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ICAT Special Purpose Arrangement 6123

Syndicate Annual Report and Accounts

31 December 2016

Contents

Directors and Administration

Managing Agent

Asta Managing Agency Ltd

Directors

T A Riddell (Chairman)*
C V Barley
L Harfitt
A J Hubbard*
D J G Hunt
M D Mohn*
D F C Murphy*
S P A Norton
J W Ramage*
K Shah*
J M Tighe

Non Executive Directors*

Company Secretary

C Chow

Managing Agent's Registered Office

5th Floor
Camomile Court
23 Camomile Street
London
EC3A 7LL

Managing Agent's Registered Number

1918744

Active Underwriter

M H McConnell

Host Syndicate/Reinsured

Syndicate 4242

Registered Auditors

KPMG LLP

Signing Actuary

N Sharif, KPMG LLP

Annual Report of the Directors of the Managing Agent

The directors of the Managing Agent (the directors) present their report below, together with the audited annual accounts for Special Purpose Arrangement 6123 (the SPA), for year ended 31 December 2016 on pages 15 to 39.

The directors prepared this annual report using the annual basis of accounting required by Statutory Instruments No. 1950 of 2008, the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008.

Results

The SPA generated a loss of $1.9 million (2015: loss of $1.8 million) on gross written premiums of $18.8 million (2015: $6.6 million).

This table details the forecast for the 2015 and 2016 open underwriting year.

	2016 Open	**2015 Open**
	$'000	$'000
Loss	(1,325)	(731)
Return on insurance capacity	(7.1%)	(7.4%)

Principal activities

The SPA Lloyd's vehicle was established in May 2015 to offer additional capacity to ICAT's Middle Market Business Unit (MMBU). The SPA reinsures up to $5 million of per risk limit on smaller commercial properties, typically habitational, located in areas of the United States (U.S.) that are prone to hurricanes and earthquakes. Limit is offered as a variable quota share to ICAT Syndicate 4242 (the Host Syndicate) where up to 80% of the per risk limit assumed by Syndicate 4242 can be reinsured to the SPA. Syndicate 4242 and the SPA offer capacity to ICAT, alongside other insurance companies and Lloyd's syndicates, to underwrite smaller commercial risks that are generally $10 million to $100 million in total insured value. Total authorised insurance capacity for the SPA is £15.0 million ($18.6 million), measured as gross written premium net of acquisition costs.

Reinsured hurricane policies include coverage for tropical storms and also provide attritional protection against tornados, hail, and other windstorm risks. Reinsured policies also offer limited flood coverage when purchased alongside hurricane or earthquake coverage and All Other Peril (AOP) coverage. AOP coverage provides protection against fires, theft, vandalism, water damage, and other covered property perils.

The Host Syndicate and SPA contract with certain wholly owned subsidiaries of Paraline Group, Ltd, a Bermuda based insurance organisation, for certain insurance services; these subsidiaries include International Catastrophe Insurance Managers, LLC (ICAT Managers), Boulder Claims, LLC (Boulder Claims), and Paraline International, Ltd (Paraline International). ICAT Managers and Boulder Claims are Delaware companies, while Paraline International is a Bermuda company.

Annual report of the Directors of the Managing Agents continued

ICAT Managers underwrites the business being assumed by the Host Syndicate. Although the Host Syndicate and SPA delegate day-to-day underwriting and related reinsurance and operational management responsibility to ICAT Managers, the Directors regularly review the results of the coverholder's monitoring procedures and supplement these procedures with Managing Agent and third party audits. Paraline International also provides underwriting oversight for the Host Syndicate.

Boulder Claims provides claims administration services to the Host Syndicate and, therefore, the SPA. The Managing Agent contracts with a third party to coordinate oversight of Boulder Claims.

The insurance services that ICAT Managers and Boulder Claims (collectively, ICAT) provide to the Host Syndicate and by extension to the SPA account for 59.4% (53.8% at 31 December 2015) of their total business. ICAT also provides services to other syndicates and insurance carriers and claims services to a state sponsored risk pool. ICAT's main office is in Broomfield, Colorado.

Business review

The Host Syndicate entered into a binding authority agreement with ICAT to underwrite insurance business and the SPA proportionately reinsures a portion of this business. ICAT writes this business in the underwriting regions of the U.S. below.

i. Eastern Seaboard

ii. Florida

iii. Gulf Coast

iv. Hawaii

v. Earthquake (primarily California, the U.S. Pacific Northwest, the U.S. Intermountain West, Alaska, the New Madrid area of the U.S., and Hawaii)

Since formation in May 2015, the SPA has been building momentum and finished 2016 with $18.8m of gross premium. A full twelve months of writing was the driver for the substantial growth, although all regions grew particularly in the last quarter of the year. The relative higher inception of Q4 writings has meant that a lot of premium has not been earned in 2016 and is exposed to the 2017 hurricane season.

Key financial performance indicators

In the opinion of the directors, the key financial performance indicators below best represent the performance and position of the SPA.

	2016 $'000	2015 $'000
Gross written premiums:		
Eastern Seaboard	3,159	1,115
Florida	8,007	2,620
Gulf Coast	3,029	992
Hawaii	10	2
Earthquake	4,591	1,884
Total gross written premiums	18,796	6,613
% of insurance capacity	72.5%	38.4%
Outward reinsurance premiums	(9,511)	(3,192)
Loss for the financial year	(1,877)	(1,806)
Members' balances	(3,728)	(1,806)

The SPA is currently in a loss position as it builds to critical mass. Approximately half of the 2016 underwriting year gross premium is earned with remaining premium to be earned in 2017. With a full year of premium earnings on current production volume the SPA will be able to support operating expenses going forward.

The majority of the SPA's claims expense emanate from Hurricane Matthew. This storm paralleled the Florida and southern states of the Eastern Seaboard coastline before making landfall on 8th October in South Carolina as a Category 1 Hurricane. The SPA has received claims in Florida, Georgia and South Carolina proportionate to its portfolio. The storm has been reserved well within its tolerance before reinsurance protection and is developing consistently with expectations. Other claims during the year for AOP and attritional losses remain within expectations.

Non-financial key performance indicators

	2016	2015
Adherence to underwriting authority limits	100.0%	100.0%
Customer retention ratio	85.2%	N/A

The Managing Agent contracts with ICAT to perform a majority of the SPA's activities. The Managing Agent's staff, however, reviews and monitors the activities of ICAT and provides actuarial (both reserving and capital modelling), regulatory compliance, and risk management services to the SPA. The Managing Agent is responsible for the environmental activities of the SPA, although by their nature, insurers generally do not produce significant environmental emissions. Therefore, the directors do not consider it appropriate to monitor and report any performance indicators for environmental matters.

Outward reinsurance arrangements

Catastrophe Coverage – The SPA has layered catastrophe reinsurance to protect against the adverse accumulation of the losses below from multiple reinsured policies as a result of large catastrophic events.

i. First event: Losses in excess of $4 million up to $109 million

ii. Second event: Losses in excess of $2 million up to $74 million

If the SPA exhausts any of its catastrophe reinsurance, a portion of the coverage is automatically reinstated for additional premiums to protect against more catastrophic events during the rest of the coverage term, subject to certain aggregate limits.

With the exception of the last layer of the SPA's first event coverage, the reinsurers charge the SPA flat premiums for the coverage they provide. Also, the first layer of the SPA's first event coverage has a no claim bonus, where the reinsurers agree to return 15% of the layer's premiums to the SPA subject to no claims being paid under the layer.

Attritional Catastrophe Coverage – The SPA has attritional catastrophe reinsurance to protect against tornadoes, hail, and other windstorm events, each with losses in excess of $333,333 up to $1.3 million with no reinstatement.

All Other Peril Coverage – The SPA has reinsurance to protect against the occurrence of other events such as large fires. The SPA reinsures losses excluding flood, earthquake, windstorm or hail in excess of $1 million for each building up to $5.7 million and events damaging several buildings in the same location with losses in excess of $666,666 up to $1.6 million. For multiple sinkhole collapse and terrorism events, total coverage is limited to $11.7 million. The SPA earns contingent profit commissions on this coverage equal to 25% of the excess of ceded premiums over deductions for underwriting expenses (equal to 35% of ceded premiums) and any claims, including adjustment expenses being paid under the coverage.

Future outlook

The SPA is looking to achieve moderate growth in 2017 with a focus on balancing the portfolio across peril and region. The SPA will continue to operate within the ICAT MMBU segment and is anticipating growth consistent with ICAT's plans. Reinsurance coverage will be evaluated and optimised in accordance with risk appetite and profitability targets.

Foreign exchange

Foreign exchange is not significant to the SPA since all underwriting business is in U.S. Dollars.

Principal risks and uncertainties

The following paragraphs summarise the principal risks and uncertainties facing the SPA.

Insurance risk

Underwriting Risk – Underwriting risk may either arise from an inaccurate assessment of the risks entailed in writing an insurance policy or from factors wholly out of the SPA's control. As a result, losses paid by the SPA may exceed earned premiums. The SPA tries to reduce underwriting risk by basing its risk appetite on its maximum loss tolerance. The SPA sets its tolerance for catastrophe losses based on nationwide and regional Exceedance Probabilities (EP) in the U.S., as well as on Realistic Disaster Scenarios (RDS) designed to stress test the SPA for material catastrophe risks at different probability levels by potential loss of capital. The EP is the probability that losses exceed a certain threshold for a catastrophic loss event at a selected probability of occurrence. The SPA generally quantifies its risk appetite at the 99.5% EP level or the 1 in 200 year loss. RDS include the events below.

i. Windstorm in the Northeastern U.S.

ii. Windstorm in the Carolinas

iii. Two separate Florida windstorms (Miami-Dade and Pinellas)

iv. Windstorm in the U.S. Gulf

v. Two separate California earthquakes (Los Angeles and San Francisco)

vi. New Madrid area of the U.S. earthquake

vii. Two separate Syndicate-specific scenarios (Mississippi windstorm and U.S. Pacific Northwest earthquake)

The SPA monitors its EP estimated losses throughout the year. The SPA sets its tolerance for AOP losses at the building and location level. ICAT monitors the SPA's loss exposures against its underwriting risk appetite using various methods, including RDS modelling. Also, the SPA periodically evaluates and adjusts its reinsurance protection to manage its overall retention of insurance risk.

Under the binding authority agreement with the Host Syndicate, ICAT underwrites all of the policies that the SPA proportionately reinsures. Underwriters adhere to daily monitored regional blueprints, which identify where the Host Syndicate's and by extension the SPA's insurance capacity should be deployed. These blueprints, with their defined underwriting guidelines alongside modelling and pricing practices, determine the prescribed range of rates at which ICAT may sell insurance capacity. Underwriters must refer underwriting decisions for risks outside of those outlined in the blueprints or in excess of their authority limit to higher levels of authority. ICAT audits the individuals who have binding authority in both groups on a regular basis to ensure adherence to established underwriting authority limits. ICAT also conducts other underwriting audits on an ad-hoc basis and reviews significant risks written each month. The Managing Agent also has its own controls.

The Managing Agent has a governance structure in place to monitor the underwriting and loss exposure management controls of ICAT. The Managing Agent appoints the Host Syndicate's Board (the Board), which manages the SPA. The Board ensures the appropriate management of the SPA in accordance with the Managing Agent's responsibilities. The Board meets quarterly and has delegated authority to approve underwriting related matters, including:

i. non-material changes to the business plan,

ii. underwriting authority levels and guidelines,

iii. operational and ICAT procedures,

iv. risk policies, the risk register, and all other risk management matters, and

v. the SPA's compliance plan.

Annual report of the Directors of the Managing Agents continued

The Managing Agent also monitors the SPA's performance against its underwriting risk appetite in several ways, including regular meetings with the Active Underwriter and participation in the monthly meetings of the Production Risk Management Committee (the Committee), which is a subcommittee of the Board, that considers reports from the Active Underwriter and other areas of the business. The Committee also reviews underwriting related matters, including:

i. progress against the business plan or forecast,

ii. premium rates and volumes,

iii. overall loss exposures,

iv. significant product and premium rate changes;

v. market conditions, and

vi. the outcome of underwriting audits covering the operations of ICAT.

Furthermore, Paraline International provides oversight of the underwriting policies adopted by the Active Underwriter. Paraline International identifies key underwriting and reinsurance guidelines and limitations in ICAT's binding authority agreement and the reinsurance agreement between the Host Syndicate and the SPA and monitors ICAT's adherence to these guidelines including consideration of material changes in authority, risk profile, reinsurance, and any breaches of agreement.

The SPA's annual business planning process sets the targets for written premiums and overall profitability for the coming year. Factors taken into account in determining these targets include the risk appetite of the SPA's capital providers, reinsurance agreement terms and conditions, and other risk metrics.

Reserving Risk – The SPA's financial condition and profitability depend heavily on its ability to accurately assess its liability for claims outstanding from its reinsured risks. The SPA tries to reduce the risk associated with this assessment by hiring qualified third party claims administrators that have specialised adjusters and forensic engineers to set reserves on notified damaged properties. Both ICAT and the Managing Agent review these reported claims monthly. The SPA also employs standard actuarial methods to assess its overall best estimate of reserves for each underwriting account quarterly using historical losses loaded for future uncertainty in areas where reserves may prove to be materially inadequate; this assessment process requires ongoing discussions between the SPA's actuaries and the underwriters and claims adjusters of ICAT, and includes various levels of approval supplemented by external actuarial validation. The SPA's actuaries track projected loss ratios quarterly and may reassess their reserving methods if necessary. The Board approves the reserves of the SPA quarterly, after considering the recommendation of the Reserve Committee (a subcommittee of the Board).

Catastrophe Risk – The occurrence of adverse economic conditions, natural or other disasters, or other circumstances specific to or otherwise significantly impacting the regions and states in which the SPA mainly reinsures business in may adversely affect its profitability and financial condition. The SPA tries to limit this risk through geographic diversification. ICAT uses catastrophe models to set the SPA's overall loss exposure limits; these models include provisions for secondary uncertainty, loss amplification (demand surge), storm surge coverage leakage. ICAT models every property in the Host Syndicate's book of business and by extension the SPA's reinsurance business monthly using adjusted modelling parameters to address observed deficiencies in these models to better reflect historical losses. In managing the Host Syndicate's risk appetite, ICAT allocates limits to various geographic zones. The identification and determination of each zone and its area as well as whether to include a particular policy within a zone's limits requires significant judgment. ICAT controls and limits the Host Syndicate's concentration of risk within these zones as well as the risk at the neighbourhood and street level using an accumulation tool.

In addition to the SPA's catastrophe risks, the SPA's profitability and financial condition may be adversely affected by unexpectedly large accumulations of AOP losses. ICAT tries to reduce this risk to the SPA by using appropriate underwriting processes for the Host Syndicate, which include inspections of every property, to guide the pricing and acceptance of risks. These processes help to ensure that premiums cover the expected levels of loss.

The SPA tries to limit its risk of insolvency from a single large catastrophe or multiple smaller catastrophes by purchasing reinsurance. The SPA evaluates the probability of catastrophes using a catastrophe model that quantifies its hurricane and earthquake related loss exposures. ICAT developed the catastrophe model used by the SPA by applying its model adjustment methodology on a model from a major vendor to align the vendor model to the SPA's assessment of risk. The SPA applies ICAT's model adjustment methodology because it estimates building vulnerability, storm surge coverage leakage, losses from inland risks and coastal risks, and landfall frequency and severity more precisely than the vendor model. The SPA validates the results from ICAT's methodology against alternate models from other major vendors.

Reinsurance Risk – The cost of reinsurance also impacts the SPA where the availability of reinsurance and associated pricing is subject to prevailing market conditions which fluctuate in cycles over time. These cycles are affected by various factors including the frequency and severity of worldwide catastrophic events, market capacity, competition, and general economic conditions. The SPA monitors market cycles and seeks favourable reinsurance pricing with a diversified group of secure reinsurers.

Operational risk

Operational risk is the risk that events caused by people, internal controls, processes, or systems lead to losses for the SPA. The Managing Agent together with ICAT and Paraline International try to manage this risk for the SPA by having detailed procedure manuals in place. They also have business continuity and disaster recovery plans in place. The close involvement of the directors in the SPA's key decision making further reduces the risk of these losses.

Market risk

Interest Rate Risk – The SPA has no investments, and therefore has no exposure to interest rate risk.

Currency Risk – The SPA writes all its business in U.S. Dollars, which is its functional currency. The SPA also keeps all of its reinsurance balances in U.S. Dollars. The SPA has Great British Pound expenses; these expenses, however, do not create material currency risk for the SPA. The SPA has no exposure to other currencies.

Investment Price Risk – The SPA has no investments, and therefore has no exposure to investment price risk.

Credit risk

Bankruptcy, liquidity problems, distressed financial condition, or the general effects of today's economic environment may increase the risk that policyholders or intermediaries, such as insurance agents and brokers, may not pay a part of or the full amount of premiums owed to ICAT, despite an obligation to do so. If non-payment becomes widespread, whether as a result of bankruptcy, lack of liquidity, adverse economic conditions, operational failure, or otherwise, it could have a material adverse impact on the financial condition of ICAT and its ability to pay the premiums it in turn owes to the Host Syndicate and the Host Syndicate in turn owes the SPA. No single agent, broker, or policyholder accounted for more than 12.3% (2015: 13.2%) of the premiums that ICAT wrote for the Host Syndicate and 12.9% (2015: 13.4%) of the Host Syndicate's premium balances due at 31 December 2016. Further, the insurance policies that the SPA reinsures may be cancelled for non-payment from policyholders.

The SPA transfers significant amounts of insurance risk to reinsurers. If these reinsurers fail to honor their obligations, the SPA's financial condition, profitability, and cash flows could be adversely affected. The SPA tries to reduce this risk by setting maximum exposure and credit limits for each of its reinsurers based on their industry credit rating and net asset balance. The SPA regularly evaluates the financial condition and payment performance of its reinsurers with the help of outside brokers; evaluations include reviewing credit ratings and monitoring concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics to minimise the SPA's exposure to significant losses from reinsurer insolvencies. The SPA mostly purchases reinsurance from reinsurers with an A.M. Best or Standard & Poor's rating of A or better. If a reinsurer does not have an A or better rating, the Syndicate may obtain collateral from the reinsurer to secure their reinsurance obligations. The SPA had no collateral from its reinsurers at 31 December 2016 (Nil at 31 December 2015) to secure their obligations. There were no catastrophe or AOP reinsurance recoveries outstanding at 31 December 2016.

Liquidity risk

The Host Syndicate pays insurance claims and other liabilities on the SPA's behalf in accordance with the funds withheld and inter-syndicate loan arrangements that SPA has with the Host Syndicate. Under the inter-syndicate loan arrangement that the SPA has with the Host Syndicate, the Host Syndicate may advance up to $10 million to the SPA. The SPA's operations, however, could be adversely affected if the Host Syndicate did not have enough cash to pay the SPA's obligations. The Host Syndicate tries to reduce this risk by reviewing its expected cash obligations on a quarterly basis and keeping adequate cash on deposit to meet those obligations. The Host Syndicate settles the SPA's payment obligations in accordance with the vendor terms of each transaction. The Host Syndicate holds any excess funds in cash or invests them in money funds readily convertible to cash without excessive cost to the business. The Host Syndicate also has a $35 million letter of credit facility from Barclays Bank PLC.

Regulatory and compliance risk

The SPA is subject to continuing approval by Lloyd's to operate in the Lloyd's market and must comply with the regulatory requirements set by Lloyd's, the Financial Conduct Authority (FCA) and Prudential Regulatory Authority (PRA). Lloyd's requirements include those imposed on the Lloyd's market by overseas regulators, particularly by U.S. regulators concerning U.S. risks underwritten by the Lloyd's market. The SPA tries to reduce the risk of its approval to operate in the Lloyd's market being revoked by monitoring and fully complying with all of its regulatory obligations. The Managing Agent helps the SPA in this regard by regularly monitoring regulatory and legal compliance related developments and assessing the impact of these developments on agency and SPA policies.

Insurance business is state regulated in the U.S., and therefore, state legislatures may enact laws that adversely affect the industry. Such unfavourable changes could adversely impact the Host Syndicate's operations and by extension the operations of the SPA. The Host Syndicate's operating status in all states as an approved non-admitted surplus lines carrier rather than as a licensed and admitted carrier, however, reduces this risk. Surplus lines carriers are less regulated, specifically in the forms they use and the rates they can charge. Surplus lines carriers, however, cannot write insurance that is typically available in the admitted market and, traditionally, may only write a policy if it has been rejected by three different admitted carriers and provided the agent or broker placing the business with them has a surplus lines license. Surplus lines carriers are not protected by state guarantee funds, although the U.S. trust funds and Lloyd's Central Fund provide a chain of security for policyholders.

Future developments

The SPA insurance capacity to write business remained consistent at £15.0 million ($18.6 million) for the 2017 underwriting year (2016: £15.0 million, $18.6 million).

The risks to UK economic growth remain significant not least because of the UK's decision to leave the European Union ("EU") ("Brexit"). There is significant change and associated uncertainty ahead for the market which is difficult to anticipate as the terms of the UK's exit from the EU remain unclear. Until that happens, the market will need to plan carefully for all possible scenarios to mitigate the impact of Brexit on Lloyd's businesses.

EU membership and access to the single market has enabled underwriters at Lloyd's to underwrite insurance and reinsurance from all the other 27 member states on a cross-border basis. The underwriters operate under a "passport" system, which allows them to conduct business throughout the EU while being regulated and supervised by the PRA.

It is expected that Lloyd's will publish its final Brexit plan in the first quarter of 2017. Lloyd's has a dedicated team putting forward the argument to the UK government on behalf of the marketplace for retaining EU passporting, but has yet to decide on how this is achieved; either by a single insurance company or a branch solution.

Effective 1 January 2016, Lloyd's is subject to the Solvency II capital regime and Solvency I figures are no longer applicable from that date. Although the capital regime changed, it has not impacted the Solvency Capital requirement of the SPA, since the SPA calculated its requirement based on Solvency II principles.

Annual report of the Directors of the Managing Agents continued

Directors

Details of the Directors of the Managing Agent that served during the year end and up to the date of signing of the financial statements are provided on page 1. Changes to directors were as follows:-

C V Barley	Appointed 27 April 2016
M D Mohn	Appointed 16 May 2016
K Shah	Appointed 1 October 2016
Y A Lancaster (nee Bouman)	Resigned 12 February 2016
G M J Erulin	Resigned 31 March 2016

The directors of Asta did not participate on the SPA and did not have an interest in any of its contracts.

Disclosure of information to the auditors

Each of the directors who held office at the approval date of this report confirms to the best of their knowledge, that there is no relevant audit information of which the SPA's auditors are unaware, and each Director took all action necessary as a Director to become aware of any relevant audit information and to establish that the SPA's auditors are aware of that information.

Auditors

Pursuant to Section 14(2) of Schedule 1 of the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008, the auditors will be deemed to be reappointed and KPMG LLP will therefore continue in office.

On behalf of the Board

Charmaine Chow
Company Secretary
21 March 2017

Statement of Managing Agent's responsibilities

The Managing Agents are responsible for preparing the Syndicate financial statements in accordance with applicable law and regulations.

Insurance Accounts Directive (Lloyds's Syndicate and Aggregate Accounts) Regulations 2008 requires the Managing Agent to prepare their Syndicates financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*.

Under Insurance Accounts Directive (Lloyds's Syndicate and Aggregate Accounts) Regulations 2008 the Managing Agents must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Syndicate and of the profit or loss of the Syndicate for that period. In preparing these financial statements, the Managing Agents are 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 financial statements; and
- prepare the financial statements assuming there are no uncertainties surrounding the Syndicate's ability to continue to write business in the future as required to provide a true and fair view

The Managing Agents are responsible for keeping adequate accounting records that are sufficient to show and explain the Syndicate's transactions and disclose with reasonable accuracy at any time the financial position of the Syndicate and enable them to ensure that the financial statements comply with the Insurance Accounts Directive (Lloyds's Syndicate and Aggregate Accounts) Regulations 2008. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

The Managing Agents are responsible for the maintenance and integrity of the Syndicate and financial information included on the Syndicate's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Independent auditor’s report

Independent auditor's report to the members of Special Purpose Arrangement 6123

We have audited the financial statements of Special Purpose Arrangement 6123 for the year ended 31 December 2016, as set out on pages 15 to 39. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice), including FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland.*

This report is made solely to the members of the Syndicate, 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 in an auditors’ 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 and 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 auditors

As explained more fully in the Statement of Managing Agent’s Responsibilities set out on page 12, the Managing Agent is responsible for the preparation of the Syndicate's financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the Syndicate's financial statements 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 financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council’s website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion the financial accounts:

- give a true and fair view of the Syndicate’s affairs at 31 December 2016 and its loss for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Insurance Accounts Directive (Lloyd’s Syndicate and Aggregate Accounts) Regulations 2008.

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 Report of the Directors of the Managing Agent is consistent with the financial statements.

Independent auditor's report continued

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:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations we require for our audit.

Timothy Butchart (Senior Statutory Auditor)
For and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants
15 Canada Square
London, E14 5GL

21 March 2017

Income statement

Technical account – general business

For the year ended 31 December 2016

	Notes	2016 $'000	2015 $'000
Earned premiums, net of reinsurance:			
Gross premiums written	3	18,796	6,613
Outward reinsurance premiums		(9,511)	(3,192)
Net written premiums		9,285	3,421
Change in the gross provision for unearned premiums	6	(4,209)	(4,756)
Change in the provision of unearned premiums, reinsurers' share	6	926	958
Net change in provision for unearned premiums		(3,283)	(3,798)
Earned premiums, net of reinsurance		6,002	(377)
Allocated investment return transferred from the non-technical account		5	-
Claims incurred, net of reinsurance			
Claims paid			
• Gross amount		(781)	(26)
• Reinsurers' share		-	-
Claims paid		(781)	(26)
Change in the provision for claims:	6		
• Gross amount		(2,439)	(98)
• Reinsurers' share		-	-
Change in provision for claims		(2,439)	(98)
Claims incurred, net of reinsurance		(3,220)	(124)
Net operating expenses	4,5	(4,658)	(1,323)
Balance on technical account – general business		(1,871)	(1,824)

All operations relate to continuing activities.

The notes are on pages 21 to 39 form part of these annual accounts

Income statement continued

Non-technical account - general business

For the year ended 31 December 2016

	2016 $'000	2015 $'000
Balance on technical account – general business	(1,871)	(1,824)
Investment income	4	-
Unrealised gains on investments	1	-
Investment expenses and charges	(1)	-
Unrealised losses on investments	1	-
Allocated investment return transferred to general business technical account	(5)	-
Other income - profit / (loss) on exchange	(6)	18
Loss for the financial year	(1,877)	(1,806)

All operations relate to continuing activities.

Special Purpose Arrangement 6123 had no recognised gains and losses this year other than those included in the Profit and Loss Account. Therefore, the directors of the Managing Agent have not presented a Statement of Comprehensive Income.

The notes on pages 21 to 39 form part of these annual accounts.

Statement of financial position

For the year ended 31 December 2016

	Notes	2016 $'000	2015 $'000
ASSETS			
Reinsurers' share of technical provisions	6		
Provision of unearned premiums		1,883	958
Claims outstanding		-	-
		1,883	958
Debtors:			
Debtors arising out of reinsurance operations		5,285	4,359
Other debtors		45	106
		5,330	4,465
Prepayments and accrued income:			
Deferred acquisition costs	6	2,524	1,323
Other prepayments and accrued income		331	51
		2,855	1,374
Total assets		10,068	6,797

The notes on pages 21 to 39 form part of these annual accounts.

Statement of financial position continued

For the year ended 31 December 2016

	Notes	2016 $'000	2015 $'000
MEMBERS' BALANCE AND LIABILITIES			
Capital and reserves			
Members' balances		(3,728)	(1,806)
Liabilities			
Technical provisions	6		
Provision for unearned premiums:			
Gross amount		8,965	4,756
Claims outstanding			
Gross amount		2,536	98
		11,501	4,854
Creditors			
Creditors arising out of reinsurance operations	7	2,035	164
Inter-syndicate loan		-	3,320
Other creditors		118	102
		2,153	3,586
Accruals and deferred income		142	163
Total liabilities		10,068	6,797

The board of Asta Managing Agency Ltd approved Special Purpose Arrangement 6123's annual accounts on pages 15 to 39 on 15 March 2017, which the Director below signed on the board's behalf.

David J G Hunt
Director
21 March 2017

The notes on pages 21 to 39 form part of these annual accounts.

Statement of changes in members' balances

For the year ended 31 December 2016

	2016 $'000	2015 $'000
Members' balances at beginning of year	(1,806)	-
Loss for the financial year	(1,877)	(1,806)
Members' agent fees	(45)	-
Members' balances at end of year	(3,728)	(1,806)

Members participate in Special Purpose Arrangement 6123 on an underwriting year basis. Special Purpose Arrangement 6123 assesses its results and net assets for each underwriting year based on the policies incepting in that year for the membership of that year.

The notes on pages 21 to 39 form part of these annual accounts.

Statement of cash flows

For the year ended 31 December 2016

	Notes	2016 $'000	2015 $'000
Cash flows from Operating activities			
Loss on ordinary activities		(1,877)	(1,806)
Increase in gross technical provisions		2,438	98
(Increase) in reinsurers' share of gross technical provisions		-	-
(Increase) in debtors		(865)	(4,465)
(Decrease)/Increase in creditors		(1,433)	3,586
Movement in other asset/liabilities/foreign exchange		1,742	2,587
Investment Return		(5)	-
Net cash inflows from operating activities		-	-
Cash from Investing activities			
Investment income received		-	-
Net cash inflows from investing activities		-	-
Cash from Financing activities			
Collection of losses		-	-
Other		-	-
Net cash inflows from financing activities		-	-
Net increase in cash and cash equivalents		-	-
Cash and cash equivalents at beginning of year		-	-
Cash and cash equivalents at end of year		-	-

Notes to the annual accounts

For the year ended 31 December 2016

1. Basis of preparation

Statement of compliance

The Directors of the Managing Agent (the directors) prepared these annual accounts for Special Purpose Arrangement 6123 (the SPA) in compliance with The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 and Financial Reporting Standard 102, *The Financial Reporting Standard* (FRS 102) and Financial Reporting Standard 103, *Insurance Contracts* (FRS 103), being applicable United Kingdom (U.K.) Generally Accepted Accounting Practice (GAAP), 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 Directors prepared these accounts on the historical cost basis, except for certain financial instruments measured at fair value through profit or loss, and presented them in U.S. Dollars, which is the functional and presentational currency of the SPA. The SPA has no cash and cash equivalents and accordingly, the directors did not present a Statement of Cash Flows in these accounts.

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.

2. Accounting policies

Use of estimates

The preparation of accounts in conformity with U.K. GAAP requires that the directors to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the accounts, and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. Significant items subject to such estimates and assumptions include:

(i) provision for claims outstanding (refer to claims incurred accounting policy);

(ii) expected policy cancellations;

(iii) accruals for contingent commissions under reinsurance contracts; and

(iv) estimates of future premium for binder contracts (refer to gross premiums accounting policy).

Accounting policies continued

Insurance contracts

Insurance contracts are contracts where the SPA (as a reinsurer) accepts significant insurance risk (risk arising from both underwriting risk and timing risk), from a reinsured by agreeing to compensate them if a specified uncertain future event (the reinsured event) adversely affects them. The SPA determines whether it has significant insurance risk by comparing the amount and timing of premiums, commissions, and claim settlement expenses paid with the amount and timing of such cash flows if the reinsured event did not occur. Insurance contracts can also transfer financial risk.

Once the SPA classifies a contract as an insurance contract, it remains an insurance contract for the remainder of its term, even if the insurance risk decreases significantly during this period, unless all rights and obligations extinguish or expire.

Gross premiums written

Gross premiums written consist of premiums from inward reinsurance acceptances during the year. Gross premiums written also include premiums on reported but unprocessed reinsurance acceptances at the balance sheet date and a deduction for expected reinsurance acceptance cancellations based on the reinsured's historical cancellation activity over the past two years. The SPA shows premiums gross of ceding commissions on inward reinsurance acceptances and excludes taxes and fees levied on them.

Outward reinsurance premiums

Outward reinsurance premiums consist of premiums on outward reinsurance contracts with other insurers and reinsurers bound during the year to reduce the SPA's exposure to losses from catastrophes and all other property perils. The SPA's catastrophe reinsurers also charge reinstatement premiums to restore reinsurance contracts to their full limits when large catastrophes occur that exhaust all or a portion of these limits. Reinsurance transactions do not relieve the SPA of its primary obligations to its policyholders.

Provisions for unearned premiums

The provision for unearned premiums is the portion of gross premiums written that the SPA will earn in the future and the corresponding amount of reinsurance premiums that it will expense. The SPA earns hurricane premiums, inclusive of attritional catastrophe coverage covering tornados, hail, and other windstorm risks, evenly over the Atlantic Hurricane Season(s) (the incidence of risk) that occur during the policy term. The Atlantic Hurricane Season runs from June 15th to November 15th of each year. The SPA earns earthquake and all other property peril premiums evenly over the policy term. The SPA expenses related reinsurance premiums evenly over the contract term (remaining contract term for reinstatement premiums), or incidence of risk, if significantly different. The SPA also expenses the deferred premium balance on exhausted coverage when large catastrophes occur.

Provision for unexpired risks

At the balance sheet date, the SPA performs a liability adequacy test on it insurance liabilities less related deferred acquisition costs to ensure that the carrying value is adequate, using current estimates of future cash flows. If this test shows that the liabilities is inadequate, any deficiency is recognised as an expense to the profit or loss account initially by recognising an additional liability for claims provisions or recognising a provision for unexpired risks.

Accounting policies continued

The directors assess the provision for unexpired risks by class of business. No provision for unexpired risks was recorded in 2016 (2015: Nil).

Claims incurred, Net of reinsurance

Gross claims incurred consist of the estimated cost of settling all claims occurring before the balance sheet date, whether reported or not, including related claims handling expenses. The SPA does not discount claims outstanding. The SPA anticipates subrogation recoveries when it sets provisions for reported claims. The SPA accounts for reinsurance recoveries when it incurs the related losses. The directors assess the provision for claims outstanding on a case basis based on the estimated cost of all claims notified but not settled at the balance sheet date.

The provision also includes the estimated cost of claims incurred but not reported (IBNR) at the balance sheet date based on statistical methods and includes adjustments for catastrophes and other significant events, changes in historical trends, economic and social conditions, judicial decisions, and legislation, as necessary.

In evaluating the provision, the directors use the findings of the SPA's actuaries, which include an associated third party claims administrator's loss estimates for large catastrophes. The claims administrator, together with loss modelling staff, base the selected estimate of losses for each large catastrophe after considering the range of ultimate loss estimates using various methods. Such methods include expected claim count and average cost per claim, incurred loss development, stochastic event scenario modelling from different software vendors, market share analysis, and other information, including independent third party evaluations. For smaller catastrophes and all other property perils, the SPA's actuaries apply Initial Expected Loss Ratios (IELRs) for each class of business, which is segmented by homogeneous regions and policy types. The SPA's actuaries develop these IELRs against catastrophe models, market data, and past claims on similar classes of business.

The provision for claims outstanding is subject to significant variability. While the directors believe that the recorded provision for gross claims and reinsurance recoveries is adequate, establishing this liability is a judgmental and inherently uncertain process. Therefore, it is possible that actual losses may not conform to the assumptions that the directors used in determining the amount of this provision. Accordingly, the ultimate provision may be significantly greater or less than the outstanding amount held at the balance sheet date. The SPA recognises adjustments to the provision for claims outstanding in the profit and loss account when known. The nature of short tail claims, such as the property insurance that the reinsured syndicate provides, where policyholders typically notify the reinsured syndicate of their claims within an average of 30 days and the reinsured syndicate typically settles these claims within a short time period which is normally less uncertain after a few years than long tail risks, such as some liability lines of business, where it may be several years before policyholders advise their insurance carriers of their claims and the carriers settle them.

The directors base the reinsurers' share of the provision for claims outstanding on the provisions for reported claims and IBNR, net of estimated irrecoverable amounts from potential reinsurer insolvencies based on the type of balance and security ratings of the involved reinsurers. The directors use statistical methods to help them make these estimates.

Accounting policies continued

Claims handling expenses

Claims handling expenses mostly consist of fees to an associated third party claims administrator for the handling of claims. In exchange for these services, the claims administrator charges a base fee equal to a percentage of gross premiums written. The base fee gives the SPA access to the claims administrator's staff for the administration of claims; it also entitles the SPA to a predetermined number of new claim file allowances. To the extent that actual claim volume exceeds the accumulated claim file allowances under the base fee, the claims administrator charges an additional fee for each additional claim.

This claims administration arrangement contains multiple deliverables, each representing a separate unit of accounting. As such, the SPA defers the portion of fees attributable to new claim file allowances based on their selling prices (contract rates) until actual claims are reported against them, or the allowances expire, whichever occurs first. If an actual claim is reported against a claim file allowance, the SPA recognises the allowance expense over the period that the claim is administered based on historical settlement patterns. If a claim is not reported against a claim file allowance before the allowance expires, the SPA includes the allowance in the profit and loss account when the allowance expires. The SPA defers the rest of the base fee (for access to staff and infrastructure) and recognises it as expense evenly over the term of services. The SPA includes deferred claims handling expenses in other prepayments and accrued income.

Acquisition costs, net of reinsurance

Acquisition costs consist of ceding commissions on inward reinsurance acceptances. The SPA defers acquisition costs to the extent that they are attributable to unearned premiums at the balance sheet date and expenses them as it earns the underlying insurance contract premiums. The SPA includes acquisition costs in net operating expenses.

Net operating expense

The SPA recognises operating expenses when incurred. Operating expenses include acquisition costs and the change in deferred acquisition costs, administrative expenses, and reinsurance commissions and profit participation. Administrative expenses consist of:

(i) operating costs,

(ii) Managing Agent fees,

(iii) Lloyd's membership costs, and

(iv) auditor fees.

Administrative expenses also include profit commissions charged by the Managing Agent. Profit commissions equal a percentage of each underwriting year's profits subject to a two-calendar-year deficit carry-forward provision. The SPA charges commissions to expense when incurred. The SPA recognises brokerage sharing when brokers place the reinsurance coverage.

Reinsurance commissions and profit participation consist of contingent profit commissions from reinsurers. The SPA accrues for contingent profit commissions based on the contract formulas. The SPA's contingent profit commission calculations include a provision for IBNR.

Accounting policies continued

Offsetting

The SPA sets off and presents its financial assets and liabilities net where:

(i) each it and another party owes the other determinable amounts,

(ii) it has the right to set off the amount owed with the amount owed by the other party,

(iii) it intends to set off, and

(iv) the right of setoff is enforceable at law.

Foreign currency translation

The Directors measure foreign currency assets and liabilities at the closing exchange rate in effect at the balance sheet date, while they measure foreign currency revenues and expenses at the historical exchange rates in effect at the time of the related transactions. The Directors used an exchange rate of 1.24 to translate Sterling balances into U.S. Dollars at 31 December 2016 (1.48 at 31 December 2015).

Taxation

Schedule 19 of the Finance Act 1993 does not require the Managing Agent to deduct basic rate income tax from the SPA's trading income. Therefore, payments of profits made to members of the SPA or their members' agents are gross of tax. Trading income includes capital appreciation, which is also paid gross of tax. The SPA did not make any provision for U.S. federal income tax payable on its underwriting results. The SPA's members pay these taxes alongside the U.K. income taxes resulting from the SPA's trading income. The SPA includes any tax payments made on account of its members during the year in members' balances.

3. Segmental analysis

The tables below detail the SPA's underwriting results before investment return by class of business.

2016	Gross premiums written	Gross premiums earned	Gross claims incurred	Gross operating expenses	Reinsurance balance	Total
	$'000	$'000	$'000	$'000	$'000	$'000
Reinsurance accepted	18,796	14,587	(3,220)	(4,769)	(8,474)	(1,876)

2015	Gross premiums written	Gross premiums earned	Gross claims incurred	Gross operating expenses	Reinsurance balance	Total
	$'000	$'000	$'000	$'000	$'000	$'000
Reinsurance accepted	6,613	1,857	(124)	(1,335)	(2,222)	(1,824)

Included in the reinsurance balance is reinsurance profit participation of $110,724 (2015: $11,998)

Surplus lines wholesale brokers pay fire and other damage to property premiums to the reinsured in single payments, while policyholders working through licensed retail agents pay premiums in single or multiple instalments to reinsured. The SPA's reinsurance agreement with the reinsured operates on a funds withheld basis, with the reinsured holding the SPA's funds for each underwriting year in premium trust funds for three years; after which, the reinsured remits these funds to the SPA.

The SPA only reinsures properties in the U.S.

4. Net operating expenses

	2016	2015
	$000	$000
Acquisition costs	5,313	1,833
Change in deferred acquisition costs	(1,201)	(1,323)
Administration expenses	657	825
Reinsurance commissions and profit participation	(111)	(12)
Total	4,658	1,323

This table details administrative expenses included in net operating expenses.

	2016	2015
	$000	$000
Operating costs (includes Managing Agent recharges)	164	282
Managing Agent fees	503	500
Lloyd's membership costs	144	70
Auditor remuneration – audit fees	80	76
Legal and professional fees	77	2
Brokerage sharing	(311)	(105)
Total	657	825

Managing Agent fees consist of service fees paid or payable to the Managing Agent. Auditor fees were primarily for the audit of the SPA's annual accounts and the audits of the Lloyd's regulatory returns. Audit fees also include fees for the SPA's half year review of $26,144. Non audit fees of $3,375 are for the actuarial review of the SPA's technical provisions and the preparation of the statements of actuarial opinion.

5. Key management personnel compensation

The directors did not receive any compensation for their services during the year, nor did the directors participate on the SPA or have an interest in any of its contracts.

The Managing Agent employed an average of 10 people that worked for the SPA. The Managing Agent recharged the SPA for the payroll costs of one of these employees. Service fees to the Managing Agent as part of their Managing Agent fees included compensation for the other employees.

International Catastrophe Insurance Managers, LLC (ICAT Managers), a Delaware company, underwrites most of the Syndicate's insurance business. Boulder Claims, LLC (Boulder Claims), also a Delaware company and a wholly owned subsidiary of ICAT Managers (collectively ICAT), provides claims administration services to the SPA. The SPA's staff compensation expense includes reimbursements to ICAT Managers for the recharged portion their underwriting and operations staff's salaries.

This table details the payroll recharges, included in administrative expenses under operating costs, to the SPA by category.

	2016	2015
	$000	$000
Wages and salaries	21	17
Social security costs	2	1
Total	23	18

Compensation to the Active Underwriter accounted for $11,873 (2015: $13,752) of the total payroll recharges.

6. Technical provisions

	2016 Gross provisions $'000	2016 Reinsurance assets $'000	2016 Net $'000	2015 Gross provisions $'000	2015 Reinsurance assets $'000	2015 Net $'000
Claims outstanding						
Balance at 1 January	97	-	97	-	-	-
Claims incurred during current underwriting year	2,439	-	2,439	109	-	109
Paid claims during the year	-	-	-	(12)	-	(12)
Balance at 31 December	**2,536**	**-**	**2,536**	**97**	**-**	**97**
Unearned premiums						
Balance at 1 January	4,756	(958)	3,798	-	-	-
Change in unearned premiums	4,209	(926)	3,283	4,756	(958)	3,798
Balance at 31 December	**8,965**	**1,883**	**7,081**	**4,756**	**(958)**	**3,798**
Deferred acquisition costs						
Balance at 1 January	1,323	-	1,323	-	-	-
Change in deferred acquisition costs	1,201	-	1,201	**1,323**	**-**	**1,323**
Balance at 31 December	**2,524**	**-**	**2,524**	**1,323**	**-**	**1,323**

7. Other creditors

	2016 $000	2015 $000
U.S. federal excise taxes payable	73	25
Amounts due to others	45	77
Total	118	102

8. Related parties

Asta Managing Agency Ltd (Asta) is the SPA's Managing Agent.

This table details amounts expensed or payable to Asta.

	2016	2015
	$000	$000
Managing Agent fees on insurance capacity	238	117
Managing Agent Service fee	265	383
Recharges (expenses)	20	-
Total expenses	523	500
Balance payable (including expenses accrued but not yet due) to the Managing Agent at 31 December	31	22

Fees to ICAT for claims administration services totalled $115,600 (2015: $62,435). ICAT provides accounting and capital modelling services to the SPA for an annual fee of $100,000 (2015: $75,000).

ICAT is an indirect subsidiary of Paraline Group, Ltd (Paraline Group), a company registered in Bermuda that also provided 10.0% (2015: 10%) of the SPA's insurance capacity through its indirectly owned ICAT corporate member. An unrelated foreign reinsurer fully supports the ICAT corporate member's participation.

From time to time, syndicates managed by Asta enter into (re)insurance contracts with one another. All such transactions are subject to Asta's internal controls which ensure that all are compliant with Lloyd's Related Party Byelaw provisions. All transactions are entered into on an arms length basis.

The table below details the percentage of total Syndicate capacity provided by other parties for the 2016 underwriting year.

	2016	2015
Hampden Agencies Limited (MAPA 7217)	19.9%	19.9%
IAT CCM Limited	20.0%	20.0%
Labuan Re Underwriting Limited	20.0%	20.0%
Nomina (No. 1253) Limited	0.1%	0.1%
Securis LCM Limited	15.0%	15.0%
Taiping Re UK Ltd	15.0%	15.0%
Total	90.0%	90.0%

Paraline CCM Limited, an indirectly owned Lloyd's corporate member of Paraline Group, is the beneficiary of a catastrophe reinsurance brokerage sharing agreement with the SPA. The balance payable (including amounts accrued but not yet due) to Paraline CCM Limited was $43,908 at 31 December 2016 (2015: $77,391).

Related parties continued

Paraline International, a wholly owned subsidiary of Paraline Group, owns 30.21% (2015: 30.21%) of Asta's ultimate parent, Asta Capital Limited, a company incorporated in the U.K. and registered in England and Wales. Asta has an agreement with Paraline International to review and monitor the adherence of ICAT to the SPA's underwriting guidelines. No contingent commissions were paid or payable to Paraline International for this oversight because the SPA generated a loss of the financial year.

Pursuant to an inter-syndicate loan deed between the reinsured and the SPA, the reinsured may advance up to $10.0 million to the SPA (2015: $10 million); such advances accrue interest at an annual rate equal to the greater of:

(a) the Six Month U.S. Treasury Bill rate at the date of the advance, or

(b) the Syndicate's average investment yield earned during the period of the advance.

At 31 December 2016, the SPA had a loan payable balance to reinsured of $5.8 million (2015: $3.3 million) measured at cost. The reinsured also owed the SPA $6.8 million at 31 December 2016 (2015: $1.9 million).

During 2016 Asta was the managing agent for eight Syndicates and three Special Purpose Arrangements. Syndicate 1686, 1729, 1897, 1910, 2357, 2525, 2786 and 4242 as well as Special Purpose Arrangements 6117, 6123 and 6126 were managed on behalf of third party capital providers.

On 7 February 2017, Syndicate 1910 and Special Purpose Arrangement 6117 migrated to Argo Managing Agency Limited.

On 1 January 2017, Asta took on management of Syndicate 2689 and Syndicate 5886.

The agency also provides administrative services to Syndicates and undertakes a number of ancillary roles for clients.

The Financial Statements of the Managing Agency can be obtained by application to the Registered Office (see page 1).

The syndicates that Asta manages may enter into reinsurance contracts with the SPA; these transactions are subject to Asta's internal controls, which ensure compliance with the Lloyd's Related Party Byelaw.

9. Funds at Lloyd's

The Society of Lloyd's (Lloyd's) requires every member of the SPA to hold capital in trust, known as Funds at Lloyd's, to support their supplied insurance capacity. Lloyd's intends for these funds to mainly cover the participating members' underwriting liabilities if the SPA's assets prove to be inadequate. Paraline Group's ICAT corporate member held $22.9 million of such funds in trust at 31 December 2016 (2015: $18.1 million). Since third parties supplied the rest of the funds, the directors did not disclose these funds in the accounts since they are not under the control of the Managing Agent or its affiliates; the Managing Agent, however, can make calls on these funds along with the funds provided by Paraline Group's ICAT corporate member to meet liquidity requirements or settle claims.

10. Contingent liabilities

The SPA is regularly involved in legal proceedings in the ordinary course of business. The directors believe the outcome of these proceedings will not have a material adverse effect on the SPA's financial condition or future profitability.

11. Risk management

a) Governance framework

The SPA's risk and financial management framework aims to protect member capital from events that might otherwise prevent the SPA from meeting its policyholder obligations, while maximising the returns to its members. The Directors recognise the critical importance of having efficient and effective risk management systems and processes in place.

Asta maintains a risk management function for the SPA with clear terms of reference from the Board that it appoints and from the Board's committees and subcommittees; Asta supplements this with a clear organisational structure with documented authorities and responsibilities from the Board to ICAT, who performs a majority of the SPA's activities. Lastly, the SPA policy framework sets its risk management and control and business conduct standards for operations. Asta reviews and monitors each policy to ensure compliance with the policy throughout the SPA and by ICAT.

The Board approves the SPA's risk management policies and meets regularly to approve any commercial, regulatory, or 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 the underwriting and reinsurance strategies to the SPA's goals, and specify any reporting requirements. The Board places significant emphasis on the assessment and documentation of risks and controls, including the quantification of the SPA's risk appetite.

b) Capital management

Capital framework at Lloyd's

The Prudential Regulatory Authority (PRA) under the Financial Services and Markets Act 2000, and in accordance with the Solvency II Framework, regulates Lloyd's.

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

Although, as described below, 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, not at the syndicate level, Accordingly, the directors have not disclosed a capital requirement for the SPA in these accounts.

Risk management continued

Lloyd's capital setting process

In order to meet Lloyd's requirements, each syndicate must calculate its Solvency Capital Requirement (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 the requirements of Solvency II. The Lloyd's Capital and Planning Group reviews and approves the SCRs of each syndicate.

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 syndicates on which it is participating, but not other members' shares. Accordingly, the capital requirements that Lloyd's sets for each member operate on a similar basis. Lloyd's determines each member's SCR by the sum of the member's share of the syndicate SCR 'to ultimate'. Where a member participates on more than one syndicate, Lloyd's gives a credit for diversification to reflect the spread of risk, but consistent with determining an SCR which reflects the capital requirement to cover a 1 in 200 loss 'to ultimate' for that member. Over and above this, Lloyd's applies a capital uplift to the member's capital requirement, known as the Economic Capital Assessment (ECA). The purpose of this uplift, which is a requirement of Lloyd's not Solvency II, is to meet Lloyd's financial strength, license, and ratings objectives. The capital uplift applied for 2016 was 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 (Funds at Lloyd's), assets held 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, the ending members' balances reported in the Statement of Changes in Members' Balances on page 19, represent resources available to meet members' and Lloyd's capital requirements.

c) Insurance risk

Insurance risk may either arise from an inaccurate assessment of the risks entailed in writing an insurance policy or from factors wholly out of the SPA's control. As a result, losses paid by the SPA may exceed earned premiums. The SPA tries to reduce insurance risk by basing its risk appetite on its maximum loss tolerance, geographically diversifying its business, and using appropriate underwriting processes, which include inspections of every property, to guide the pricing and acceptance of risks; this helps to ensure that premiums cover the expected levels of loss.

The SPA sets its tolerance for catastrophe losses based on nationwide and regional Exceedance Probabilities (EP) in the U.S., as well as on Realistic Disaster Scenarios (RDS) designed to stress test the SPA for material catastrophe risks at different probability levels by potential loss of capital. The EP is the probability that losses exceed a certain threshold for a catastrophic loss event at a selected probability of occurrence. The SPA generally quantifies its risk appetite at the 99.5% EP level or the 1 in 200 year loss.

ICAT developed the catastrophe model that the SPA uses to set its overall EP loss exposure limits by adjusting a model from a major vendor to better align it to the SPA's assessment of risk. ICAT's model adjustment methodology more precisely estimates building vulnerability, storm surge coverage leakage, losses from inland risks and coastal risks, and landfall frequency and severity than the standard vendor model. The SPA validates the results from

Risk management continued

ICAT's methodology against alternate models from other major vendors. ICAT uses its model adjustment methodology to model every property in the reinsured's book of business monthly. In managing the SPA's risk appetite, ICAT allocates limits to various geographic zones. The identification and determination of each zone and its area as well as whether to include a particular policy within a zone's limits requires significant judgment. ICAT controls and limits the reinsured's concentration of risk within these zones as well as the risk at the neighbourhood and street level using an accumulation tool.

The SPA monitors EP estimated gross losses and balances the offering of new and renewal accounts between low and high loss-driving areas. The SPA sets its tolerance for All Other Peril (AOP) losses at the building and location level. ICAT also monitors the SPA's loss exposures against its risk appetite using RDS modelling. RDS include the events below.

(i) Windstorm in the Northeastern U.S.

(ii) Windstorm in the Carolinas

(iii) Two separate Florida windstorms (Miami-Dade and Pinellas)

(iv) Windstorm in the U.S. Gulf

(v) Two separate California earthquakes (Los Angeles and San Francisco)

(vi) New Madrid area of the U.S. earthquake

(vii) Two separate Syndicate-specific scenarios (Mississippi windstorm and U.S. Pacific Northwest earthquake)

The table below shows the hypothetical estimated gross losses arising out of the RDS listed above based on the SPA's in-force exposures at 31 December 2016.

	Estimated gross losses $000
Windstorm in the North-eastern U.S.	24,435
Windstorm in the Carolinas	6,976
Florida windstorm (Miami-Dade)	38,277
Florida windstorm (Pinellas)	30,013
Windstorm in the U.S. Gulf	32,108
California earthquake (Los Angeles)	26,454
California earthquake (San Francisco)	18,899
New Madrid area of the U.S. earthquake	6,361
Syndicate-specific scenario (Mississippi windstorm)	12,027
Syndicate-specific scenario (U.S. Pacific Northwest earthquake)	19,479

Also, the SPA periodically evaluates and adjusts its reinsurance protection to manage its overall retention of insurance risk. The SPA has layered catastrophe reinsurance from a diversified group of secure reinsurers among other reinsurance to protect it against an adverse accumulation of the losses from multiple policies as a result of catastrophic events, each with losses of up to $109.0 million (2015: $43.0 million), $163.0 million in the aggregate (2015: $68.0 million). This reinsurance helps to limit the SPA's risk of insolvency from a single large catastrophe or multiple smaller catastrophes.

Risk management continued

Under a binding authority agreement with the reinsured, ICAT underwrites most of the reinsured's business. ICAT sets and controls the underwriting authority of each of its underwriters. Underwriters adhere to daily monitored regional blueprints, which identify where the reinsured's insurance capacity should be deployed. These blueprints, with their defined underwriting guidelines alongside modelling and pricing practices, determine the prescribed range of rates at which ICAT may sell the reinsured's insurance capacity. Underwriters must refer underwriting decisions for risks outside of those outlined in the blueprints or in excess of their authority limit to higher levels of authority. ICAT audits the individuals who have binding authority on a regular basis to ensure adherence to established underwriting authority limits. ICAT also conducts other underwriting audits on an ad-hoc basis and reviews significant risks written each month. Asta also has its own controls.

Asta has a governance structure in place to monitor the underwriting and loss exposure management controls of ICAT. The Board ensures the appropriate management of the SPA in accordance with the Managing Agent's responsibilities. The Board meets quarterly and has delegated authority to approve underwriting related matters, including:

(i) Non-material changes to the business plan,

(ii) underwriting authority levels and guidelines,

(iii) operational and ICAT procedures,

(iv) risk policies, the risk register, and all other risk management matters, and

(v) the SPA's compliance plan.

Asta also monitors the SPA's performance against its underwriting risk appetite in several ways, including regular meetings with the Active Underwriter and participation in the monthly meetings of the Production Risk Management Committee (the Committee), which is a subcommittee of the Board, that considers reports from the Active Underwriter and other areas of the business. The Committee also reviews underwriting related matters, including:

(i) progress against the business plan or forecast,

(ii) premium rates and volumes,

(iii) overall loss exposures,

(iv) significant product and premium rate changes;

(v) market conditions, and

(vi) the outcome of underwriting audits covering the operations of ICAT.

Furthermore, Paraline International provides oversight of the underwriting policies adopted by the Active Underwriter. Paraline International identifies key underwriting guidelines and limitations in the binding authority agreement between ICAT and the reinsured and monitors ICAT adherence to these underwriting guidelines including consideration of material changes in underwriting authority, risk profile, reinsurance, and any breaches of the ICAT binding authority agreement.

Risk management continued

The SPA's annual business planning process sets the targets for written premiums and overall profitability for the coming year. Factors taken into account in determining these targets include the risk appetite of the SPA's capital providers, anticipated pricing, insurance policy terms and conditions, and other risk metrics.

The SPA hires qualified third party claims administrators that have specialised adjusters and forensic engineers to set reserves on notified damaged properties and incidental liability claims. Both ICAT and Asta review these reported claims monthly. The SPA also employs standard actuarial methods to assess its overall best estimate of reserves for each underwriting account quarterly using historical losses loaded for future uncertainty in areas where reserves may prove to be materially inadequate; this assessment process requires ongoing discussions between the SPA's actuaries and the underwriters and claims adjusters of ICAT, and includes various levels of approval supplemented by external actuarial validation. The SPA's actuaries track projected loss ratios quarterly and may reassess their reserving methods if necessary. The Board approves the reserves of the SPA quarterly, after considering the recommendation of the Reserve Committee (a subcommittee of the Board).

The tables below detail the SPA's liabilities for claims outstanding by class of business.

	2016		
	Gross $000	Reinsurance $000	Net $000
Reinsurance accepted	2,537	-	2,537

	2015		
	Gross $000	Reinsurance $000	Net $000
Reinsurance accepted	98	-	98

The liabilities in the tables above may be significantly greater or less than the ultimate cost of settling the associated claims; this level of uncertainty varies by class of business. The Syndicate considers a five percent increase or decrease in the ultimate cost of settling its outstanding claim liabilities reasonably possible at the balance sheet date.

The table below show how a five percent increase or decrease in net claim liabilities would affect the SPA's profit for the financial year and its members' balances.

	2016	
	Five percent increase	Five percent decrease
	$000	$000
Reinsurance accepted	(127)	127

	2015	
	Five percent increase	Five percent decrease
	$000	$000
Reinsurance accepted	(5)	5

Risk management continued

The table below shows the SPA's cumulative incurred claims development, including both claims notified and IBNR for each underwriting year, together with the cumulative payments to date on a gross and net of reinsurance basis at the balance sheet date.

	2015	2016	
Underwriting year	**$000**	**$000**	**Total**
Estimate of cumulative claims incurred:			
At end of underwriting year	110	2,080	2,080
One year later	1,127		1,127
Less cumulative paid	(420)	(250)	(670)
Liability for gross outstanding claims (2015 to 2016)	707	1,830	2,537
Total			2,537

d) Financial risk

(i) Market Risk

Market risk is the risk that the fair value or future cash flows of the SPA's financial assets will fluctuate because of changes in the market. Market risk consists of the following three risks; interest rate risk, currency risk and investment price risk (page 8).

(ii) Credit Risk

Credit risk is the risk that other parties fail to honor their obligations to the reinsured and the reinsured in turn fails to honor its obligations to the SPA (page 9).

Risk management continued

The table below shows the maximum exposure that the SPA's assets have to credit risk.

2016	$'000			
	Neither past due nor impaired	Past due	Impaired	Total
Debtors arising out of reinsurance operations	-	-	-	-
Other debtors	10,068	-	-	10,068
Total	10,068	-	-	10,068

2015	$'000			
	Neither past due nor impaired	Past due	Impaired	Total
Debtors arising out of reinsurance operations	4,359	-	-	4,359
Other debtors	106	-	-	106
Total	4,465	-	-	4,465

The tables below classify the exposure that the SPA's assets have to credit risk by the Standard & Poor's credit ratings of the investments and parties involved.

2016	$'000				
	AAA	AA	A	Not Rated	Total
Debtors arising out of reinsurance operations	-	-	-	-	-
Other debtors	-	-	-	10,068	10,068
Total	-	-	-	10,068	10,068

2015	$'000				
	AAA	AA	A	Not Rated	Total
Debtors arising out of reinsurance operations	-	-	4,359	-	4,359
Other debtors	-	-		106	106
Total	-	-	4,359	106	4,465

Risk management continued

(iii) Liquidity risk

The reinsured pays insurance claims and other liabilities on the SPA's behalf in accordance with the funds withheld and inter-syndicate loan arrangements that SPA has with the reinsured. The SPA's operations, however, could be adversely affected if the reinsured did not have enough cash to pay the SPA's obligations. The reinsured tries to reduce this risk by reviewing its expected cash obligations on a quarterly basis and keeping adequate cash on deposit to meet those obligations. The reinsured settles the SPA's payment obligations in accordance with the vendor terms of each transaction. The reinsured holds any excess funds in cash or invests them in money funds readily convertible to cash without excessive cost to the business. The reinsured also has a $35.0 million (2015: $35.0 million) letter of credit facility from Barclays Bank PLC.

The table below summarises the SPA's future expected cash obligations on its undiscounted liabilities, including payments of its outstanding claim liabilities based on historical settlement patterns.

2016			**$'000**		
	Up to a year	**1-3 years**	**3-5 years**	**More than 5 years**	**Total**
Claims outstanding	1,613	813	110	-	2,536
Creditors arising out of reinsurance operations	2,035	-	-	-	2,035
Inter-syndicate loan	-	-	-	-	-
Other creditors	118	-	-	-	118
Total	3,766	813	110	-	4,689

2015			**$'000**		
	Up to a year	**1-3 years**	**3-5 years**	**More than 5 years**	**Total**
Claims outstanding	88	9	1	-	98
Creditors arising out of reinsurance operations	164	-	-	-	164
Inter-syndicate loan	-	3,320	-	-	3,320
Other creditors	102	-	-	-	102
Total	354	3,329	1	-	3,684

12. Subsequent events

The Directors evaluated other events subsequent to the balance sheet date through 21 March 2017, the date the SPA issued these annual accounts, and determined that no other items require disclosure.