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Beat Special Purpose Arrangement 6123

Annual Report and Accounts
31 December 2018

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Directors and administration

Managing Agent

Asta Managing Agency Ltd

Directors

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

*Non-Executive Directors

Company Secretary

N J Burdett

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	(Resigned 01 March 2018)
S P A Norton	(Appointed 01 March 2018 – Resigned 09 April 2018)
P M Rayner	(Appointed 09 April 2018 – Resigned 01 November 2018)
A J T Milligan	(Appointed 01 November 2018)

Registered Auditors

KPMG LLP

Signing Actuary

P Chappell, KPMG LLP

Managing Agent's report

The Special Purpose Arrangement's ("SPA") Managing Agent (The Agency) is a company registered in England and Wales. The directors of the Managing Agent present their report for the year ended 31 December 2018.

This annual report is 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 ("Lloyd's Regulations 2008").

Results

The total recognised result for calendar year 2018 is a loss of \$14,767,902 (2017: loss of \$8,493,264).

The SPA presents its results under FRS102, the Financial Reporting Standard applicable in the UK and Republic of Ireland. In accordance with FRS102, the Syndicate has identified its insurance contracts and accounted for them in accordance with FRS103.

Principal activity and review of the business

The SPA was established in May 2015 to underwrites a variable quota share of Syndicate 4242.

All policies reinsured by the SPA are underwritten by Syndicate 4242 in association with ICAT Managers (LLC). ICAT Managers underwrites through a network of relationships with surplus line wholesale brokers and licensed retail agents. It specialises in underwriting property insurance located in areas of the United States (U.S.) that are prone to hurricanes and earthquakes. Coverage includes natural catastrophe perils, All Other Perils ("AOP"), general liability, equipment breakdown and limited flood coverage.

The portfolio comprises small commercial properties underwritten by Syndicate 4242. The cession to SPA 6123 is determined by the characteristics and location of the risks. The parameters for such cession being determined in accordance with the targeted delivery of the SPA's business plan. The portfolio is derived from the 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)

Beat Capital Partners Ltd ("Beat"), a long-term venture capital fund focused on the insurance industry, became the corporate sponsor of Syndicate 4242 and the SPA during 2018 through a transaction to acquire Paraline UK (Group) Ltd, a company that holds certain capital and operational rights in respect to the Syndicate and SPA.

Boulder Claims provides claims administration services to Syndicate 4242 in respect to the SPA subject portfolio. The Managing Agent contracts with a third party to coordinate oversight of Boulder Claims.

Managing Agent's report continued

Total authorised underwriting capacity for the SPA for 2018 was £20.0 million (2017: £15.0 million). Underwriting capacity is a measure of the maximum gross premiums, net of acquisition costs that the SPA is eligible to write; the SPA in 2018 wrote \$18.6 million (\$12.6 million in 2017) in such premiums.

Gross written premium income by class of business for the calendar year was as follows;

	2018 \$'000	2017 \$'000
Gross written premiums:		
Eastern Seaboard	5,074	4,007
Florida	9,157	6,025
Gulf Coast	4,009	2,615
Hawaii	28	3
Earthquake	7,681	5,016
	25,949	17,666

The SPA's key financial performance indicators during the year were as follows;

	2018 \$'000	2017 \$'000
Gross written premiums	25,949	17,666
Loss for the financial year	(14,768)	(8,493)
Net loss ratio*	169.2%	119.8%
Combined ratio*	231.4%	170.5%

*The net loss ratio is the ratio of net claims incurred to net premiums earned, while the combined ratio is the ratio of net claims incurred and net operating expenses to net premiums earned. Lower ratios represent better performance.

The SPA has material natural catastrophe exposure and hence the loss ratios particularly reflect the impacts of Hurricanes Harvey and Irma to the 2017 calendar year (impacting the 2016 and 2017 years of account) and Hurricanes Michael and Florence to the 2018 calendar year (impacting the 2017 and 2018 years of account).

The return on capacity for the 2016 closed year of accounts at 31 December 2018 is shown below, together with forecasts for the two open years of account.

	2018 Open \$'000	2017 Open \$'000	2016 Closed \$'000
Capacity	25,400	19,050	19,050
Loss	(11,578)	(11,246)	(4,164)
Return on insurance capacity	(45.6%)	(59.0%)	(21.9%)

Managing Agent's report continued

Outward reinsurance arrangements

Catastrophe Coverage - The SPA has an 11% 'certain perils' quota share cover in place covering named windstorm and earthquake perils. The remaining 89% is subject to a layered catastrophe reinsurance to protect against the adverse accumulation of the losses from multiple policies as a result of large catastrophic events. The 2018 programme inceptioned at 1 June 2018 (a similar structure was also placed for 12 months inceptioning 1 June 2017).

All Other Peril Coverage – The SPA has per risk reinsurance to protect against the occurrence of losses from other perils such as large fires that impact upon the portfolio underwritten.

Principal risks and uncertainties

The Syndicate sets risk appetite annually, which is approved by the Agency as part of the Syndicate's business planning and Solvency Capital Requirement ('SCR') process. The Agency Risk and Solvency Committee meets at least quarterly to oversee the risk management framework. The Syndicate Board, a sub-committee of the Agency Board, reviews the risk profile as reflected in the risk register, and monitors performance against risk appetite using a series of key risk indicators. The principal risk and uncertainties facing the Syndicate are as follows:

Insurance risk

Insurance risk includes the risks that a policy will be written for too low a premium or provide inappropriate cover (underwriting risk), that the frequency or severity of insured events will be higher than expected (claims risk), or that estimates of claims subsequently prove to be insufficient (reserving risk). The Syndicate Board manages insurance risk through the approved business plan, which sets out targets for volumes, pricing, line sizes and retention by class of business. The Syndicate Board then monitors performance against the business plan through the year. Reserve adequacy is monitored through quarterly review by the Syndicate actuary and the Reserving Committee.

Credit risk

The key aspect of credit risk is reinsurance counterparty risk which is the risk of default by one or more of the Syndicate's reinsurers and intermediaries. The Syndicate Board's policy is that the Syndicate will only reinsure with approved reinsurers, supported by collateralisation, where required. The Agency Reinsurance Security Committee monitors reinsurer ratings and is required to approve all new reinsurers before business is placed with them.

Market risk

Market risk exposure impacting the SPA relates to fluctuations in interest rates or exchange rates. The SPA is exposed to foreign exchange movements as a result of mismatches between the currencies in which assets and liabilities are denominated. The Agency's policy is to maintain received income or incurred expenditure in the core currencies in which they were received or paid. Any surplus or deficit in a core currency would be subject to review by the Syndicate Board. Investments and cash are held on the SPA's behalf by the Host Syndicate in accordance with the funds withheld arrangement.

Managing Agent's report continued

Exposure to changes in interest rates comes from the Host Syndicate's investment portfolio. The Agency seeks to minimise this risk through investing in either fixed interest securities or high quality floating rate notes.

In addition, the Host Syndicate's Investment Committee, which reports to the Syndicate Board, ensures that the Syndicate's investment portfolio is managed by the external investment manager in accordance with the Syndicate's risk appetite and to guidelines as approved by the Syndicate Board.

The SPA writes the majority of its business in U.S. Dollars, which is its functional currency. The SPA incurs the majority of its expenses in Sterling; these expenses, however, do not create material currency risk for the SPA.

Liquidity risk

The Host Syndicate pays insurance claims and other liabilities (including expenses) on the SPA's behalf in accordance with the funds withheld arrangement. Cash calls can be made by the Host Syndicate on the SPA under certain circumstances.

The SPA has called on Capital Providers of the 2016, 2017 and 2018 years of account.

Operational risk

This is the risk that errors caused by people, processes, systems and external events lead to losses to the SPA. The Agency seeks to manage this risk through the use of an operational risk and control framework throughout the SPA, detailed procedures manuals and a structured programme of testing of processes and systems by internal audit. Business continuity and disaster recovery plans are in place and are regularly updated and tested.

Regulatory risk is the risk of loss owing to a breach of regulatory requirements or failure to respond to regulatory change. The Agency is required to comply with the requirements of the Financial Conduct Authority (FCA), Prudential Regulatory Authority (PRA) and Lloyd's. Lloyd's requirements include those imposed on the Lloyd's market by overseas regulators, particularly in respect of US situs business. The Agency has a compliance officer who manages a team of four that monitor business activity and regulatory developments and assesses any effects on the Agency.

The SPA has no appetite for failing to treat customers fairly. The SPA manages and monitors its conduct risk through a suite of risk indicators and reporting metrics as part of its documented conduct risk framework.

Group / strategic risk

This is the risk of contagion that arises from being associated with key stakeholders and the impact that activities and events that occur within other connected or third parties has on the business.

Strategic risk covers the risks faced by the SPA due to changes in underlying strategy of the business or that of its key stakeholders (including strategic conflicts of interest).

Managing Agent's report continued

Future developments

The SPA insurance capacity to write business has increased to £35 million for the 2019 underwriting year (2018: £20 million).

Significant uncertainty remains associated with the UK's planned exit from the European Union. The risks to UK economic growth remain significant as the terms of the UK's exit from the EU remain unclear. The SPA does not consider its business to be directly susceptible to the risks posed by the UK's exit from the EU.

To mitigate the risk of losing access to EEA business and mitigate the impact of the Lloyd's syndicates losing EEA passporting rights, Lloyd's have set up an EU regulated insurance company (LIC) in Brussels to underwrite EEA-exposed business from 1 January 2019. This is a fully operational, capitalised insurance company under Solvency II. It is authorised and regulated by the National Bank of Belgium and regulated by the Financial Services and Markets Authority and licensed to write non-life risks across the EEA and the UK.

Writing business via Lloyd's Brussels has necessitated a number of operational changes that syndicates have had to make to enable them to be able to write EEA business via a reinsurance arrangement with LIC. The Managing Agency has been working with the Syndicate to implement these changes to ensure that the Syndicate is set up to write business via Lloyd's Brussels from 1 January 2019.

Directors

Details of the directors of the Managing Agent that were serving at the year end and up to the date of signing of the SPA annual accounts are provided on page 1. Changes to the directors were as follows:

R P Barke	Appointed 1 January 2018
P A Jardine	Appointed 1 November 2018
R A Stevenson	Appointed 1 November 2018
C Chow**	Resigned 28 February 2019
N J Burdett**	Appointed 01 March 2019

Company Secretaries**

Disclosure of information to the auditors

So far as each person who was a director of the Managing Agent at the date of approving the report is aware, there is no relevant audit information, being information needed by the SPA auditor in connection with the auditor's report, of which the auditor is unaware. Having made enquiries of fellow directors of the Agency and the SPA's Auditors, 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 SPA's auditor is 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 auditor will be deemed to be reappointed and KPMG LLP will therefore continue in office.

Managing Agent's report continued

SPA Annual General Meeting

In accordance with the Syndicate Meetings (Amendment No 1) Byelaw (No 18 of 2000) the Managing Agent does not propose holding an annual meeting this year; objections to this proposal or the intention to reappoint the auditors for a further 12 months can be made by SPA members before 26 April 2019.

On behalf of the Board

A handwritten signature in black ink, appearing to read 'N J Burdett', with a stylized flourish at the end.

N J Burdett
Company Secretary
22 March 2019

Statement of Managing Agent's responsibilities

The directors of the managing agent are responsible for preparing the Syndicate annual accounts in accordance with applicable law and regulations.

The Insurance Accounts Directive (Lloyds's Syndicate and Aggregate Accounts) Regulations 2008 requires the directors of the managing agent to prepare their Syndicates annual accounts for each financial year. Under that law they have elected to prepare the annual accounts 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 directors of the managing agent must not approve the annual accounts 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 directors of the managing agent 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 annual accounts; and
- assess the syndicate's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to cease trading, or have no realistic alternative but to do so.

The directors of the managing agent 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 are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and 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 directors of the managing agent 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

Opinion

We have audited the financial statements of Syndicate 6123 for the year ended 31 December 2018 which comprise the Statement of profit or loss: technical account – General business, Statement of profit or loss: Non-technical account, Statement of financial position, Statement of changes in members' balances, Statement of cash flows and related notes, including the accounting policies in note 2.

In our opinion the financial statements:

- give a true and fair view of the state of the syndicate's affairs as at 31 December 2018 and of its loss for the year then ended;
- have been properly prepared in accordance with UK accounting standards, including FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*; and
- have been prepared in accordance with the requirements of the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We have fulfilled our ethical responsibilities under, and are independent of the syndicate in accordance with, UK ethical requirements including the Financial Reporting Council ("FRC") Ethical Standard. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

Going concern

The directors of the Managing Agent have prepared the Annual Return on the going concern basis as they do not intend to liquidate the syndicate or to cease its operations, and as they have concluded that the syndicate's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over its ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least a year from the date of approval of the financial statements. In our evaluation of the directors' conclusions, we considered the inherent risks to the syndicate's business model, including the impact of Brexit, and analysed how those risks might affect the syndicate's financial resources or ability to continue operations over the going concern period. We have nothing to report in these respects.

However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the syndicate will continue in operation.

Independent auditor's report continued

Report of the directors of the Managing Agent

The directors are responsible for the Report of the directors of the Managing Agent. Our opinion on the financial statements does not cover that report and we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the Report of the directors of the Managing Agent and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work we have not identified material misstatements in that report.

In our opinion the information given in the Report of the Directors of the Managing Agent is consistent with the financial statements.

Matters on which we are required to report by exception

Under the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008, we are required to report to you if, in our opinion:

- adequate accounting records have not been kept; or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

Responsibilities of the Directors of the Managing Agent

As explained more fully in their statement set out on page 8, the directors of the Managing Agent are responsible for: the preparation of the financial statements and for being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the syndicate's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to cease trading, or have no realistic alternative but to do so.

Independent auditor's report continued

Auditor's responsibilities

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

The purpose of our audit work and to whom we owe our responsibilities

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 company and the syndicate's members, as a body, for our audit work, for this report, or for the opinions we have formed.



Timothy Butchart (Senior Statutory Auditor)
For and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
London
22 March 2019

Statement of profit or loss

Technical account - General business

For the year ended 31 December 2018

	Notes	2018 \$'000	2017 \$'000
Gross premiums written	3	25,949	17,666
Outward reinsurance premiums		<u>(12,176)</u>	<u>(7,529)</u>
Net written premiums		13,773	10,137
Change in the provision for unearned premiums			
• Gross amount		(3,427)	2,767
• Reinsurers' share		<u>914</u>	<u>(831)</u>
Change in the net provision for unearned premiums	4	(2,513)	1,936
Earned premiums, net of reinsurance		11,260	12,073
Allocated investment return transferred from the non-technical account		40	9
Claims paid			
• Gross amount		(26,634)	(6,635)
• Reinsurers' share		<u>9,124</u>	<u>736</u>
		(17,510)	(5,899)
Changes in claims outstanding			
• Gross amount		(54,167)	(16,077)
• Reinsurers' share		<u>52,620</u>	<u>7,507</u>
Change in the net provision for claims		(1,547)	(8,570)
Claims incurred, net of reinsurance	4	(19,057)	(14,469)
Net operating expenses	5	<u>(7,004)</u>	<u>(6,112)</u>
Balance on technical account – general business		<u>(14,761)</u>	<u>(8,499)</u>

All the amounts above are in respect of continuing operations.

The notes on pages 18 to 37 form part of these financial statements.

Statement of profit of loss continued

Non-technical account

For the year ended 31 December 2018

	Notes	2018 \$'000	2017 \$'000
Balance on technical account – general business		(14,761)	(8,499)
Investment income	8	33	11
Unrealised gains on investments		2	1
Unrealised losses on investments		-	(1)
Gains on realisation of investments		8	-
Investment expenses and charges		(3)	(2)
Allocated investment return transferred to the general business technical account		(40)	(9)
Other income - (loss) / profit on exchange		(7)	6
Loss for the financial year		<u>(14,768)</u>	<u>(8,493)</u>

There were no recognised gains and losses in the year other than those reported in the Statement of Profit or Loss and hence no Statement of Other Comprehensive Income has been presented.

All the amounts above are in respect of continuing operations. The notes on pages 18 to 37 form part of these financial statements.

Statement of changes in members' balances

For the year ended 31 December 2018

	2018 \$'000	2017 \$'000
Members' balances brought forward at 1 January	(12,253)	(3,728)
Total comprehensive loss for the year	(14,768)	(8,493)
Payments of loss from members	290	-
Cash call	7,500	-
Members' charges	<u>(24)</u>	<u>(32)</u>
Members' balances carried forward at 31 December	<u>(19,255)</u>	<u>(12,253)</u>

Members participate on Syndicates by reference to years of account (YOA) 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.

The notes on pages 18 to 37 form part of these financial statements.

Statement of financial position

As at 31 December 2018

	Notes	2018 \$'000	2017 \$'000
Assets			
<i>Reinsurers' share of technical provisions</i>			
Provision for unearned premiums	4	1,966	1,052
Claims outstanding	4	<u>60,127</u>	<u>7,507</u>
		62,093	8,559
<i>Debtors</i>			
Debtors arising out of reinsurance operations	9	<u>28,600</u>	<u>22,160</u>
		28,600	22,160
<i>Prepayments and accrued income</i>			
Deferred acquisition costs	4	2,729	1,761
Other prepayments and accrued income		<u>845</u>	<u>278</u>
		<u>3,574</u>	<u>2,039</u>
Total assets		<u>94,267</u>	<u>32,758</u>

The notes on pages 18 to 37 form part of these annual accounts.

Statement of financial position continued

As at 31 December 2018

	Notes	2018 \$'000	2017 \$'000
Members' balance and liabilities			
<i>Capital and reserves</i>			
Members' balances		(19,255)	(12,253)
<i>Liabilities</i>			
<i>Technical provisions</i>			
Provision for unearned premiums	4	9,625	6,198
Claims outstanding	4	<u>72,755</u>	<u>18,613</u>
		82,380	24,811
<i>Creditors</i>			
Creditors arising out of reinsurance operations	10	30,369	19,820
Other creditors		<u>115</u>	<u>169</u>
		30,484	19,989
<i>Accruals and deferred income</i>		<u>658</u>	<u>211</u>
<i>Total liabilities</i>		<u>113,522</u>	<u>45,011</u>
<i>Total members' balances and liabilities</i>		<u>94,267</u>	<u>32,758</u>

The notes on pages 18 to 37 form part of these annual accounts.

The financial statements on pages 12 to 37 were approved by board of directors on 19 March 2019 and were signed on its behalf by:



D J G Hunt
Director
22 March 2019

Statement of cash flows

For the year ended 31 December 2018

	Notes	2018 \$'000	2017 \$'000
Cash flows from Operating activities			
<i>Loss for the financial year</i>		(14,768)	(8,493)
Increase in gross technical provisions		57,569	16,077
(Increase) in reinsurers' share of gross technical provisions		(53,534)	(7,507)
(Increase) in debtors		(6,440)	(16,830)
Increase in creditors		10,495	17,836
Movement in other assets/liabilities/foreign exchange		(1,088)	(1,074)
Investment Return		<u>(40)</u>	<u>(9)</u>
<i>Net cash outflows from operating activities</i>		<u>(7,806)</u>	<u>-</u>
Cash from Investing activities			
Investment income received		<u>40</u>	<u>-</u>
<i>Net cash inflows from investing activities</i>		<u>40</u>	<u>-</u>
Cash from Financing activities			
Payments of loss from members' personal reserve fund		290	-
Cash calls in period		7,500	-
Members' agent fees in period		<u>(24)</u>	<u>-</u>
<i>Net cash inflows from financing activities</i>		<u>7,766</u>	<u>-</u>
Net increase in cash and cash equivalents		-	-
Cash and cash equivalents at beginning of year		<u>-</u>	<u>-</u>
Cash and cash equivalents at end of year		<u><u>-</u></u>	<u><u>-</u></u>

Notes to the financial statements

For the year ended 31 December 2018

1. Basis of preparation

Statement of compliance

The SPA comprises a group of members of the Society of Lloyd's that underwrites insurance business in the London Market. The address of the SPA's Managing Agent is stated on page 1.

The financial statements have been prepared in compliance with The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 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. The SPA's functional currency is USD. The financial statements are prepared in USD which is the reporting and presentational currency of the SPA and rounded to the nearest \$'000.

As permitted by FRS 103 the SPA 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).

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.

Accounting policies continued

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 its 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 are 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.

The directors assess the provision for unexpired risks by class of business. No provision for unexpired risks was recorded in 2018 (2017: 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.

Accounting policies continued

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.

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.

Accounting policies continued

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.

Offsetting

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

- (i) both 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.

Accounting policies continued

Investment return

Investment return comprises all investment income, realised investment gains and losses and movements in unrealised gains and losses, net of investment expenses, charges and interest.

Dividend income is recognised when the right to receive income is established. Usually this is the ex-dividend date for equity securities. Interest income on financial assets measured at amortised cost is recognised using the effective interest method. For the purpose of separately presenting investment income and unrealised gains and losses for financial assets at fair value through profit or loss, interest income is recognised as it accrues on the next coupon payment.

For investments at fair value through profit or loss, realised gains and losses represent the difference between the net proceeds on disposal and the purchase price. For investments measured at amortised cost, realised gains and losses represents the difference between the net proceeds on disposal and the latest carrying value (or if acquired after the last reporting date, the purchase price).

Unrealised gains and losses on investments represent the difference between the fair value at the balance sheet date and their purchase price. Movements in unrealised investment gains and losses comprise the increase/decrease in the reporting period in the value of the investments held at the reporting date and the reversal of unrealised investment gains and losses recognised in earlier reporting periods in respect of investment disposals of the current period, or the valuation at the beginning of the year, as well as the reversal of previously recognised unrealised gains and losses in respect of investments disposed of in the current period.

Investment return is initially recorded in the non-technical account. The return is transferred in full to the general business technical account to reflect the investment return on funds supporting underwriting business.

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 1.27 to translate Sterling balances into U.S. Dollars at 31 December 2018 (1.35 at 31 December 2017).

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.

Going concern

These financial statements have been prepared on a going concern basis, as the SPA will be continuing to underwrite business for the foreseeable future.

3. Segmental analysis

An analysis of the underwriting result before investment return is set out below:

2018	Gross written premiums	Gross premium earned	Gross claims incurred	Gross operating expenses	Reinsurance balance	Total
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Reinsurance accepted	25,949	22,522	(80,801)	(7,507)	50,985	(14,801)

2017	Gross written premiums	Gross premium earned	Gross claims incurred	Gross operating expenses	Reinsurance balance	Total
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
Reinsurance accepted	17,666	20,433	(22,711)	(6,532)	302	(8,508)

All premiums were concluded in the UK.

Included in the reinsurance balance is the reinsurance profit participation of \$0.5 million (2017: \$0.4 million) which has been reallocated from net operating expenses to provide the gross figures.

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 the 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. Technical provisions

2018	Gross provisions \$'000	Reinsurance assets \$'000	Net \$'000
Claims outstanding			
Balance at 1 January	18,613	(7,507)	11,106
Claims incurred during current underwriting year	80,801	(61,744)	19,057
Paid claims during the year	(26,634)	9,124	(17,510)
Balance RITC'd into 4242	(25)	-	(25)
Balance at 31 December	72,755	(60,127)	12,628
Unearned premiums			
Balance at 1 January	6,198	(1,052)	5,146
Change in unearned premiums	3,427	(914)	2,513
Balance at 31 December	9,625	(1,966)	7,659
Deferred acquisition costs			
Balance at 1 January	1,761	-	1,761
Change in deferred acquisition costs	968	-	968
Balance at 31 December	2,729	-	2,729
2017	Gross provisions \$'000	Reinsurance assets \$'000	Net \$'000
Claims outstanding			
Balance at 1 January	2,536	-	2,536
Claims incurred during current underwriting year	22,712	(8,243)	14,469
Paid claims during the year	(6,635)	736	(5,899)
Balance RITC'd into 4242	-	-	-
Balance at 31 December	18,613	(7,507)	11,106
Unearned premiums			
Balance at 1 January	8,965	(1,883)	7,082
Change in unearned premiums	(2,767)	831	(1,936)
Balance at 31 December	6,198	(1,052)	5,146
Deferred acquisition costs			
Balance at 1 January	2,524	-	2,524
Change in deferred acquisition costs	(763)	-	(763)
Balance at 31 December	1,761	-	1,761

5. Net Operating Expenses

	2018	2017
	\$'000	\$'000
Acquisition costs	(7,356)	(5,045)
Change in deferred acquisition costs	968	(763)
Administration expenses	(1,119)	(724)
Reinsurance commissions and profit participations	503	420
Net operating expenses	(7,004)	(6,112)

6. Auditor's remuneration

	2018	2017
	\$'000	\$'000
Fees payable to the Syndicate's auditor of these financial statements	(32)	(32)
Other services pursuant to Regulations and Lloyd's Byelaw	(78)	(78)
Other services relating to actuarial review	(13)	(13)
	(123)	(123)

Auditor's remuneration is included as part of the administrative expenses in note 5 to the financial statements.

7. Emoluments of the Directors of Asta Managing Agency Ltd

The aggregate emoluments of the directors and staff of the Managing Agency are met by Asta Managing Agency Ltd and are disclosed within the financial statements of that company, with the exception of J. M. Tighe, S.P.A. Norton, D.J.G. Hunt and L Harfitt. J.M. Tighe and S.P.A Norton's remuneration is disclosed in the financial statements of Asta Capital Ltd and the remuneration of D.J.G. Hunt and L Harfitt is disclosed in the financial statements of Asta Insurance Markets Ltd and were all charged in the accounts of Asta Managing Agency Ltd.

No emoluments of the directors or staff of Asta Managing Agency Ltd were directly charged to the SPA.

No other compensation was payable to key management personnel.

The Active Underwriter received the following aggregate remuneration, charged as an SPA expense:

	2018	2017
	\$'000	\$'000
Active Underwriter's emoluments	(33)	(12)
	(33)	(12)

8. Investment return

	2018	2017
	\$'000	\$'000
Bank interest	16	4
Income from Investments	22	7
Accrued interest on investments	(5)	-
Total investment income	33	11

The SPA operates on a funds withheld basis with its host, Syndicate 4242. As such, a portion of Syndicate 4242's investment return is allocated to the SPA to reflect the return on the funds withheld.

9. Debtors arising out of reinsurance operations

	2018	2017
	\$'000	\$'000
Due from ceding insurers (within one year)	8,837	5,730
Due from ceding insurers (after one year)	17,030	15,694
Due from reinsurers (within one year)	2,733	736
Total	28,600	22,160

10. Creditors arising out of reinsurance operations

	2018	2017
	\$'000	\$'000
Due to reinsurers (within one year)	12,740	4,124
Due to reinsurers (after one year)	17,629	15,696
Total	30,369	19,820

11. Related parties

Asta provides services and support to SPA 6123 in its capacity as Managing Agent. Asta's remuneration for the year was:

	2018	2017
	\$'000	\$'000
Managing Agent's fees on insurance capacity	241	176
Managing Agent's service fees	572	382
Recharge expenses	33	10
Total expenses	846	568
Amount outstanding at 31 December	276	44

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 arm's length basis.

The table below details the percentage of total Syndicate capacity provided by member for the two open underwriting years and the closing underwriting year.

	2018	2017	2016
Labuan Re Underwriting Limited	15.00%	20.00%	20.00%
IAT CCM Limited	20.00%	20.00%	20.00%
Securis LCM Limited	11.25%	15.00%	15.00%
Hampden Members	16.25%	20.00%	20.00%
Taiping Re UK Ltd	15.00%	15.00%	15.00%
Sompo Japan Nipponkoa (via Beat CCM 9 Ltd)	0.00%	10.00%	10.00%
Point Dume LLP	21.75%	0.00%	0.00%
Hyde Park Capital Limited	0.75%	0.00%	0.00%
Total	100.00%	100.00%	100.00%

The Managing Agent is owned by Asta Capital Limited, a company incorporated in the U.K. and registered in England and Wales. Paraline International, a wholly owned subsidiary of Paraline Group, owns 31.3% of Asta Capital Limited. Paraline Group Ltd (Paraline Group), a company registered in Bermuda, facilitated 10% of the Syndicate's insurance capacity on the 2017 and 2016 underwriting years through its owned corporate member.

In October 2018, Paraline Group sold their interest in the corporate member (CCM 9 Ltd) to Beat Capital Partners Ltd (Beat) as part of a merger. Paraline Group is now a joint shareholder of Beat.

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) from the SPA to Paraline CCM Limited was \$0 at 31 December 2018 (2017: \$26,357)

Related parties continued

Pursuant to an inter-syndicate loan deed between the reinsured and the SPA, the reinsured may advance up to \$10 million to the SPA (2017: \$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 2018, the SPA had a loan payable balance to the reinsured of \$27.0 million (2017: \$19.0 million) measured at cost. The reinsured also owed the SPA \$22.8 million at 31 December 2018 (2017: \$18.6 million).

12. Disclosure of interests

Managing Agent's interest

During 2018 Asta was the Managing Agent for ten Syndicates and three Special Purpose Arrangements. Syndicates 1729, 1897, 1980, 2357, 2525, 2689, 2786, 3268, 4242 and 5886 as well as Special Purpose Arrangements 6123, 6126 and 6131 were managed on behalf of third party capital providers.

On 1 January 2018 Asta took on management of Syndicate 1980 and Syndicate 3268. Asta also took on management of Special Purpose Arrangement 6131.

The agency also provides administrative services to Syndicates and Special Purpose Arrangements, also undertaking a number of ancillary roles for other clients.

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

13. Funds at Lloyd's

Every member is required to hold capital at Lloyd's which is held in trust and known as Funds at Lloyd's (FAL). These funds are intended primarily to cover circumstances where SPA assets prove insufficient to meet participating members' underwriting liabilities.

The level of FAL that Lloyd's requires a member to maintain is determined by Lloyd's based on PRA requirements and resource criteria. FAL has regard to a number of factors including the nature and amount of risk to be underwritten by the member and the assessment of the reserving risk in respect of business that has been underwritten. Since FAL is not under the management of the Managing Agent, no amount has been shown in these annual accounts by way of such capital resources. However, the Managing Agent is able to make a call on the members' FAL to meet liquidity requirements or to settle losses. Refer to note 15 for further details.

14. Off-balance sheet items

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

15. 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 objectives, policies and approach

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.

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.

Risk management continued

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 2018 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 14, 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 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.

Risk management continued

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 2018.

	Estimated gross losses \$'000
Windstorm in the North-eastern U.S.	34,862
Windstorm in the Carolinas	37,419
Florida windstorm (Miami-Dade)	44,151
Florida windstorm (Pinellas)	43,687
California earthquake (Los Angeles)	44,871
California earthquake (San Francisco)	62,265
New Madrid area of the U.S. earthquake	15,523
Windstorm in the U.S. Gulf	38,751
Syndicate-specific scenario (Mississippi windstorm)	15,990
Syndicate-specific scenario (U.S. Pacific Northwest earthquake)	50,426

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 \$121 million (2017: \$105 million), \$242 million in the aggregate (2017: \$210 million). This reinsurance helps to limit the SPA's risk of insolvency from a single large catastrophe or multiple smaller catastrophes.

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

Risk management continued

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.

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.

Risk management continued

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 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.

2018	Five percent increase \$'000	Five percent decrease \$'000
Reinsurance accepted	(631)	631
2017	Five percent increase \$'000	Five percent decrease \$'000
Reinsurance accepted	(555)	555

The Syndicate has material exposure to the Hurricanes Harvey and Irma in the 2016 and 2017 year of account and to Hurricanes Florence and Michael in the 2017 and 2018 year of account. This increases the uncertainty of the Syndicate's total reserves, but does not increase that uncertainty in an adverse direction significantly beyond the normal range of uncertainty for insurance liabilities at this stage of development.

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.

	2016 \$'000	2017 \$'000	2018 \$'000
Underwriting year			
Estimate of cumulative gross claims incurred:			
At end of underwriting year	2,080	14,260	34,020
One year later	10,670	51,653	
Two years later	19,805		
Less cumulative paid	(8,978)	(18,445)	(5,300)
Liability for gross outstanding claims (2016 to 2018)	10,827	33,208	28,720
Total gross outstanding claims (all years)			72,755

Risk management continued

	2016	2017	2018
Underwriting year	\$'000	\$'000	\$'000
Estimate of cumulative net claims incurred:			
At end of underwriting year	2,080	9,693	13,987
One year later	9,897	14,501	
Two years later	7,004		
Less cumulative paid	(6,398)	(11,689)	(4,777)
Liability for gross outstanding claims (2016 to 2018)	606	2,812	9,210
Total net outstanding claims (all years)			12,628

d) Financial risk

1) Credit Risk

Credit risk is the risk that other parties fail to honour their obligations to the reinsured and the reinsured in turn fails to honour its obligations to the SPA (page 4).

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

2018	\$'000			
	Neither past due nor impaired	Past due	Impaired	Total
Reinsurers share of claims outstanding	60,127	-	-	60,127
Debtors arising out of reinsurance operations	28,600	-	-	28,600
Other debtors	5,540	-	-	5,540
Total	94,267	-	-	94,267

2017	\$'000			
	Neither past due nor impaired	Past due	Impaired	Total
Reinsurers share of claims outstanding	7,507	-	-	7,507
Debtors arising out of reinsurance operations	22,160	-	-	22,160
Other debtors	3,091	-	-	3,091
Total	32,758	-	-	32,758

Risk management continued

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.

2018	\$'000				
	AAA	AA	A	Not Rated	Total
Reinsurers share of claims outstanding	-	10,433	14,366	35,328	60,127
Debtors arising out of reinsurance operations	-	1,661	23,111	3,828	28,600
Other debtors	-	-	-	5,540	5,540
Total	-	12,094	37,477	44,696	94,267

2017	\$'000				
	AAA	AA	A	Not Rated	Total
Reinsurers share of claims outstanding	-	505	3,121	3,881	7,507
Debtors arising out of reinsurance operations	-	49	306	21,805	22,160
Other debtors	-	-	-	3,091	3,091
Total	-	554	3,427	28,777	32,758

2) 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 regular 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.

In the year, the Syndicate requested a cash call of \$7.5 million from the members participating on the 2017 YOA.

The reinsured also has a \$55 million (2017: \$35 million) letter of credit facility from Barclays Bank PLC, which was utilised in the year.

Risk management continued

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.

2018		\$'000			
	Up to a year	1-3 years	3-5 years	More than 5 years	Total
<i>Assets</i>					
Reinsurer's share of claims outstanding	35,767	22,059	2,198	103	60,127
Debtors	11,570	17,030	-	-	28,600
Total	47,337	39,089	2,198	103	88,727
<i>Liabilities</i>					
Claims outstanding	(43,278)	(26,692)	(2,660)	(125)	(72,755)
Creditors	(12,855)	(17,629)	-	-	(30,484)
Total	(56,133)	(44,321)	(2,660)	(125)	(103,239)

2017		\$'000			
	Up to a year	1-3 years	3-5 years	More than 5 years	Total
<i>Assets</i>					
Reinsurer's share of claims outstanding	4,580	2,528	378	21	7,507
Debtors	6,466	15,694	-	-	22,160
Total	11,046	18,222	378	21	29,667
<i>Liabilities</i>					
Claims outstanding	(11,357)	(6,268)	(937)	(51)	(18,613)
Creditors	(4,293)	(15,696)	-	-	(19,989)
Total	(15,650)	(21,964)	(937)	(51)	(38,602)

3) Market risk

Market risk is the risk that the fair value of 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 other price risk (page 4).

Risk management continued

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.

Sensitivity to changes

The SPA transacts in US Dollar only, therefore there is no impact on profit and members' balances from changes to the relative strength of other currencies against the US Dollar.

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 SPA has no significant concentration of interest rate risk.

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

	2018	2017
	\$'000	\$'000
Interest Rate Risk		
Impact of 50 basis point increase on result	(2)	(5)
Impact of 50 basis point decrease on result	2	4
Impact of 50 basis point increase on net assets	(2)	(5)
Impact of 50 basis point decrease on net assets	2	4

The method used for deriving sensitivity information and significant variables did not change from the previous period.

16. Post balance sheet events

A cash call was made to members in January 2019 for \$3.25m on 2016 year of account, for \$2.75m on 2017 year of account and for \$6.5m on 2018 year of account. Following this, a cash call was made to members in March 2019 for \$3.5m on 2018 year of account.

The Syndicate will collect the 2016 year of account losses in US Dollars from members in 2019.

The directors evaluated other events subsequent to the balance sheet date through 22 March 2019, the date the SPA issued these annual accounts, and determined that no other items require disclosure.