | 26,779 |

The non-sterling denominated net assets of the syndicate may lead to a reported loss (depending on the mix relative to the liabilities), should sterling strengthen against these currencies. Conversely, reported gains may arise should sterling weaken.

In part, foreign currency forward contracts may be used to achieve the desired exposure to each currency. From time to time the syndicate may also choose to utilise options on foreign currency derivatives to mitigate the risk of reported losses due to changes in foreign exchange rates. The degree to which options are used is dependent on the prevailing cost versus the perceived benefit to members' value from reducing the chance of a reported loss due to changes in foreign currency exchange rates. The details of all foreign currency derivatives contracts entered into are given in note 9.

**21. Risk management** *continued*

*Sensitivity to changes in foreign exchange rates*

The table below gives an indication of the impact on profit of a percentage change in the relative strength of sterling against the value of the US dollar, Canadian dollar and euro simultaneously. The analysis is based on the information as at 31 December 2016.

**Impact on profit**

| | *2016* | *2015* |
|---|---|---|
| | *£'000* | *£'000* |
| **Sterling weakens** | | |
| 10% against other currencies | 1,508 | 959 |
| 20% against other currencies | 3,392 | 2,159 |
| **Sterling strengthens** | | |
| 10% against other currencies | (1,234) | (785) |
| 20% against other currencies | (2,262) | (1,439) |

*(b) Interest rate risk*

Interest rate risk is the risk that the value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Floating rate instruments expose the syndicate to cash flow interest risk, whereas fixed rate instruments expose the syndicate to fair value interest risk.

The syndicate has no significant concentration of interest rate risk.

Insurance liabilities are not discounted and therefore not exposed to interest rate risk.

The analysis below is performed for reasonably possible movements in interest rates with all other variables held constant, showing the impact on profit of the effects of changes in interest rates on financial assets and liabilities for items recorded at fair value through profit and loss.

**21. Risk management** *continued*

The correlation of variables will have a significant effect in determining the ultimate impact on interest rate risk, but to demonstrate the impact due to changes in variables, the variables were altered on an individual basis. It should be noted that movements in these variables are non-linear.

| *Changes in variables* | *Impact on profit £'000* |
|---|---|
| **31 December 2016** | |
| +50 basis points | (1,012) |
| -50 basis points | 571 |
| **31 December 2015** | |
| +50 basis points | (1,159) |
| -50 basis points | 392 |

The method used for deriving sensitivity information and the significant variables are the same for both periods.

*(c) Equity price risk*

Equity price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

The syndicate's equity price risk exposure relates to financial assets and financial liabilities whose values will fluctuate as a result of changes in market prices, principally investment securities.

The financial market risk policy requires it to manage such risks by setting and monitoring objectives and constraints on investments, diversification plans, limits on investments in each sector and market, and careful and planned use of derivative financial instruments.

There is no significant concentration of equity price risk.

**21. Risk management** *continued*

The analysis below is performed for reasonably possible movements in market indices on financial instruments, with all other variables held constant, showing the impact on profit due to changes in fair value of financial assets and liabilities whose fair values are recorded in the profit and loss account. The correlation of variables will have a significant effect in determining the ultimate impact on equity price risk, but to demonstrate the impact due to changes in variables, the variables were altered on an individual basis. It should be noted that movements in these variables are non-linear.

| | *Change in variables £'000* | 31 December 2016 *Impact on profit £'000* | 31 December 2015 *Impact on profit £'000* |
|---|---|---|---|
| **Changes in variables – market indices** | | | |
| S&P 500/FTSE 100 | +5% | 3 | (24) |
| S&P 500/FTSE 100 | –5% | (3) | 24 |

The method used for deriving sensitivity information and the significant variables are the same for both periods.

SYNDICATE

# 2121

## UNDERWRITING YEAR ACCOUNTS

AS AT 31 DECEMBER 2016

2014 YEAR OF ACCOUNT

CLOSED

## Statement of Managing Agent's Responsibilities

The 2008 Regulations require the managing agent to prepare syndicate underwriting year accounts at 31 December in respect of any underwriting year which is being closed by reinsurance to close which give a true and fair view of the result of the underwriting year at closure. Detailed requirements in respect of the underwriting year accounts are set out in the Lloyd's Syndicate Accounting Byelaw (No. 8 of 2005).

In preparing the syndicate underwriting year accounts, the managing agent is required to:

- select suitable accounting policies, which are applied consistently and where there are items which affect more than one year of account, ensure a treatment which is equitable as between the members of the syndicate affected. In particular, the amount charged by way of premium in respect of the reinsurance to close shall, where the reinsuring members and reinsured members are members of the same syndicate for different years of account, be equitable as between them, having regard to the nature and amount of the liabilities reinsured;
- take into account all income and charges relating to a closed year of account without regard to the date of receipt or payment;
- make judgments and estimates that are reasonable and prudent; and
- state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the underwriting year accounts.

The managing agent is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the syndicate and enable it to ensure that the syndicate underwriting year accounts comply with the 2008 Regulations and the Lloyd's Syndicate Accounting Byelaw (No 8 of 2005). It is also responsible for safeguarding the assets of the syndicate and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

# Independent Auditor's Report to the Members of Syndicate 2121 – 2014 closed year of account

We have audited the syndicate underwriting year accounts for the 2014 year of account of Syndicate 2121 ('the syndicate') for the three years ended 31 December 2016 which comprise the Income Statement, the Statement of Changes in Members' Balances, the Statement of Financial Position, the Statement of Cash Flows, the related notes 1 to 16 and the Statement of Managing Agent's Responsibilities. The financial reporting framework that has been applied in their preparation is applicable law, the Lloyd's Syndicate Accounting Byelaw (No. 8 of 2005) and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' and Financial Reporting Standard 103 'Insurance Contracts'.

This report is made solely to the syndicate's members, as a body, in accordance with the Lloyd's Syndicate Accounting Byelaw (No. 8 of 2005) and the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008. Our audit work has been undertaken so that we might state to the syndicate's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the syndicate's members as a body, for our audit work, for this report, or for the opinions we have formed.

**Respective responsibilities of the managing agent and the auditor**

As explained more fully in the Statement of Managing Agent's Responsibilities set out on page 67, the managing agent is responsible for the preparation of the syndicate underwriting year accounts, under the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 and in accordance with the Lloyd's Syndicate Accounting Byelaw (No. 8 of 2005), which give a true and fair view. Our responsibility is to audit and express an opinion on the syndicate underwriting year accounts in accordance with applicable legal and regulatory requirements and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

**Scope of the audit of the syndicate underwriting year accounts**

An audit involves obtaining evidence about the amounts and disclosures in the syndicate underwriting year accounts sufficient to give reasonable assurance that the syndicate underwriting year accounts are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the syndicate's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the managing agent; and the overall presentation of the syndicate underwriting year accounts. In addition, we read all the financial and non-financial information in the Report and Underwriting Year Accounts to identify material inconsistencies with the audited syndicate underwriting year accounts and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

**Opinion on syndicate underwriting year accounts**

In our opinion the syndicate underwriting year accounts:

- give a true and fair view of the profit for the 2014 closed year of account;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 102 'The Financial Reporting Standard applicable in the UK and Republic of Ireland' and Financial Reporting Standard 103 'Insurance Contracts'; and
- have been prepared in accordance with the requirements of the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 and have been properly prepared in accordance with the Lloyd's Syndicate Accounting Byelaw (No. 8 of 2005).

**Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Lloyd's Syndicate Accounting Byelaw (No. 8 of 2005) requires us to report to you if, in our opinion:

- the managing agent in respect of the syndicate has not kept proper accounting records; or
- the syndicate underwriting year accounts are not in agreement with the accounting records.

Michael Purrington (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London

20 March 2017

# Income Statement for the 2014 year of account

*closed at the end of the third year at 31 December 2016*

**Technical account – general business**

| | Notes | *£'000* | *Cumulative balance at 31 December 2016 £'000* |
|---|---|---|---|
| Syndicate allocated capacity | | | 240,000 |
| **Earned premiums, net of reinsurance** | | | |
| Gross premiums written | 2 | | 221,747 |
| Outward reinsurance premiums | | | (39,552) |
| | | | 182,195 |
| Reinsurance to close premiums received, net of reinsurance | | | 93,567 |
| | | | 275,762 |
| Allocated investment return transferred from the non-technical account | 8 | | 1,648 |
| **Claims incurred, net of reinsurance** | | | |
| Gross claims paid | | (85,857) | |
| Reinsurers' share | | 5,820 | |
| | | (80,037) | |
| Reinsurance to close premiums payable, net of reinsurance | 4 | (93,467) | |
| | | | (173,504) |
| Net operating expenses | 5 | | (84,059) |
| Balance on the technical account for general business | | | 19,847 |

**Non-technical account**

| | Notes | *Cumulative balance at 31 December 2016 £'000* |
|---|---|---|
| Balance on the general business technical account | | 19,847 |
| Investment income | 8 | 2,004 |
| Net unrealised losses on investments | 8 | (272) |
| Investment expenses and charges | 8 | (84) |
| Allocated investment return transferred to the general business technical account | | (1,648) |
| Exchange gains | | 14,736 |
| Result for the closed year of account | | 34,583 |

There are no recognised gains or losses in the accounting period other than those dealt with in the technical and non-technical accounts. Accordingly a separate statement of comprehensive income has not been presented.

## Statement of Changes in Members' Balances

*for the 36 months ended 31 December 2016*

| | *2014 year of account £'000* |
|---|---|
| At 1 January 2014 | – |
| Profit | 34,583 |
| Members' agents' fees | (1,152) |
| Payment of profit to members' personal reserve funds | (8,400) |
| At 31 December 2016 | 25,031 |

## Statement of Financial Position

*as at 31 December 2016*

| | Notes | 2016 £'000 | £'000 |
|---|---|---|---|
| **ASSETS** | | | |
| Investments | 9 | | 102,269 |
| Deposits with ceding undertakings | | | 16 |
| **Debtors** | | | |
| Debtors arising out of direct insurance operations | 10 | 3,824 | |
| Debtors arising out of reinsurance operations | 11 | 6,195 | |
| Other debtors | | 14,374 | |
| | | | 24,393 |
| Reinsurance recoveries anticipated on gross reinsurance to close premiums payable to close the year of account | | | 33,219 |
| **Cash and other assets** | | | |
| Cash at bank and in hand | | 4,247 | |
| Other assets | 12 | 8,974 | |
| | | | 13,221 |
| Prepayments and accrued income | | | 26 |
| **TOTAL ASSETS** | | | 173,144 |
| **LIABILITIES** | | | |
| Amounts due to members | | | 25,031 |
| Reinsurance to close premiums payable to close the year of account – gross amount | | | 128,167 |
| **Creditors** | | | |
| Creditors arising out of direct insurance operations | | 4,935 | |
| Creditors arising out of reinsurance operations | | 6,189 | |
| Other creditors | | 7,460 | |
| | | | 18,584 |
| Accruals and deferred income | | | 1,362 |
| **TOTAL LIABILITIES** | | | 173,144 |

The syndicate underwriting year accounts on pages 70 to 97 were approved by the Board of Argenta Syndicate Management Limited on 20 March 2017 and were signed on its behalf by

**Andrew J Annandale**
*Managing Director*

## Statement of Cash Flows

*for the 36 months ended 31 December 2016*

| | Notes | *2016* *£'000* |
|---|---|---|
| **Profit on ordinary activities** | | 34,583 |
| Increase in outstanding claims | | 128,167 |
| Increase in reinsurers' share of outstanding claims | | (33,219) |
| Increase in debtors | | (24,419) |
| Increase in creditors | | 19,946 |
| Investment return | | (1,784) |
| Movement in other assets/liabilities | | – |
| **Net cash inflow from operating activities** | | 123,274 |
| **Investing activities** | | |
| Investment income received | | 2,139 |
| Purchase of debt and equity instruments | | (177,529) |
| Sale of debt and equity instruments | | 113,593 |
| Purchase of derivatives | | (618) |
| Sale of derivatives | | 618 |
| Increase in overseas deposits | | (8,364) |
| Increase in deposits with ceding undertakings | | (16) |
| **Net cash outflow from investing activities** | | (70,177) |
| **Financing activities** | | |
| Payment of profit to members' personal reserve funds | | (8,400) |
| Members' agents' fee advances | | (1,152) |
| **Net cash outflow from financing activities** | | (9,552) |
| Increase in cash and cash equivalents | | 43,545 |
| Cash and cash equivalents at 1 January | | – |
| **Cash and cash equivalents at 31 December** | 13 | 43,545 |

# Notes to the Accounts

**1. Accounting policies**

*1.1 Statement of compliance*

The syndicate underwriting year accounts have been prepared under the 2008 Regulations and in accordance with the Syndicate Accounting Byelaw (No.8 of 2005) and applicable accounting standards in the United Kingdom. FRS102 and FRS 103 have been applied to the extent that they are relevant for a proper understanding of the underwriting year accounts.

The 2014 year of account has closed and all assets and liabilities have been transferred to a reinsuring year of account. The result for the year of account was declared in both sterling and US dollars and translated at the rate of exchange ruling at the balance sheet date. The payment of the closed year profit will be made in the currencies in which it is declared with the exchange risk in respect of this transferring to the capital providers to the syndicate with effect from 31 December 2016. To this extent, the risks that it is exposed to in respect of the reported financial position and financial performance are significantly less than the syndicate annual accounts. Accordingly, these underwriting year accounts do not have associated risk disclosures as required by section 34 of FRS 102 and section 4 of FRS 103. Full disclosures relating to these risks are provided in the syndicate annual accounts. In addition certain other disclosure requirements under FRS 102 and FRS 103, which include reconciliations of changes in insurance liabilities, reinsurance assets and deferred acquisition costs, have not been provided as the directors believe they are not required for a proper understanding of the underwriting year accounts.

*1.2 Basis of preparation*

Members participate on a syndicate by reference to a year of account and each syndicate year of account is a separate annual venture. These accounts relate to the 2014 year of account which has been closed by reinsurance to close at 31 December 2016; consequently the statement of financial position represents the assets and liabilities of the 2014 year of account and the income statement and statement of cash flows reflect the transactions for that year of account during the 36 month period until closure.

The financial statements for the period ended 31 December 2016 were approved for issue by the board of directors on 20 March 2017.

The financial statements are prepared in sterling which is the functional and presentational currency of the syndicate and rounded to the nearest £'000.

As permitted by FRS 103 the syndicate continues to apply the existing accounting policies that were applied prior to this standard for its insurance contracts.

The syndicate has elected to apply early the March 2016 amendments to FRS 102, *Fair value hierarchy disclosures*. As a result the fair value hierarchy disclosures shown in note 9 are prepared on a basis consistent with the measurement of the financial instruments.

As each syndicate year of account is a separate annual venture, there are no comparative figures.

*1.3 Judgements and key sources of estimation uncertainty*

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the amounts reported for assets and liabilities as at the statement of financial position date and the amounts reported for revenues and expenses during the period. However, the nature of estimation means that actual outcomes could differ from those estimates. The following are the syndicate's key sources of estimation uncertainty:

**1. Accounting policies** *continued*

*Insurance contract technical provisions*

For insurance contracts, estimates have to be made both for the expected ultimate cost of claims reported at the reporting date and for the expected ultimate cost of claims IBNR at the reporting date. It can take a significant period of time before the ultimate claims cost can be established with certainty and, for some types of policies, IBNR claims form the majority of the liability in the statement of financial position.

The ultimate cost of outstanding claims is estimated by using a range of standard actuarial claims projection techniques, such as Chain Ladder and Bornhuetter-Ferguson methods.

The main assumption underlying these techniques is that past claims development experience can be used to project future claims development and hence ultimate claims costs. The provision for claims outstanding is based on the estimated ultimate cost of all claims notified but not settled by the statement of financial position date assessed on an individual case basis, together with the provision for related claims handling costs. The provision also includes the estimated cost of claims IBNR at the statement of financial position date based on statistical methods.

These methods generally involve projecting from past experience the development of claims over time to form a view of the likely ultimate claims to be experienced for more recent underwriting, having regard to variations in the business accepted and the underlying terms and conditions. For the most recent years, where a high degree of volatility arises from projections, estimates may be based in part on output from rating and other models of the business accepted and assessments of underwriting conditions. The amount of salvage and subrogation recoveries is separately identified and, where material, reported as an asset.

*Fair value of financial assets and derivatives determined using valuation techniques*

Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of discounted cash flow models and/or mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, judgement is required to establish fair values. The judgements include considerations of liquidity risk, credit risk, and model inputs such as estimated future cash flows based on management's best estimates and discount rates.

For discounted cash flow analysis, estimated future cash flows and discount rates are based on current market information and rates applicable to financial instruments with similar yields, credit quality and maturity characteristics. Estimated future cash flows are influenced by factors such as economic conditions (including country specific risks), concentrations in specific industries, types of instruments or currencies, market liquidity and financial conditions of counterparties. Discount rates are influenced by risk free interest rates and credit risk. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

Further details are given in the syndicate annual accounts in note 21.

*1.4 Significant accounting policies*

*Financial investments*

As permitted by FRS 102, the syndicate has elected to apply the recognition and measurement provisions of section 11 and 12 in full to account for all of its financial instruments.

Financial assets and financial liabilities are recognised when the syndicate becomes a party to the contractual provisions of the instrument.

**1. Accounting policies** *continued*

All financial assets and liabilities are initially measured at transaction price (including transaction costs), except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value (which is normally the transaction price excluding transaction costs), unless the arrangement constitutes a financing transaction. If an arrangement constitutes a financing transaction, the financial asset or financial liability is measured at the present value of the future payments discounted at a market rate of interest for a similar debt instrument.

Financial liabilities are derecognised only when the obligation specified in the contract is discharged, cancelled or expires.

*Derivative financial instruments*

The syndicate uses derivative financial instruments to reduce exposure to foreign exchange risk and interest rate movements. The syndicate does not hold or issue derivative financial instruments for speculative purposes. Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each reporting date. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit or loss depends on the nature of the hedge relationship.

*Cash and cash equivalents*

For the purpose of the statement of cash flows, cash and cash equivalents comprise cash at banks and in hand and short term deposits with an original maturity date of three months or less, net of outstanding bank overdrafts.

*Fair value of financial assets*

The syndicate uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

- Level 1: The unadjusted quoted price in an active market for identical assets or liabilities that the entity can access at the measurement date.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable (i.e. developed using market data) for the asset or liability, either directly or indirectly.
- Level 3: Inputs are unobservable (i.e. for which market data is unavailable) for the asset or liability.

See Note 9 for details of financial instruments classified by fair value hierarchy.

*Impairment of financial assets*

For financial assets not held at fair value through profit or loss, the syndicate assesses at each reporting date whether the financial asset or group of financial assets is impaired. The syndicate first assesses whether objective evidence of impairment exists for financial assets. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in the collective assessment of impairment.

**1. Accounting policies** *continued*

*Derecognition of financial assets*

A financial asset or, when applicable, a part of a financial asset is derecognised when:

- The rights to the cash flows from the asset have expired; or
- The syndicate retains the right to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass–through' arrangement and either (a) the syndicate has transferred substantially all the risks and rewards of the asset; or (b) the syndicate has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the syndicate has transferred its right to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards nor transferred control of the asset, the asset is recognised to the extent of the syndicate's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the syndicate could be required to repay. In that case, the syndicate also recognises an associated liability.

*Offsetting of financial instruments*

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if, and only if:

- There is a currently enforceable legal right to offset the recognised amounts; and
- There is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

*Financial liabilities*

The syndicate's financial liabilities include trade and other payables, borrowings, insurance payables and derivative financial instruments, where applicable. All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings, net of directly attributable transaction costs.

Trade and other payables and loans and borrowings are subsequently measured at amortised cost using the EIR method. Gains and losses are recognised in the income statement when the liabilities are derecognised as well as through the EIR method amortisation process. Amortised cost is calculated by taking into account any discount or premium on acquisition and fee or costs that are an integral part of the EIR. The EIR amortisation is included in investment return in the profit or loss. Derivative financial liabilities are subsequently measured at fair value through profit or loss. A financial liability is derecognised when the obligation under the liability is discharged or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of the existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective amounts is recognised in profit or loss.

**1. Accounting policies** *continued*

*Investment return*

Dividends are recognised when the investments to which they relate are declared 'ex-dividend'. Interest income is recognised on a time proportionate basis taking into account effective interest yield.

Unrealised and realised gains and losses on financial investments are recognised based on the appropriate classification of financial investments and are covered in detail under the accounting policy for financial investments.

An allocation of actual investment return on investments supporting the general insurance technical provisions and associated members' balance is made from the non-technical account to the technical account. Investment return related to non-insurance business and members' balance is attributed to the non-technical account. Investment return has been wholly allocated to the technical account as all investments relate to the technical account.

*Insurance contracts – product classification*

Insurance contracts are those contracts when the syndicate (the insurer/reinsurer) has accepted significant insurance risk from another party (the policyholder/reinsured) by agreeing to compensate the policyholder if a specified uncertain future event (the re/insured event) adversely affects the policyholders. As a general guideline, the syndicate determines whether it has significant insurance risk, by comparing benefits paid with benefits payable if the insured event did not occur. Insurance contracts can also transfer financial risk.

Once a contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly during this period, unless all rights and obligations are extinguished or expire.

Any separable embedded derivatives within an insurance contract are separated and accounted for in accordance with sections 11 and 12 of FRS 102 unless the embedded derivative is itself an insurance contract (i.e. the derivative is not separated if the policyholder benefits from the derivative only when the insured event occurs).

*Underwriting transactions*

The underwriting accounts for each year of account are normally kept open for three years before the result on that year is determined. At the end of the three year period, outstanding liabilities can normally be determined with sufficient accuracy to permit the year of account to be closed by payment of a reinsurance to close premium to the successor year of account.

*The reinsurance to close premium*

The reinsurance to close premium is determined by reference to the outstanding technical provisions (including those for outstanding claims, unearned premiums net of deferred acquisition costs, and unexpired risks) relating to the closed year and to all previous closed years reinsured therein. Although this estimate of net outstanding liabilities is considered to be fair and reasonable, it is implicit in the estimation procedure that the ultimate liabilities will be at variance from the premium so determined. The reinsurance to close premium transfers the liability in respect of all claims, reinsurance premiums, return premiums and other payments in respect of the closing year (and previous closed years reinsured within) to the members of the successor year of account and gives them the benefit of refunds, recoveries, premiums due and other income in respect of those years in so far as they have not been credited in these accounts.

**1. Accounting policies** *continued*

*Gross premiums*

Gross premiums are allocated to years of account on the basis of the inception date of the policy. Commission and brokerage are charged to the year of account to which the relevant policy is allocated. Policies written under binding authorities, lineslips or consortium arrangements are allocated to the year of account into which the arrangement incepts. Additional and return premiums follow the year of account of the original premium. Premiums are shown gross of brokerage payable and exclude taxes and duties levied on them. Estimates are made for pipeline premiums, representing amounts due but not yet notified to the syndicate year of account. Premium written are treated as fully earned. Outwards reinsurance premiums ceded are attributed to the same year as the original risk being protected.

*Gross claims*

Gross claims paid are allocated to the same year of account as that to which the corresponding premiums are allocated and include internal and external claims settlement expenses. Reinsurance recoveries are allocated to the year of account to which the claim was charged.

*Outstanding claims*

Outstanding claims comprise amounts set aside for claims notified and IBNR claims. Notified claims are estimated on a case by case basis with regard to the circumstances as reported, any information available from loss adjusters, and previous experience of the cost of settling claims with similar characteristics.

The amount included in respect of IBNR is based on statistical techniques of estimation applied by syndicate staff and reviewed by the auditor’s actuarial team. These techniques generally involve projecting from past experience of the development of claims over time to form a view of the likely ultimate claims to be experienced for more recent underwriting, having regard to variations in the business accepted and the underlying terms and conditions. For the most recent years where a high degree of volatility arises from projections, estimates may be based in part on output from rating and other models of the business accepted and assessments of underwriting conditions.

The provision for claims includes amounts in respect of internal and external claims handling costs. The reinsurers’ share of provisions for claims is based on calculated amounts of outstanding claims and projections for IBNR, net of estimated irrecoverable amounts, having regard to the reinsurance programme in place for the class of business, the claims experience for the period and the current security rating of the reinsurance companies involved.

The syndicate uses a number of statistical techniques to assist in making the above estimates.

*Reinsurance assets*

The syndicate cedes insurance risk in the normal course of business for all of its areas of operation. Reinsurance assets represent balances due from reinsurance companies. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision or settled claims associated with the reinsurer’s policies and are in accordance with the related reinsurance contract.

Reinsurance assets are reviewed for impairment at each reporting date, or more frequently, when an indication of impairment arises during the reporting year. Impairment occurs when there is objective evidence as a result of an event that occurred after initial recognition of the reinsurance asset that the syndicate may not receive all outstanding amounts due under the terms of the contract and the event has a reliably measurable impact on the amounts that the syndicate will receive from the reinsurer. The impairment loss is recorded in the income statement.

**1. Accounting policies** *continued*

Gains or losses on buying reinsurance are recognised in the income statement immediately at the date of purchase and are not amortised. There were no such gains recognised relating to the 2014 year of account.

Ceded reinsurance arrangements do not relieve the syndicate from its obligations to policyholders.

*Insurance receivables*

Insurance receivables are recognised when due and measured on initial recognition at the fair value of the consideration received or receivable. Subsequent to initial recognition, insurance receivables are measured at amortised cost, using the EIR method. The carrying value of insurance receivables is reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable, with the impairment loss recorded in the income statement.

Insurance receivables are derecognised when the derecognition criteria for financial assets have been met.

*Insurance payables*

Insurance payables are recognised when due and measured on initial recognition at the fair value of the consideration received less directly attributable transaction costs. Subsequent to initial recognition, they are measured at amortised cost using the EIR method. Insurance payables are derecognised when the obligation under the liability is settled, cancelled or expired.

*Foreign currencies*

The syndicate's functional currency and presentational currency is sterling. Transactions denominated in currencies other than the functional currency are initially recorded in the functional currency at the exchange rate ruling at the date of the transactions or at an approximate average rate.

Monetary assets and liabilities (which include all assets and liabilities arising from insurance contracts including unearned premiums and deferred acquisition costs) denominated in foreign currencies are retranslated into the functional currency at the exchange rate ruling on the reporting date.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction and are not subsequently restated. Non-monetary items denominated in a foreign currency, measured at fair value, are translated into the functional currency using the exchange rate ruling at the date when the fair value was determined.

Exchange differences are recorded in the non-technical account.

*Taxation*

Under Schedule 19 of the Finance Act 1993 managing agents are not required to deduct basic rate income tax from trading income. In addition, all UK basic rate income tax deducted from syndicate investment income is recoverable by managing agents and consequently the distribution made to members or their members' agents is gross of tax. Capital appreciation falls within trading income and is also distributed gross of tax.

No provision has been made for any United States Federal Income Tax payable on underwriting results or investment earnings. Any payments on account made by the syndicate are included in the statement of financial position under the heading 'other debtors'.

No provision has been made for any overseas tax payable by members on underwriting results.

**1. Accounting policies** *continued*

*Syndicate operating expenses*

Costs incurred by the managing agent in respect of the syndicate are charged to the syndicate and included within the relevant profit and loss account heading. Where expenses do not relate to any specific year of account they are apportioned between years of account on a basis which reflects the benefit obtained by each year of account from each type of expense. Where expenses are incurred jointly by the managing agent and the syndicate, they are apportioned generally based on time spent, estimated utilisation or head count. The franchise performance and risk management charge, to the extent that this is levied by Lloyd's, is considered to arise solely in respect of the day to day transaction of underwriting business at Lloyd's. This is therefore allocated to managed syndicates based on their written premium in that year. The managing agent operates a defined contribution pension scheme and its recharges to the syndicate in respect of salaries and related costs include an element for pension costs. These pension costs are expensed in full in the period to which the recharge relates.

Amounts recharged by the managing agent include costs arising from the use of assets in the period. These rental costs are expensed in full in the period to which the recharge relates.

*Profit commission*

Profit commission is charged by the managing agent for the 2014 year of account at a rate of 17.5% of profit subject to the operation of a deficit clause. Where profit commission is charged, it is included within members' standard personal expenses within administrative expenses. Profit commission does not become payable until after the appropriate year of account closes, normally at 36 months, although the managing agent may receive payments on account of anticipated profit commissions in line with interim profits released to members.

**2. Particulars of business written**

**2014 year of account after three years**

*Type of business*

An analysis of the technical account balance before investment return is set out below:

| | *Gross premiums written and earned £'000* | *Gross claims incurred £'000* | *Gross operating expenses* £'000* | *Reinsurance balance £'000* | *Total £'000* |
|---|---|---|---|---|---|
| **Direct insurance:** | | | | | |
| Marine, aviation and transport | 49,812 | (14,766) | (21,366) | (6,549) | 7,131 |
| Fire and other damage to property | 107,021 | (35,304) | (39,149) | (19,971) | 12,597 |
| Other | 4,883 | (2,312) | (2,058) | (447) | 66 |
| | 161,716 | (52,382) | (62,573) | (26,967) | 19,794 |
| Reinsurance accepted | 153,598 | (153,676) | (21,486) | 19,969 | (1,595) |
| | 315,314 | (206,058) | (84,059) | (6,998) | 18,199 |

Reinsurance acceptances include the reinsurance to close premium of £93,567,289 received from the 2013 year of account.

All premiums were concluded in the UK.

* Gross operating expenses are the same as net operating expenses shown in the profit and loss account, as no commissions in respect of outward reinsurance were received and set off in arriving at the net operating expenses.

*Geographical analysis by destination*

| | *Gross written premiums £'000* |
|---|---|
| UK | 68,904 |
| EU | 17,986 |
| Other | 228,424 |
| | 315,314 |

**3. Analysis of underwriting result**

| | *2013 and prior years of account £'000* | *2014 pure year of account £'000* | *Total 2014 year of account £'000* |
|---|---|---|---|
| Technical account balance before allocated investment return and net operating expenses | 12,311 | 89,947 | 102,258 |
| Acquisition costs | (269) | (66,087) | (66,356) |
| | 12,042 | 23,860 | 35,902 |

**4. Reinsurance to close premiums payable net of reinsurance**

| | *Reported* *£'000* | *IBNR* *£'000* | *Total* *£'000* |
|---|---|---|---|
| Gross outstandings | 67,480 | 52,721 | 120,201 |
| Reinsurance recoveries anticipated | (16,073) | (10,661) | (26,734) |
| | 51,407 | 42,060 | 93,467 |

All amounts are stated at the rate of exchange at the date of the transaction or an approximate average rate.

**5. Net operating expenses**

| | *2016* *£'000* |
|---|---|
| Acquisition costs | 66,356 |
| Administrative expenses | 17,703 |
| Net operating expenses | 84,059 |

Members' standard personal expenses amounting to £10.8 million are included in administrative expenses. Members' standard personal expenses include Lloyd's subscriptions, New Central Fund contributions, managing agent's fees and profit commission.

**6. Staff numbers and costs**

All staff are employed by the managing agency. The following amounts were recharged to the syndicate in respect of staff costs:

| | *2016* *£'000* |
|---|---|
| Wages and salaries | 7,226 |
| Social security costs | 988 |
| Other pension costs | 472 |
| | 8,686 |

The average number of employees working for the syndicate during the period was as follows:

| | *2016* *Number* |
|---|---|
| Underwriting | 20 |
| Underwriting support | 19 |
| Claims | 7 |
| Administration and finance | 19 |
| | 65 |

The aggregate remuneration charged to the syndicate in respect of emoluments paid to the directors of ASML and the active underwriter was £1.3 million. This includes £278,000 that relates to the active underwriter.

## 7. Auditor's remuneration

| | 2016 £'000 |
|---|---|
| Audit services | 169 |
| Other services pursuant to regulations and Lloyd's byelaws | 95 |
| | 264 |

## 8. Investment return

| | 2016 £'000 |
|---|---|
| Income from other investments | 2,325 |
| Net losses on realisation of investments | (321) |
| Total investment income | 2,004 |
| Net unrealised losses on investments | (272) |
| Investment expenses and charges | (84) |
| Total investment return | 1,648 |

## 9. Financial investments

| | Market value 2016 £'000 |
|---|---|
| Shares and other variable yield securities and units in unit trusts | |
| – designated at fair value through profit or loss | 38,324 |
| Debt securities and other fixed income securities | |
| – designated at fair value through profit or loss | 61,803 |
| Deposits with credit institutions held at fair value | 364 |
| Loans secured by mortgages | 1,778 |
| | 102,269 |

The shares and other variable yield securities and units in unit trusts relate to holdings in highly diversified collective investment schemes, which include an element of low volatility absolute return funds managed in accordance with the UCITS regulations.

There was no material change in fair value for financial instruments held at fair value attributable to own credit risk during the 36 month period.

There have been no day one profits recognised in respect of financial instruments designated at fair value through profit or loss.

By market value, approximately 65% of shares and other variable yield securities and units in unit trusts are listed on a recognised stock exchange.

**9. Financial investments** *continued*

The syndicate's investment managers are permitted to directly purchase derivative financial instruments (interest rate futures) to hedge its interest rate risks. These derivatives are classified as trading instruments.

There were no derivatives held at the period end.

The following table shows financial investments including overseas deposits recorded at fair value analysed between three levels in the fair value hierarchy.

| | *Level 1* | *Level 2* | *Level 3* | *Total* |
|---|---|---|---|---|
| | *£'000* | *£'000* | *£'000* | *£'000* |
| Shares and other variable yield securities and units in unit trusts | 16,538 | 21,786 | – | 38,324 |
| Debt securities and other fixed income securities | 32,269 | 29,534 | – | 61,803 |
| Loans and deposits with credit institutions | 364 | 1,778 | – | 2,142 |
| Overseas deposits | 2,156 | 6,818 | – | 8,974 |
| | 51,327 | 59,916 | – | 111,243 |

Included in the level 1 category are financial assets that are measured by reference to published quotes in an active market. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry syndicate, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Included in the level 2 category are financial assets measured using a valuation technique based on assumptions that are supported by prices from observable current market transactions. For example, assets for which pricing is obtained via pricing services but where prices have not been determined in an active market, financial assets with fair values based on broker quotes, investments in private equity funds with fair values obtained via fund managers and assets that are valued using the syndicate's own models whereby the significant inputs into the assumptions are market observable.

Included in the level 3 category are financial assets measured using a valuation technique (model) based on assumptions that are neither supported by prices from observable current market transactions in the same instrument nor are they based on available market data. Therefore, unobservable inputs reflect the syndicate's own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). These inputs are developed based on the best information available, which might include the syndicate's own data.

## 10. Debtors arising out of direct operations

| | 2016 £'000 |
|---|---|
| Amounts falling due within one year – intermediaries | 3,771 |
| Amounts falling due after one year – intermediaries | 53 |
| | 3,824 |

## 11. Debtors arising out of reinsurance operations

| | 2016 £'000 |
|---|---|
| Amounts falling due within one year | 6,195 |

## 12. Other assets

| | 2016 £'000 |
|---|---|
| Amounts advanced in Illinois, USA as a condition of carrying on business there | 969 |
| Amounts advanced in Australia and other countries as a condition of carrying on business there | 8,005 |
| | 8,974 |

## 13. Cash and cash equivalents

| | 2016 £'000 |
|---|---|
| Cash at bank and in hand | 4,247 |
| Short-term deposits with financial institutions | 39,298 |
| | 43,545 |

## 14. Off balance sheet items

The syndicate has not been party to an arrangement which is not reflected in its statement of financial position, where material risks or benefits arise for the syndicate.

**15. Related parties**

**Argenta Holdings plc**

ASML is a wholly owned subsidiary of AHP which owns 100% of the voting and economic rights of ASML. AHP is regarded by ASML as its ultimate parent and is also the parent undertaking of the smallest and largest group to consolidate the financial statements of ASML. Copies of the accounts for AHP can be obtained from Companies House.

AHP is controlled by Glenrinnes Farms Ltd, RBC cees Trustee Ltd as trustee of the Argenta Employee Benefit Trust and Wren Properties Ltd who own 44.75%, 25% and 25% of the economic and voting rights in the company respectively. Mr Alasdair Locke is a 99% controller of Glenrinnes Farms Ltd and up until 2014 owned this shareholding directly. Wren Properties Ltd is owned and controlled by members of the Robinson family.

AHP and its related parties provide certain underwriting, administrative, accounting, human resource, information technology and risk management and compliance services to ASML. These services are provided on a non-profit making basis by way of inter-group cross charges and direct salary charges.

Argenta Tax and Corporate Services Limited (ATCSL), an AHP group company, provides taxation services to the syndicate. Fees are agreed on a commercial basis and the profit ATCSL generates from providing these services is less than £1,000.

AUA, a subsidiary of AHP, is a service company approved by Lloyd's and the MAS to operate on the Lloyd's Asia platform. AUA also holds a licence granted by the Australian Securities and Investment Commission and has a branch office approved by Lloyd's in Sydney, Australia. Syndicate 2121 uses this service company as a coverholder to bind risks on its behalf. Such services relating to business written in Singapore are provided at cost plus a small profit margin of 5% mainly for tax purposes. The total value of the margin is less than £50,000. The commission retained by AUA for business underwritten by the Australian branch is 27.5% of gross premium, which is in line with other Australian facilities currently supported by the syndicate. This commission charged in Australia covers original acquisition costs, branch office expenses and processing costs. No commission was charged by the branch in relation to the 2014 year of account.

Other than by virtue of directorship fees, salaries and other related remuneration in respect of their employment by AHP or its related parties, and any potential future investment earnings or growth in capital value arising from their shareholding, none of the directors, officers, shareholders or related parties concerned, derive any personal benefit from the arrangements that exist.

**Business transactions**

Mr Mumford was a director of another Lloyd's managing agency, Neon Underwriting Ltd (formerly Marketform Managing Agency Ltd), until his resignation on 10 February 2017.

Mr Whiter is chairman of Lloyd's broker Ed Broking (London) Ltd (formerly CGNMB LLP) and a director of its parent company, Ed Broking Group Ltd (formerly Cooper Gay Swett & Crawford Ltd).

Mr Graham White, who was a director of ASML until his resignation on 31 March 2015, is a director of Lloyd's broker Marine Aviation & General (London) Ltd.

Mr Newbery was a director of Lloyd's broker Tyser & Co Ltd, a member of the board of underwriting agency Aquila Underwriting LLP, and a director of Hawkes Bay Holdings Ltd, the parent company of both entities, until his resignation from all of the companies on 31 October 2015. Mr Newbery became a non-executive director of Arthur J. Gallagher Holdings (UK) Limited, the holding company of a number of Lloyd's brokers, and the non-executive chairman of Pen Underwriting Limited, a managing general agent, on 11 November 2015 and 8 December 2015 respectively.

**15. Related parties** *continued*

The above entities may in the past have transacted business with syndicates managed by ASML and may do so in the future. Any such business, however, has been and will continue to be, conducted on an arm's length commercial basis with no involvement, either directly or indirectly, from the individuals above.

Other than directorship fees, salaries and other related remuneration, no personal benefit is derived by the individuals concerned from these arrangements.

Messrs Hunt and Mumford both benefit from fees paid in respect of independent review services that they carry out on sections of Syndicate 2121's book of business. It is a regulatory requirement that such reviews are performed by individuals who are separate from the day to day underwriting of the specific classes of business under review and have the necessary skill and experience to fulfil their independent review obligations.

Total fees and profit commission payable to ASML in respect of its role as managing agent for the 2014 year of account amounted to £1.8 million and £7.3 million respectively. Creditors at the period end include £7.3 million in respect of profit commission. In addition to this, creditors at the period end include £77,000 due to ASML in respect of expenses paid on behalf of the 2014 year of account.

Mr Annandale is a director of AUA; Mr Hunt was a director of AUA until his resignation on 31 January 2014; and Mr Maguire was appointed as a director of AUA on 3 June 2014. AUA receives a commission on business accepted under a binding authority granted to it by Syndicate 2121. The total commissions payable for the 2014 year of account were £0.9 million. Creditors at the period end include amounts due to AUA in respect of the 2014 year of account of £11,000.

AUA was also appointed during 2015 as a coverholder to bind risks from Australia. No such business was underwritten for the benefit of the 2014 year of account.

**Capital support for Syndicate 2121**

Mr Annandale is a director of Argenta Private Capital Limited (APCL), a subsidiary of AHP. Messrs Graham White and David Williams were directors of APCL until their resignations on 31 July 2015 and 29 July 2015 respectively, and were also directors of ASML until their resignations on 31 March 2015.

Mr Alan Tucker, who was a director of ASML until his resignation on 31 March 2015, is a director of Cantril Investments Ltd, Kemah Lime Street Capital Ltd, Kling Investment Ltd, Nidarich Ltd and Rechter Underwriting Ltd, all corporate members. Mr Tucker was also a director of Celeiros Ltd until his resignation on 19 December 2014.

APCL allocates capacity to Syndicate 2121 for the 2014 to 2017 years of account. Cantril Investments Ltd, Celerios Ltd, Rechter Underwriting Ltd, Kling Investment Ltd, and Kemah Lime Street Capital Ltd all allocate capacity to Syndicate 2121 for the 2014 to 2017 years of account. Hampden Agencies Ltd became the member's agent for Celerios Ltd from 19 December 2014.

Nidarich Ltd allocates capacity to Syndicate 2121 for the 2014 and 2015 years of account.

Mr Tucker is also a director of Fifteen B Limited, which is a member of Alizadeh Underwriting LLP that allocates capacity to Syndicate 2121 for the 2014 to 2017 years of account, and also a director of Inswin Ltd, which is a member of Winins LLP that allocates capacity to Syndicate 2121 for the 2017 year of account only.

**15. Related parties** *continued*

Mr Annandale is or was a director of the following corporate members:

Argenta Underwriting No. 2 Limited (AU2)
Argenta Underwriting No. 3 Limited (AU3)
Argenta Underwriting No. 8 Limited (AU8)
Argenta Underwriting No. 9 Limited (AU9)
Argenta Underwriting No. 10 Limited (AU10)
Argenta Underwriting No. 11 Limited (AU11)
Argenta Underwriting No. 12 Limited (AU12) (resigned 15 December 2016)
Ransome's Underwriting Ltd (resigned 3 April 2014)

AU12 was sold to a third party in December 2016. The other Argenta underwriting corporate members above remain subsidiaries of AHP. In relation to Syndicate 2121, all of these corporate members participate on the 2014 year of account.

Other than directorship fees, salaries and other related remuneration and any potential future investment earnings or growth in capital value arising from shareholdings in the Lloyd's corporate members, no personal benefit is derived by the individuals concerned from these arrangements.

Mr Alasdair Locke is a director of and, via his company Glenrinnes Farms Ltd, a shareholder in AHP. Glenrinnes Farms Ltd provides capital to AU2, AU3 and AU9 for the 2014 to 2017 years of account on an excess basis through Funds at Lloyd's Provider's Agreements. Glenrinnes Farms Ltd also participates on AU3 on a pro-rata basis for each of the 2014 and 2015 years of account. Each corporate member in turn provides capital to Syndicate 2121 for each of the 2014 to 2017 years of account. Mr Locke derives no personal benefit from these arrangements other than a fee or a proportionate share of the underwriting result of the corporate members to which he is contractually entitled through his Glenrinnes Farms Ltd participation.

As part of the consideration for the provision of all such capital by Glenrinnes Farms Ltd, it was granted an option by AHP and its shareholders to acquire £98.5 million of Syndicate 2121 capacity. The option was closed out during 2015 following a payment to compensate for this.

All capital providers who underwrite on Syndicate 2121 are charged managing agency fees and profit commission on a standard basis, apart from one where the charges are less advantageous, as disclosed in the Register of Underwriting Agency Charges.

There are no other transactions or arrangements to be disclosed.

**16. Risk management**

**(a) Governance framework**

The primary objective of the syndicate's risk management framework is to protect the syndicate's members from events that hinder the sustainable achievement of financial performance objectives, including failing to exploit opportunities. ASML recognises the critical importance of having efficient and effective risk management systems in place.

The managing agent has established a risk management function for the syndicate with clear terms of reference from the board of directors and its sub-committees. This is supplemented with a clear organisational structure with documented delegated authorities and responsibilities from the board of directors to executive management committees and senior managers. Lastly, a syndicate policy framework which sets out the risk

**16. Risk management** *continued*

profiles for the syndicate, risk management, control and business conduct standards for the syndicate's operations has been put in place. Each policy has a member of senior management charged with overseeing compliance with the policy throughout the syndicate.

The board of directors approves the risk management policies and meets regularly to approve any commercial, regulatory and organisational requirements of such policies. These policies define the identification of risk and its interpretation to ensure the appropriate quality and diversification of assets, align underwriting and reinsurance strategy to the syndicate goals, and specify reporting requirements. Significant emphasis is placed on assessment and documentation of risks and controls, including the articulation of 'risk appetite'.

**(b) Capital management objectives**

*Capital framework at Lloyd's*

Lloyd's is a regulated undertaking and subject to the supervision of the PRA under the Financial Services and Markets Act 2000.

Effective 1 January 2016, Lloyd's is subject to the Solvency II capital regime and the Solvency I figures are no longer applicable from that date. Although the capital regime has changed, this has not significantly impacted the SCR of the syndicate, since this has been previously calculated based on Solvency II principles, as described below.

Within the supervisory framework, Lloyd's applies capital requirements at member level and centrally to ensure that Lloyd's complies with Solvency II capital requirements, and beyond that to meet its own financial strength, licence and ratings objectives.

Although Lloyd's capital setting processes use a capital requirement set at syndicate level as a starting point, the requirement to meet Solvency II and Lloyd's capital requirements apply at overall and member level only respectively, not at syndicate level. Accordingly the capital requirement in respect of Syndicate 2121 is not disclosed in these financial statements.

*Lloyd's capital setting process*

In order to meet Lloyd's requirements, each syndicate is required to calculate its SCR for the prospective underwriting year. This amount must be sufficient to cover a 1 in 200 year loss, reflecting uncertainty in the ultimate run-off of underwriting liabilities (SCR 'to ultimate'). The syndicate must also calculate its SCR at the same confidence level but reflecting uncertainty over a one year time horizon (one year SCR) for Lloyd's to use in meeting Solvency II requirements. The SCRs of each syndicate are subject to review by Lloyd's and approval by the Lloyd's Capital and Planning Group.

A syndicate may be comprised of one or more underwriting members of Lloyd's. Each member is liable for its own share of underwriting liabilities on the syndicate on which it is participating but not other members' shares. Accordingly, the capital requirement that Lloyd's sets for each member operates on a similar basis. For a member participating on a single syndicate, its SCR is determined by the member's share of the syndicate SCR 'to ultimate'. Where a member participates on more than one syndicate a credit for diversification is included to reflect the spread of risk. The credit given is consistent with determining an SCR which reflects the capital requirement to cover a 1 in 200 year loss 'to ultimate' for that member. Over and above this, Lloyd's applies an uplift to the member's SCR to determine the overall level of capital required. This is known as the member's Economic Capital Assessment (ECA). The purpose of this uplift, which is a Lloyd's not a Solvency II requirement, is to meet Lloyd's financial strength, licence and ratings objectives. The capital uplift applied for the 2014 year of account was 35% of the member's SCR 'to ultimate'.

**16. Risk management** *continued*

*Provision of capital by members*

Each member may provide capital to meet its ECA either by assets held in trust by Lloyd's specifically for that member (FAL), held within and managed within a syndicate (funds in syndicate) or as the member's share of the members' balances on each syndicate on which it participates. Accordingly all of the assets less liabilities of the syndicate, as represented in the members' balances reported on the statement of financial position on page 23 of the syndicate annual accounts represent resources available to meet members' and Lloyd's capital requirements.

**(c) Insurance risk**

The principal risk the syndicate faces under insurance contracts is that the actual claims and benefit payments or the timing thereof, differ from expectations. This is influenced by the frequency of claims, severity of claims, actual benefits paid and subsequent development of long–term claims. Therefore, the objective of the syndicate is to ensure that sufficient reserves are available to cover these liabilities. Reference to insurance business should, as appropriate, be understood to include the equivalent reinsurance business underwritten by the syndicate.

The risk exposure is mitigated by diversification across a large portfolio of insurance contracts and geographical areas. The variability of risks is also improved by careful selection and implementation of underwriting strategy guidelines, as well as the use of reinsurance arrangements.

The syndicate purchases reinsurance as part of its risks mitigation programme. Reinsurance ceded is placed on both a proportional and non–proportional basis. The majority of proportional reinsurance is quota share reinsurance which is taken out to reduce the overall exposure to certain classes of business. Non–proportional reinsurance is primarily excess of loss reinsurance designed to mitigate the syndicate's net exposure to catastrophe losses and large individual risk losses. Retention limits for the excess of loss reinsurance vary by product line and territory.

Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision and are in accordance with the reinsurance contracts. Although the syndicate has reinsurance arrangements, it is not relieved of its direct obligations to its policyholders and thus a credit exposure exists with respect to ceded insurance, to the extent that any reinsurer is unable to meet its obligations assumed under such reinsurance agreements. The syndicate's placement of reinsurance is diversified such that it is neither dependent on a single reinsurer nor are the operations substantially dependent upon any single reinsurance contract.

The syndicate principally issues the following types of general insurance contracts: marine, aviation and transport; fire and other damage to property; energy; and third-party liability. Risks usually cover twelve months duration.

The most significant risks arise from natural disasters, terrorist activities, cyber attacks, large risk losses and adverse attritional claims experience. For longer tail claims that take some years to settle, there is also inflation risk.

The above risk exposure is mitigated by diversification across a large portfolio of insurance contracts and geographical areas. The variability of risks is improved by careful selection and implementation of underwriting strategies, which are designed to ensure that risks are diversified in terms of type of risk and level of insured benefits. This is largely achieved through diversification across industry sectors and geography. Furthermore,

**16. Risk management** *continued*

strict claim review policies to assess all new and ongoing claims, regular detailed review of claims handling procedures and frequent investigation of possible fraudulent claims are all policies and procedures put in place to reduce the risk exposure of the syndicate. The syndicate further enforces a policy of actively managing and promptly pursuing claims, in order to reduce its exposure to unpredictable future developments that can negatively impact the business. Inflation risk is mitigated by taking expected inflation into account where appropriate when estimating insurance contract liabilities.

The syndicate has also limited its exposure by imposing maximum claim amounts on certain contracts as well as the use of reinsurance arrangements in order to limit exposure to catastrophic events (e.g. hurricanes, earthquakes and flood damage).

The purpose of these underwriting and reinsurance strategies is to limit exposure to catastrophes based on the syndicate's risk appetite as decided by management. The overall aim is currently to restrict the impact of a single RDS on a gross of reinsurance basis to less than 80% of the ECA, and less than 30% on a net of reinsurance basis. The reinsurance counterparty exposure is managed such that the exposure to, for instance, a single 'A' rated reinsurer is estimated not to exceed 10% of the total recoverable amount for the programme. The board may decide to increase or decrease the maximum tolerances based on market conditions and other factors.

The syndicate uses both its own and commercially available proprietary risk management software to assess catastrophe exposure. However, there is always a risk that the assumptions and techniques used in these models are unreliable or that claims arising from an unmodelled event are greater than those arising from a modelled event.

The 2014 year of account has closed, so no catastrophe exposure written by the syndicate remains in respect of the closing year. A further guide to the level of catastrophe exposure written by the syndicate is in note 21 of the syndicate annual accounts.

Note 21 of the syndicate annual accounts includes analysis for the syndicate overall of the concentration of outstanding claim liabilities and unearned premiums by type of contract and the geographical concentration of the outstanding claim liabilities and unearned premiums.

*Key assumptions*

The principal assumption underlying the liability estimates is that the future claims development will follow a similar pattern to past claims development experience. This includes assumptions in respect of average claim costs, claim handling costs, claim inflation factors and claim numbers for each underwriting year. Additional qualitative judgements are used to assess the extent to which past trends may not apply in the future, for example: one–off occurrence; changes in market factors such as public attitude to claiming; economic conditions; as well as internal factors such as portfolio mix, policy conditions and claims handling procedures. Judgement is further used to assess the extent to which external factors such as judicial decisions and government legislation affect the estimates.

Other key circumstances affecting the reliability of assumptions include variation in interest rates, delays in settlement and changes in foreign currency rates.

**16. Risk management** *continued*

*Sensitivities*

Claim liabilities are not sensitive to the key assumptions as the 2014 year of account has closed and all assets and liabilities have been passed to a subsequent year of account by way of a reinsurance to close. Sensitivities relating to open years of account are included in note 21 of the syndicate annual accounts.

*Claims development table*

The syndicate annual accounts include tables showing the estimates of cumulative incurred claims, including both claims notified and IBNR for each underwriting year at each reporting date, together with cumulative payments to date. The cumulative claims estimates and cumulative payments are translated to sterling at the rate of exchange that applied at 31 December 2016.

The syndicate has taken advantage of the transitional rules of FRS 103 that permit only five years of information to be disclosed upon adoption. The claims development information disclosed in the syndicate annual accounts is being increased from five years to ten years over the period 2016 to 2020.

In setting claims provisions the syndicate gives consideration to the probability and magnitude of future adverse experience. Due to the uncertainty inherent in the estimation process, the actual overall claim provision may not always be in surplus.

**(d) Financial risk**

*(1) Credit risk*

Credit risk is the risk that one party to a financial instrument will cause a financial loss to the other party by failing to discharge an obligation.

The following policies and procedures are in place to mitigate the exposure to credit risk:

- A credit risk policy setting out the assessment and determination of what constitutes credit risk for the syndicate. Compliance with the policy is monitored and exposures and breaches are reported to the syndicate risk framework and compliance committee. The policy is regularly reviewed for pertinence and for changes in the risk environment.
- Net exposure limits are set for each investment counterparty or syndicate of counterparties with minimum credit quality requirements at a portfolio level.
- Reinsurance is placed with counterparties that have a good credit rating and concentration of risk is avoided by following policy guidelines in respect of counterparties' limits that are set by the finance and investment committee and are subject to regular reviews. At each reporting date management performs an assessment of creditworthiness of reinsurers, ascertaining a suitable allowance for impairment.
- Guidelines determine when to obtain collateral and guarantees.
- The syndicate sets the maximum amounts and limits that may be advanced to corporate counterparties by reference to their long term credit ratings.

**16. Risk management** *continued*

- The credit risk in respect of customer balances, incurred on non-payment of premiums or contributions, will only persist during the grace period specified in the policy document or trust deed until expiry, when the policy is either paid up or terminated. Commission paid to intermediaries is netted off against amounts receivable from them to reduce the risk of doubtful debts.

All assets will be assumed by the reinsuring year of account. The syndicate annual accounts include tables showing the maximum exposure to credit risk (including an analysis of financial assets exposed to credit risk) for the components of the annually accounted statement of financial position.

The syndicate annual accounts also include a table showing information regarding the credit risk exposure of the syndicate at 31 December 2016 by classifying assets according to Standard & Poor's credit ratings of the counterparties.

*Maximum credit exposure*
It is the syndicate's policy to maintain accurate credit ratings across its portfolio of investments and reinsurance counterparties.

Credit ratings are provided regularly by the syndicate's investment managers and are subject to regular review to ensure any counterparty risk is in line with the syndicate's risk appetite and complies with the specified investment guidelines. The management of the syndicate's investments is largely outsourced to professional investment managers who are given clearly defined credit, concentration and asset parameters within which they can operate. Specific provisions are included within the investment guidelines around notification of any credit breaches which would result in action being taken to rectify the position, subject to materiality.

*(2) Liquidity risk*
Liquidity risk is the risk that the syndicate will encounter difficulty in meeting obligations associated with financial instruments. In respect of catastrophic events there is also a liquidity risk associated with the timing differences between gross cash out flows and expected reinsurance recoveries.

The following policies and procedures are in place to mitigate the syndicate's exposure to liquidity risk:

- A liquidity risk policy exists that sets out the assessment and determination of what constitutes liquidity risk. Compliance with the policy is monitored and exposures and breaches are reported to the risk framework and compliance committee. The policy is regularly reviewed for pertinence and for changes in the risk environment.
- Guidelines on asset allocation, portfolio limit structures and maturity profiles of assets are set, in order to ensure that sufficient funding is available to meet insurance and investment contracts obligations.

*Maturity profiles*
All liabilities will be assumed by the reinsuring year of account. The syndicate annual accounts include a table that summarises the maturity profile of the syndicate's financial liabilities based on remaining undiscounted contractual obligations, including interest payable, and outstanding claim liabilities based on the estimated timing of claim payments resulting from recognised insurance liabilities.

**16. Risk management** *continued*

*(3) Financial market risk*

Financial market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Financial market risk comprises three types of risk:

a. Currency risk;

b. Interest rate risk; and

c. Equity price risk.

The following policies and procedures are in place to mitigate the exposure to financial market risk:

- A financial market risk policy exists that sets out the assessment and determination of what constitutes financial market risk for the syndicate. Compliance with the policy is monitored and exposures and breaches are reported to the risk framework and compliance committee. The policy is reviewed regularly for pertinence and for changes in the risk environment.
- Strict control over derivative instruments (e.g. equity derivatives are only permitted to be held to facilitate portfolio management or to reduce investment risk).
- For assets backing outstanding claims provisions, financial market risk is managed by ensuring the duration and profile of assets are aligned to the technical provisions they are backing. This helps manage financial market risk to the extent that changes in the values of assets are matched by a corresponding movement in the values of the technical provisions.

*(a) Currency risk*

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The syndicate's functional currency is sterling and its exposure to foreign exchange risk arises primarily with respect to transactions in euros, US dollars and Canadian dollars. The syndicate seeks to mitigate the risk by regularly seeking to match the estimated foreign currency denominated liabilities with assets denominated in the same currency.

The year of account result has closed and is fixed in a combination of sterling and US dollars so there is no foreign currency exchange exposure. The syndicate annual accounts include a table that summarises the exposure of the financial assets and liabilities to foreign currency exchange risk at the reporting date.

In part, foreign currency forward contracts may be used to achieve the desired exposure to each currency. From time to time the syndicate may also choose to utilise options on foreign currency derivatives to mitigate the risk of reported losses due to changes in foreign exchange rates. The degree to which options are used is dependent on the prevailing cost versus the perceived benefit to members' value from reducing the chance of a reported loss due to changes in foreign currency exchange rates.

**16. Risk management** *continued*

*Sensitivity to changes in foreign exchange rates*

The closed year result is fixed in a combination of sterling and US dollars and therefore not exposed to changes in foreign currency exchange rates. The syndicate annual accounts give an indication of the impact on profit of a percentage change in the relative strength of sterling against the value of the US dollar, Canadian dollar and euro simultaneously based on the information as at 31 December 2016.

*(b) Interest rate risk*

Interest rate risk is the risk that the value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Floating rate instruments expose the syndicate to cash flow interest risk, whereas fixed rate instruments expose the syndicate to fair value interest risk.

The syndicate has no significant concentration of interest rate risk.

Insurance liabilities are not discounted and therefore not exposed to interest rate risk.

Analysis in note 21 of the syndicate annual accounts is performed for reasonably possible movements in interest rates with all other variables held constant and shows the impact on profit of the effects of changes in interest rates on financial assets and liabilities for items recorded at fair value through profit or loss.

*(c) Equity price risk*

Equity price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

The syndicate's equity price risk exposure relates to financial assets and financial liabilities whose values will fluctuate as a result of changes in market prices, principally investment securities.

The financial market risk policy requires it to manage such risks by setting and monitoring objectives and constraints on investments, diversification plans, limits on investments in each sector and market, and careful and planned use of derivative financial instruments.

There is no significant concentration of equity price risk.

Note 21 in the syndicate annual accounts includes analysis performed for reasonably possible movements in market indices on financial instruments, with all other variables held constant, showing the impact on profit due to changes in fair value of financial assets and liabilities whose fair values are recorded in the profit and loss account. The correlation of variables will have a significant effect in determining the ultimate impact on equity price risk, but to demonstrate the impact due to changes in variables, the variables were altered on an individual basis. It should be noted that movements in these variables are non-linear.

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