# Market Turning Event

## Lloyd's Guiding Principles

LLOYD'S

**Disclaimer**

This document is intended to act as a guide to Managing Agents following a Market Turning Event (MTE). The specific activities of both Managing Agents and the Corporation would be highly dependent on the nature and scale of the event and the associated impact to the market and/or associated supporting capital.

The guiding principles detailed in this paper are not intended to bind Lloyd's or Managing Agents to specific actions following a MTE. Lloyd's appreciates that an event of the magnitude that would turn the market would likely to be so unexpected or varied that a high degree of flexibility in the response would be necessary.

In all cases, following a MTE Lloyd's would provide further communication to the market and wider stakeholders (e.g. regulators, rating agencies etc) the set activities to be carried out. These may differ to what is included in this document.

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# 1. Introduction

## 1.1 Purpose and Scope

The purpose of this paper is to set out Lloyd's guiding principles in response to a Market Turning Event (MTE). It is aimed at Managing Agents but also would serve as useful information to other stakeholders e.g. regulators.

The guiding principles detailed in this document have been developed and influenced by the industry "Dry run" exercise which was carried out by the London Market in November 2016. This paper responds to the recommendations concluded from the exercise.

## 1.2 Industry dry-run recommendations

This paper responds to the following recommendations made in the white paper from the industry dry-run exercise:

- **"Prepare for rapid response.
In the best interests of its syndicates and their policyholders, Lloyd's should consider how, following a catastrophe, it could shorten the time required to review and approve syndicates' revised business plans or updated internal models. This should include, wherever possible, how it can best support syndicates' reporting requirements to the PRA and other regulators. Lloyd's could also help accelerate the process by which syndicates revalidate their internal models following a major catastrophe by providing additional guidelines on which aspects it is likely to expect syndicates to focus on when reviewing or adjusting their models".**
- **"Maintain its position as a centre of excellence by supporting (re)insurers and brokers with a best practice emergency service.
Catastrophic events can occur at any time of the day or night, and require 24/7 access to facilities and emergency service, as was done post-9/11. Lloyd's should consider building on its existing catastrophic event response mechanisms by further improving the clarity around the post event process of paying claims rapidly, co-ordinating regulatory responses across geographies, capital assessment, and underwriting opportunity. Dependent on the size and nature of the event, this may or may not require a single body of contact to bring together different Lloyd's workstreams".**

# 2. Executive Summary

This report sets out Lloyd's Guiding Principles to a Market Turning Event (MTE), an event which causes significant impact and could cause a rapid upturn in insurance pricing. It is aimed at Managing Agents in the Lloyd's market and is intended to act as a guide to help Managing Agents understand Lloyd's expectations in formulating a response to an MTE.

Six guiding principles have been defined and are categorised into two areas:

**1. Crisis management – to ensure the market responds to a crisis effectively, pays claims as quickly as possible and remains solvent.**

**1. Principle 1 – Market stability and payment of claims**
Lloyd's primary focus is on the stability of the market by ensuring it is solvent and liquid to ensure prompt payment of claims to affected policyholders

**2. Principle 2 – Management of failing syndicates / members**
It is likely that some syndicates/members will fail following an MTE. Lloyd's will ensure that the run off of those syndicates are managed in an orderly fashion to minimise any wider impact to the market

**3. Principle 3 – Stakeholder / data collection / coordination and communication**
Lloyd's would look to take a lead[1] with coordinating interaction and collation of data with key external stakeholders (e.g. regulators, governments, rating agencies) minimising any duplication where possible

**2. Opportunities – to support the market so that it can take advantage of commercial opportunities following an MTE**

**4. Principle 4 – Support to the market**
Support will be given to the market in responding to opportunities arising from an MTE which ultimately supplies capacity to clients. Where possible, activities in support of existing businesses may be prioritised ahead of new entrants

**5. Principle 5 – Accelerated key processes**
Lloyd's approach will be commercial and pragmatic. This may include the use of an accelerated version of syndicate business and capital plan review/approval process

**6. Principle 6 – Lloyd's priorities**
Corporation staff will focus on supporting the market in response to the event – potentially all other non-essential[2] central activities will be temporarily suspended

These principles are further explained in the subsequent sections of this report.

In addition Lloyd's has set out a clear internal structure and segregation of duties to ensure the Corporation is best placed to respond to an MTE.

Lloyd's also recommends that Managing Agents consider in advance the possible implications of an MTE and prepare suitably proportionate, robust and well tested contingency plans. These should reflect Lloyd's approach of reactive and proactive planning following an MTE.

1 Although Lloyd's would aim to lead and coordinate interactions with external stakeholders, there may be situations following a MTE where stakeholders (e.g. the PRA) would want to interact directly with Managing Agents and vice versa

2 Non-essential being not business critical or legal requirements

# 3. Definition of a Market Turning Event

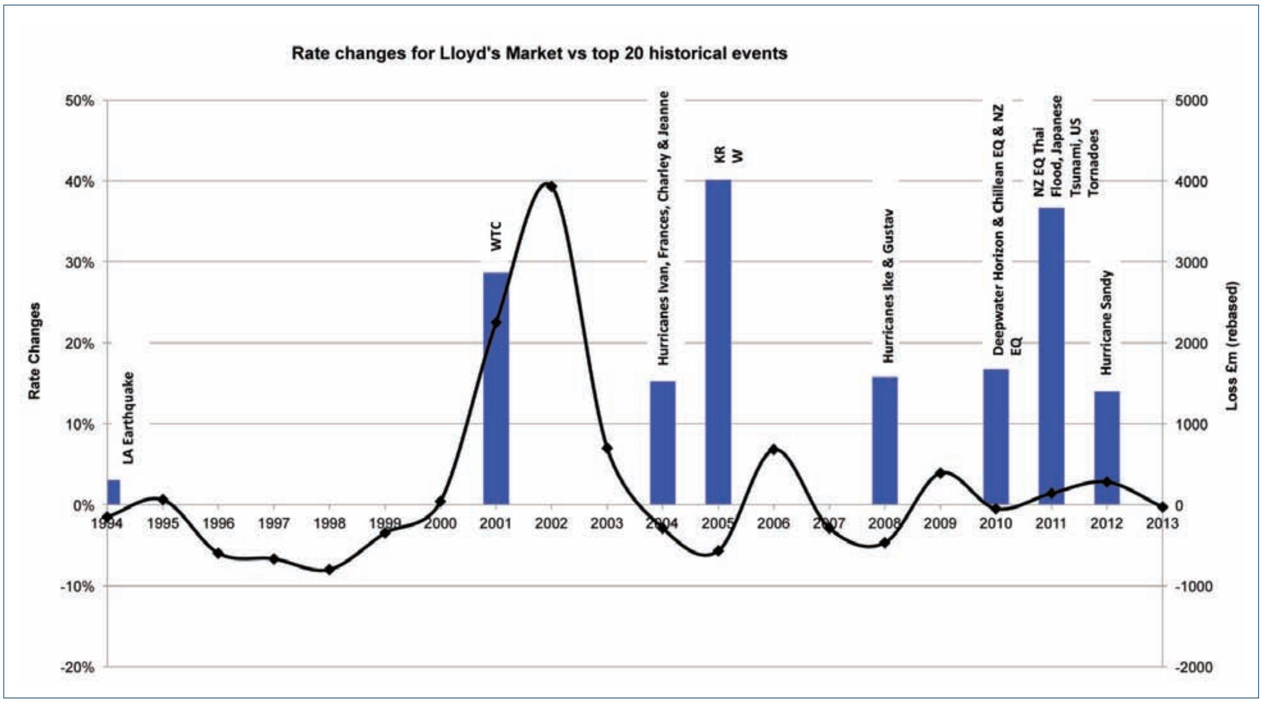
## 3.1 Definition

A Market Turning Event (MTE) is defined as an event which causes significant impact and cause a significant and rapid upturn in the pricing environment. For Lloyd's this could be:

– A major insured incident e.g. either a man-made catastrophe (such as 9/11 World Trade Centre 'WTC' attacks or a cyber blackout) or natural catastrophe (such as KRW); or

– A major external event e.g. the collapse of a key market player or a financial crisis such as a severe stock market crash.

As can be seen in the chart below, the last clear market changing event was WTC in 2001, after which there were rate increases of ~40% across the all classes of business.




**Notes:**

(1) The guiding principles detailed in this document would be applied by Lloyd's in case of an MTE as defined and not for a 'normal' event.

(2) The Lloyd's MTE Steering Group (defined in section 4) would decide whether an event meets the definition in order for the principles to be applied.

## 3.2 Characteristics of an MTE

The event in question is assumed to be sufficiently material to cause some or all of the following consequences, although this may not be an exhaustive list:

- The event is likely to generate significant insurance claims (both in volume and potentially in size) to a number of syndicates operating in the Lloyd's market;
- The event maybe unknown i.e. not included in current modelling or ever similarly experienced before;
- The full extent of likely claims and their eventual settlement cost might take some time to be known with certainty;
- Syndicates might have been impacted severely by the event, to the extent that their potential losses mean they might no longer have sufficient financial resources to meet their regulatory capital requirements;
- Given the initial uncertainties involved in estimating claims, some affected syndicates might not know for some time how the event has impacted their overall regulatory capital position, or the full nature of the claims to which they are exposed;
- Some other syndicates might not be impacted at all by claims from the event, or are impacted to a much lesser extent;
- The event impacts prevailing market conditions for general insurance products including the availability, price and/or terms of insurance coverage that syndicates are able to offer policyholders for future policies. The impact might or might not be limited to the class(es) of business most directly affected by the event;
- If premium rates rise, some syndicates are likely to wish to take advantage and refocus on support to clients and write more business;
- Some syndicates might need to raise additional capital in order to continue to trade, or might wish to raise additional capital to take advantage of perceived market opportunities. Sources of capital could include a parent company, or third-party investors;
- Impact on the availability of reinsurance capacity or liquidity and financial market risk impacts which could impair the payment of claims

# 4. Guiding Principles

## 4.1 Principles governing Lloyd's response to a MTE

Lloyd's response to an MTE is split into two distinct stages:

**1. Crisis management –** Focus on solvency and market stability
**2. Opportunities –** Supporting the market to take advantage of the commercial opportunities

The following principles have been defined in this context and are further explained in the subsequent sections.

**Market Turning Event**

**Lloyd's internal governance**

### Crisis Management

**1. Principle 1 – Market stability and payment of claims**
Lloyd's primary focus is on the stability of the market by ensuring it is solvent and liquid to ensure prompt payment of claims to affected policyholders

**2. Principle 2 – Management of failing syndicates / members**
It is likely that some syndicates/members will fail following an MTE. Lloyd's will ensure that the run off of those syndicates are managed in an orderly fashion to minimise any wider impact to the market

**3. Principle 3 – Stakeholder / data collection / coordination and communication**
Lloyd's would look to take a lead[1] with coordinating interaction and collation of data with key external stakeholders (e.g. regulators, governments, rating agencies) minimising any duplication where possible

### Opportunities

**4. Principle 4 – Support to the market**
Support will be given to the market in responding to opportunities arising from an MTE which ultimately supplies capacity to clients. Where possible, activities in support of existing businesses may be prioritised ahead of new entrants

**5. Principle 5 – Accelerated key processes**
Lloyd's approach will be commercial and pragmatic. This may include the use of an accelerated version of syndicate business and capital plan review/approval process

**6. Principle 6 – Lloyd's priorities**
Corporation staff will focus on supporting the market in response to the event – potentially all other non-essential[2] central activities will be temporarily suspended

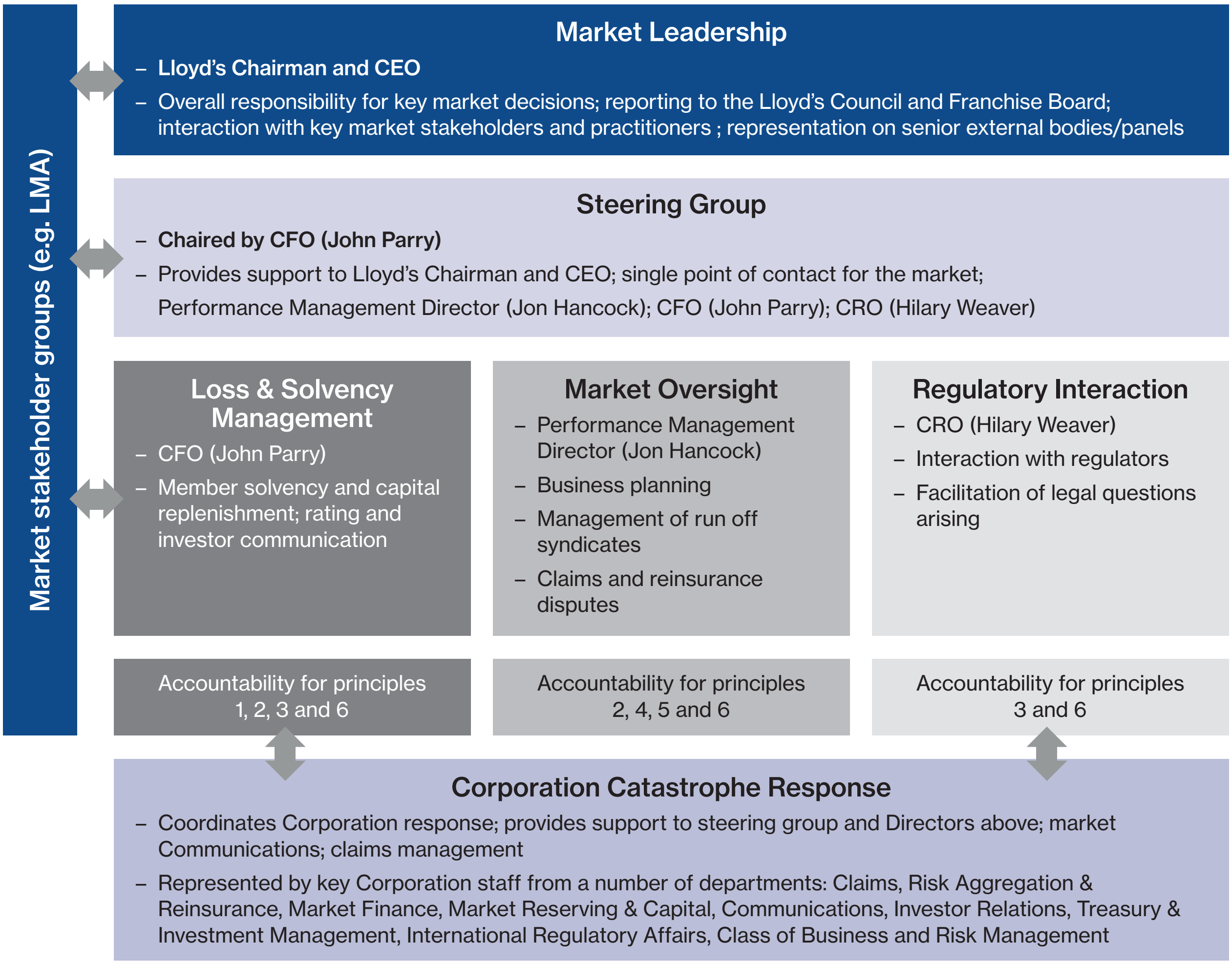
1 Although Lloyd's would aim to lead and coordinate interactions with external stakeholders, there may be situations following a MTE where stakeholders (e.g. the PRA) would want to interact directly with Managing Agents and vice versa

2 Non-essential being not business critical or legal requirements

# 5. Lloyd's Internal Governance

## 5.1 Structure and responsibilities

Lloyd's will structure itself so that it is best positioned to respond to an MTE. A clear internal structure and a segregation of duties will be put in place within Lloyd's with key roles and contacts publically known.




**Overall features:**

- Structure enables a segregation of duties within Lloyd's senior management
- Market has a single point of contact at Lloyd's for queries on specific areas
- Steering Group has an overarching view of the management of the MTE which enables clear and effective line of communication externally and upwards within Lloyd's
- Leverages Lloyd's existing internal "Catastrophe Response" processes which have been tried and tested in previous events

# 6. Contingency Planning

## 6.1 Advanced preparation

Preparing a robust and well tested contingency plan in response to a MTE will help both Lloyd's and the Managing Agents to be best prepared for response to a MTE.

Managing Agents can consider in advance the possible implications of a MTE on their business, including what steps might reasonably be taken to enable them to respond appropriately to meet their obligations, whether regulatory, policyholder or commercial.

Contingency plans should reflect Lloyd's approach of reactive and proactive planning following a MTE. The plan should look to cover for each syndicate under management:

- Reactive action plan for managing the impact or 'crisis' of a MTE; and,
- Proactive action plan to take advantage of any potential commercial opportunities of a MTE.

The contingency plan should look to be proportionate to the nature and scale of a syndicate's business model, relative to the impact a MTE might have on its operations. It should differ from a Managing Agent's Business Continuity Plan (BCP) as it should be a sufficiently stressed plan to best respond to a MTE.

Note: Managing Agents are likely to have similar plans already in place (e.g. recovery and resolution plans), where possible these should link together.

### 6.1.1 Elements for consideration

The contingency plan should pay specific attention to the impact on the syndicate's business model following a MTE. Elements for consideration should include, but not be limited to, the following areas. Some of these areas are detailed further in section 6 in this document.

| | |
|---|---|
| **Business Model Analysis** | – In general, Managing Agents should consider any vulnerabilities within the syndicates business model and how best to manage them.<br>– The MTE contingency plan should address the sustainability of a syndicate's existing business model, rather than specific detailed planning for a particular scenario.<br>– This may be approached on a class of business basis but should ensure the evaluation of the business is based on impact of any given MTE rather than a specific scenarios or events. |
| **Capital and Financing** | – Solvency is a crucial consideration pre-empting any trade or business deals during a MTE. Following an MTE, Lloyd's will need to conduct an overall market solvency assessment before considering any changes to syndicate business plans for capital levels (further details of Lloyd's assessment is described later in this document).<br>– Managing Agents should therefore provide detail on potential sources of additional capital should it be required to manage the impact of a MTE or finance any new business proposal. |

| | |
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| **Capital and Financing (cont.)** | – Details of the liquidity of assets to best demonstrate solvency should also be provided. |
| **Claims Handling** | – During a MTE, a surge in insurance claims may ensue (both in volume and size) for a Managing Agent and thus will require efficient handling.<br>– Managing Agents should therefore consider their claims management process and policy during this time.<br>– Although, the full extent of actual claims and their eventual settlement cost may take some time to be known with certainty, Managing Agents should aim to ensure prompt payment of claims to affected policyholders in accordance with the agreed terms of contract. Managing Agents should ensure in doing so, regulatory conduct principles are upheld. |
| **Resourcing** | – Resourcing levels are likely to come under pressure i.e. to service the additional requirements of managing the impact of a MTE and proposals to revise business plans.<br>– Managing Agents should detail the source of any additional resourcing and the speed of turnaround. Consideration should also be given as to the availability of resource and any potential assessment of competing priorities for the given resource. This will be particularly relevant where a group may be considered to provide addition resource but may also be impacted by the MTE. |
| **Governance** | – Changes to the governance structure may need to be considered following a MTE. Consideration should be given to the need for extraordinary Board meetings and their continued frequency.<br>– Managing Agents may also consider the creation and constituents of any temporary committees for managing a MTE. The Terms of Reference for this committee should provide sufficient detail on the stated authority levels of each member and reporting lines, inter alia. It may be beneficial for Managing Agents to consider syndicate's MTE governance structure against Lloyd's internal governance structure, as detailed in section 5, to best establish a reactive and proactive governance action plan following a MTE. |
| **Risk Management** | – Managing Agents should have the ability to measure the impact and opportunity associated with the MTE against the syndicate's risk register and risk appetite.<br>– This information will be of particular importance in assessing the viability of a syndicate's business following a MTE. The outcome of this assessment will feed into Lloyd's preliminary assessment following a MTE and will be a factor of consideration in determining whether a syndicate can or cannot write new business. |

| | |
|---|---|
| **Reporting Requirements** | – A MTE will give rise to various aspects of uncertainty surrounding a «syndicate's business model.<br>– To attain certainty, regulatory reporting requirements will be in place. Managing Agents should therefore detail the proposed approach to submitting required reporting within a short time-frame (please refer to section 8.3.1 'Mandatory reporting during an MTE' for further details). |
| **Regulation** | – Consideration should be made to the regulatory impact on both a national and international level.<br>– Although Lloyd's would look to lead on coordinating with local and international regulators (see section 7.3), Managing Agents should be able to identify all relevant regulatory contacts and should be able to provide the relevant information within a steady communication system. |
| **Communication** | – Similar to the above, Lloyd's would look to lead on coordinating with key stakeholders (see section 7.3).<br>– Managing Agents should consider developing a plan for communicating information to policyholders, regulators, staff, members, brokers, coverholders and counter-parties. Details of any emergency response systems that will be utilised to ensure a steady communication operation should also be provided as part of planning. |

### 6.1.2 Link to ORSA

There are elements of contingency planning which are already covered within the ORSA process such as scenario testing, forward looking plans and the consideration of capital requirements. It may be useful to include a high level overview of the contingency planning for a MTE in the annual ORSA to support any existing analysis, however this is a not a requirement.

### 6.1.3 Lloyd's review process of syndicate contingency plans

Managing Agents have the option to submit a MTE contingency plan in full or summary format via their ORSA to the Lloyd's Syndicate Capability Oversight team at any time of the year.

Through the annual market oversight letter / timetable process, a specific time period for submission and review can be agreed through discussion with the Managing Agent.

In the event of a MTE, Lloyd's will assess Managing Agents' success of implementing the reactive actions to manage the impact of a MTE detailed contingency plans. A meeting will be arranged between the Managing Agent and Lloyd's Account Manager to discuss and evaluate this in more detail.

# Crisis Magement

## 1. Principle 1 – Market stability and payment of claims

**Lloyd's primary focus is on the stability of the market by ensuring it is solvent and liquid with capital being replenished to ensure prompt payment of claims to affected policyholders**

## 2. Principle 2 – Management of failing syndicates

It is likely that some syndicates/members will fail following an MTE. Lloyd's will ensure that the run off of those syndicates are managed in an orderly fashion to minimise any wider impact to the market

## 3. Principle 3 – Stakeholder / data collection / coordination and communication

Lloyd's would look to take a lead with coordinating interaction and collation of data with key external stakeholders (e.g. regulators, governments, rating agencies) minimising any duplication where possible[4]

# 7. Crisis Management

## 7.1 1. Principle 1 – Market stability and payment of claims

Lloyd's primary focus is on the stability of the market by ensuring it is solvent and liquid with capital being replenished to ensure prompt payment of claims to affected policyholders.

### 7.1.1 Lloyd's preliminary assessment

Following an MTE, the primary concern would be ensuring the protection of policyholders. A secondary focus would be on reinforcing market confidence with various stakeholders (e.g. brokers, rating agencies, regulators etc) ultimately on whether claims can be paid promptly.

From an aggregate position, centrally Lloyd's would also look to gain answers to the following key questions:

1. What is the total market loss?
2. Is the market still solvent?
3. Which syndicates/members are significantly impacted or are expected to fail?
4. What is the impact to the Central Fund?
5. What are the subsequent losses that need to be considered?
6. What key lines of communication need to be made with internal and external stakeholders?

The accuracy, speed and completeness of the answers to these questions would depend on whether the MTE and associated losses are known (i.e. represented within syndicate's internal models or the Lloyd's Internal Model). Illustrations of this are detailed in the table overleaf.

**Notes:**
In all cases in the below overleaf, the specifics (e.g. timings and information requested) could vary dependent on the circumstances of the MTE.
Lloyd's would share information with the PRA as soon as available/possible and would work with the PRA to keep them closely informed.

| Lloyd's Assessment | MTE known / captured within models* | MTE unknown / not captured within models* |
|---|---|---|
| **Central assessment independent of market input** (i.e. based on no new input/data from syndicates) | **Quality/accuracy of assessment = Low to Medium**<br>– Heavily caveated and using existing information, Lloyd's would quickly be able to perform an initial assessment on answering the above questions<br>– Estimate of timings: Within one week after the MTE<br>– Available data used as part of assessment:<br>– Lloyd's Catastrophe Model data (latest quarterly in-force)<br>– Latest Syndicate Business Forecasts<br>– Market solvency return (latest quarterly return)<br>– Lloyd's Internal Model data<br>– Historical data<br>– Lloyd's Capital Returns<br>– Syndicate Realistic Disaster Scenario returns<br>– View from the Corporation's Class of Business team<br>– Syndicate MTE contingency plans | **Quality/accuracy of assessment = Low**<br>– Lloyd's preliminary assessment of the MTE would be limited due to lack of available data and would only be able to answer in part some of the questions above with a high degree of uncertainty<br>– Lloyd's would utilise the experience of internal teams within the Corporation to perform such an assessment – this could include conducting scenario analysis to bridge gaps in data/experience<br>– Estimate of timings: Within two weeks after the MTE<br>– Available data used as part of assessment: As detailed in left hand box |
| **Central assessment dependent of market input** (i.e. based on new input/data from syndicates) | **Quality/accuracy of assessment = Medium to High**<br>– Where the event is known, a best-guess modelled estimate can be obtained from syndicates in order to help provide more accurate and informed answers to the above questions under section 7.1.1<br>– Estimate of timings: (Note this could vary dependent on the circumstances)<br>– A request for data from syndicates would be made by Lloyd's within one week after an MTE, and request initial submissions from syndicates a week thereafter<br>– Data requested:<br>– Primary information Lloyd's would ask syndicates for would include firm best estimate of the losses incurred from the MTE along with narrative on the basis of the estimates and commentary on possible sources of uncertainty<br>– Secondary information requested would include: details of largest reinsurer counterparties impacted, estimate of concentration of loss by business line, pre-event SCR / SCR-ult and eligible own funds (pre & post event)<br>– This information would be requested via a data request template which would serve both Lloyd's and the PRA requirements (illustration provided in appendix based on PRA supervisory statement on MTE) | **Quality/accuracy of assessment = Low to Medium**<br>– Syndicates will have limited data/experience of the losses encountered and will take some time to form an accurate view of the MTE<br>– Estimate of timings: (Note this could vary dependent on the circumstances)<br>– Phase 1 (initial view): A request for data from syndicates would be made by Lloyd's within one week after an MTE, and request initial submissions from syndicates a week thereafter<br>– Phase 2 (more informed): As more information materialises about the MTE, syndicates would be asked to provide updates on their initial loss estimates (Note: the specific timings and number of requests will be dictated by the specific circumstances)<br>– Data requested:<br>– Same as detailed in lower left hand box<br>– In addition syndicates could be asked to complete scenario analysis to bridge gaps in data<br>– The information would be requested via a data request template which would serve both Lloyd's and the PRA (illustration provided in appendix based on PRA supervisory statement on MTE) |

*syndicate internal models and the Lloyd's Internal Model (LIM)

### 7.1.2 Solvency assessment

Lloyd's monitors solvency at the market wide and member level on a quarterly basis. Post a major event, the estimates of the losses provided by the syndicates will be used to develop an initial assessment of the impact on both market wide and member solvency positions. This initial assessment will take into consideration the most recently reported solvency position derived from the Quarterly Solvency Return submitted by syndicates for the quarter just ended.

If the market wide and/or central solvency ratios fall below Lloyd's central risk appetite levels members will be required to inject additional capital to restore them back to at least risk appetite level. There will be an element of judgement in determining which members need to inject additional capital; however where any member's capital (FAL and net underwriting position) falls below their solvency capital requirement (SCR) after the event, they will be required to inject additional funds to cover the deficit immediately.

Members' will be required to cover any individual solvency deficits before any increases to syndicates' business plans and/or new business plans are considered by the Capital and Planning Group (CPG).

### 7.1.3 Claims / operational aspects

The existing Catastrophe Response Framework both at Corporation and Market, Managing Agent level would form the foundations for the organisation of the markets claims response. These are regularly refined based on learnings over time.

An MTE would require enhanced levels of Market co-ordination (both in terms of action and informational flow). At an individual Managing Agent level it may stress the claims handling capacity.

This stress may also be experienced in the claims handling supply chain i.e. TPAs, Coverholders, Brokers and other service providers as well.

**Market Level**
The Corporation's Catastrophe Response Steering Group, Lloyd's Market Strategic Claims Group (LMSCG) and Lloyd's Market Association Claims Committee (LMACC) would work collaboratively to support the Market in meeting these needs.

Their collective priority would be to swiftly establish the actual event ground truth with a particular focus on the unique features of the event and challenges, supported by other resources where necessary.

They would determine what additional levels of Market co-ordination would be required and take the necessary steps to implement these. Working with Lloyd's they would determine whether a dedicated London based or virtual "Event Response Office" (ERO) should be established and what additional response activities beyond existing plans would be needed.

This office would be instrumental in ensuring that the key features and challenges from the MTE are identified, understood and communicated at a Market level and in being instrumental in establishing Market consensus on key thematic response matters. This would also extend to managing the communication activity with key stakeholders and giving confidence in the Market response. The ERO's core objective would be to support and ensure a swift Market level response

A decision would also be made as to whether establishing an Event Response Hub (ERH) locally to the event or within the impact zone/impact region was beneficial/feasible and how existing Lloyd's and Market resource in the region could be used to support the ERH.

Lloyd's would work with the ERO to ensure that key statistics were available to the office throughout the event response to enable a detailed understanding of the event scale, complexity and response progress. Lloyd's would also liaise with the ERO on all necessary claims related regulatory aspects.

Consideration would also be given as to whether the ERH or ERO should be joint industry initiatives and to what degree joint industry response groups should be established.

The ERO would also address demands for authorised Lloyd's Market representatives to attend event response activities organised by regulatory bodies whether in London or internationally and aid in the overall co-ordination of Market representative visits to the affected area.

**Managing Agent Level**
Every Managing Agent should have contingency plans in place for an MTE (as detailed in section 6) but these may very well be stressed in an MTE situation.

Lloyd's in its governance role would be responsible for early assessment and monitoring of the capacity of each Managing Agent to meet its demands. Where there were concerns swift steps would be taken to resolve those concerns, agree support mechanisms or find suitable alternatives.

**Claims Handling Supply Chain**
It is realistic that in an MTE there would be exceptional demand on Brokers, Coverholders, TPAs and third party suppliers which could be caused by scale of demand but also loss of personnel and offices.

Identifying these situations, case by case, and proposing how best to address the situation would fall to Managing Agents or relevant Market Sector Claims Groups involved but where there was a thematic risk at a Market level then Lloyd's would work with the Market collaboratively to establish a plan of action.

### 7.1.4 Reinsurance disputes

It is likely that following a MTE that there may be major disputes &/or material Aged Debt balances between a Lloyd's syndicate and a reinsurance counterparty. In such circumstances Lloyd's may become involved, as appropriate, to help resolve the dispute.

Key factors that determine whether Lloyd's would become involved include:

1. **The number of Lloyd's syndicates affected**
2. **The quantum of the dispute and potential reputational issues**

A dedicated Corporation virtual internal team (in conjunction with the existing Outwards Reinsurance Team) would be created to assist in any negotiation and credit control work. The team would report into the Director of Performance Management.

**Activity**
The team would work with Credit controllers in the market to help their Syndicates find a solution to any disputes or potential disputes following a MTE.

The above would be in addition to normal syndicate oversight activity, which would continue to monitor each syndicate's ability to manage its reinsurance recoveries, including Aged Debts and Disputes.

### 7.1.5 Capital replenishment

The following principles which underlie the requirement for members to inject additional funds and these will continue to be applied following a market turning event:

- Where a member's capital (FAL and net underwriting position) falls below their SCR after the event, they will be required to inject additional funds to cover the deficit immediately.
- Where a member's capital falls below their economic capital assessment (ECA) but is above their SCR, judgement will be involved in determining whether additional funds need to be injected. Where this judgement leads to the conclusion that a member needs to inject additional funds the timing of this injection will be determined on a case by case basis.
- Where changes to a syndicate's business plan or new business plans have been approved by the CPG, members will be required to satisfy the applicable capital requirements before any underwriting commences.

If the losses arising from the event give rise to undertakings on the Central Fund, which either threaten the ability to satisfy the market wide and/or central solvency coverage appetites or the Society of Lloyd's ratings, those members who continue to be financially sound will be required to inject additional funds to restore the Central Fund to an adequate level.

There are two mechanisms which are available to Lloyd's to facilitate this: (i) increasing the level of the Central Fund contributions or (ii) invoking the rights attached to the callable layer.

Where additional member contributions/funds are needed to replenish the Central Fund, the amount and timing of the injections will be determined having considered the level of undertakings on the Central Fund. [No member will be required to inject additional funds/contributions to a level which would jeopardise their solvency.]

### 7.1.6 Syndicate internal models

An event of the magnitude that would turn the market would likely to be unexpected or very varied; therefore Lloyd's recognises that it might take some time after an MTE for reliable data to become available which are sufficiently complete and accurate to enable the firm to undertake a robust assessment of their internal model.

**Initial assessment:**
As part of the immediate response, Lloyd's would expect Managing Agents to consider whether the MTE might prompt a review of elements of an approved internal model. Where possible, Managing Agents should provide Lloyd's with an indication of this, including whether a potential adjustment to capital requirements (Lloyd's ECA) is required.

Potential areas of focus within internal models would include significant changes in key risk categories (e.g. insurance risk, credit risk (outwards reinsurance), market risk etc).

The agents will be required to complete a template issued by Lloyd's to complete a preliminary assessment, as discussed in sections 7.1.1 and 7.3.

**Detailed assessment:**
Lloyd's will follow up the initial impact assessment with a request for a more detailed and accurate assessment of the impact on capital. The review will not be restricted to capital and is likely to cover other relevant areas of business. Some of the areas Lloyd's will assess post MTE with respect to models would be:

- **Reserves:** The report submitted to Lloyd's should discuss, in detail, the impact of the MTE on reserves both at a class level and at an aggregate level. The internal model is usually run on Q4 current year of account (CY) reserves. If the model is run on a different assumption following the MTE, it should be clearly specified in the submitted report.

- **Underwriting:** The report should cover all possible changes in underwriting following the MTE. This is expected to at least cover any changes in underwriting strategy, premium rates, reinsurance purchased and underwriting risk.
- **Liquidity/Counterparty risk:** A MTE can potentially have an impact on the liquidity of the company. The detailed report should cover liquidity risk that the company is exposed to following the event and should also describe the risk mitigation measures in place. Any changes in counterparty risk should be duly reported.
- **Operational risk:** Changes in the risk associated to the internal processes, systems and people of the company due to the MTE should be appropriately reported.
- **Market/investment risk:** Any changes in investment strategy or market risk assumptions should be explained appropriately in the report.
- **Changes in the model:** Any potential/anticipated changes in the internal model design, assumptions and output should be adequately analysed and explained. While a full suite of validation tests is not expected to be conducted, it is assumed

that the Managing Agent will carry out necessary reconciliation checks to ensure sufficient credibility of the results.

Managing Agents are required to submit a detailed report covering the areas as mentioned above (note: the above list is not exhaustive) within 2 to 3 months of the MTE.

**Note:** Details of the deadline will be communicated by Lloyd's once the impacts of the MTE are understood.

**Major model changes**
Following the MTE, syndicates may require a major change to their internal models. These would be categorised into:

- **Simple major changes related to business plans resubmissions:**
  Data changes related to amendments to business plans for existing lines of business will be categorised as a simple major change. Data, parameter and risk profile changes not related to any new line of business will also be included in this category following the MTE. These would be considered in line with business and capital approval timeframes. See section 6 for further details.

- **Fundamental major changes related to plan, parameters and methodology:**
  These types of changes would not be approved by Lloyd's in the same timeframe as business plan approval.

  Managing Agents will be expected to submit a major model change application to Lloyd's along with relevant information within 3 – 6 months of the MTE. This will follow the usual major model change (both qualitative and quantitative) approval process. Regulatory restrictions may apply if a syndicate fails to provide necessary information for a major model change (as a result of the MTE). Details of the deadline will be communicated by Lloyd's once the impacts of the MTE are understood.

7.2

## 2. Principle 2 – Management of failing syndicates

It is likely that some syndicates/members will fail following an MTE. Lloyd's will ensure that the run off of those syndicates are managed in an orderly fashion to minimise any wider impact to the market.

### 7.2.1 Run-off Procedures

The classification of a new run off following a MTE will determine the level of Lloyd's involvement. The classification will be based on a combination of the tiering mechanism and a risk assessment of the Managing Agent/ syndicate against a risk matrix.

The tiering mechanism will be automated and run on a quarterly basis. This will allow Lloyd's to classify run offs into three tiers each representing different risk to the Central Fund. The process addresses volatility of run offs using the following criteria:

- Size and movement in reserves
- Maturity of run off
- Aggregate results

The tiering process is designed to monitor all run-offs so that any deterioration in a run-off will be identified, especially where they may become a threat to the Central Fund.

- **Tier 1: High risk and volatility** – represents a greater than £10m impact to the Central Fund and reserves of £200m or more; Lloyd's immediate involvement

- **Tier 2: Moderate risk and volatility** – represents a greater than £10m impact to the Central Fund with reserves of less than £200m; Lloyd's immediate involvement

- **Tier 3: Lower risk and volatility** – represents a less than £10m impact to the Central Fund; Lloyd's run-off Guidance

Tiering is required in order to respond appropriately to Managing Agents' needs. This is particularly relevant when it comes to resourcing adequacy in a syndicate which is highly likely to move into runoff. The following will vary according to the tier in which a runoff falls:

- The immediacy of Lloyd's involvement
- The level of diligence undertaken in Lloyd's review
- The degree to which Lloyd's will participate in Managing Agent's decision making processes
- The attendance of Lloyd's at the Managing Agent's committee meetings
- The degree to which Lloyd's gives guidance and involvement in any outsourcing
- The frequency and depth of claims and/or reinsurance asset reviews
- The degree to which Lloyd's engages with the Investment Management function

### 7.2.2 Organisation, Resourcing and Resource Allocation

When a new run-off is identified, an internal multi-disciplinary team will be assembled to carry out an immediate review of the run off syndicate. A team leader will be appointed. The team leader would be the current run-off Executive or an experienced Account Manager or Underwriting Executive. The priority being to assess the risks associated with the run-off and to stabilise the environment. The team will include:

Full members:

- Run-off Executive(s)
- Account management expertise
- Underwriting expertise
- Claims expertise
- Reinsurance expertise

With support from the following Corporation teams:

- Accounting
- Actuarial
- Syndicate capability oversight

### 7.2.3 Recovery and Resolution Planning

Recovery and Resolution Planning provides the basis of managing run-off businesses. In advance of an MTE, syndicates should ensure their plans are up-to-date and also think about the practicality of executing them.

## 7.3 3. Principle 3 – Stakeholder / data collection / coordination and communication

Lloyd's would look to take a lead with coordinating interaction and collation of data with key external stakeholders (e.g. regulators, governments, rating agencies) minimising any duplication where possible.[4]

### 7.3.1 Data submissions (losses/claims)

In order to understand the impacts of the MTE, both Lloyd's and the PRA would need to request similar data from syndicates. In most circumstances Lloyd's and the PRA would work together in order to avoid and minimise duplication with regards to information requests from syndicates during an MTE.

Information requests will be made using a mutually agreed data template in which information will be shared between the PRA and Lloyd's regarding syndicates. The template has been provided in the appendix of this document in order to help syndicates in advance understand the information both Lloyd's and the PRA are likely to request in such circumstances.

Syndicates are expected to review the template and consider the type of information that is likely to be useful to, and required by, Lloyd's and the PRA at the time of an MTE, and to consider what steps can be taken in advance to provide this information at short notice.

It is entirely possible that the information detailed in the template would be refined in response to an actual MTE (mutually agreed between Lloyd's and the PRA) – further details will be communicated at the time of issuance.

**Note:** As detailed under section 7.1.1 ('Lloyd's preliminary assessment') the timing and speed at data will be requested and submitted to Lloyd's/PRA would be very dependent on the type of the MTE (i.e. whether or not it is known / included within existing modelling).

### 7.3.2 Communication

On behalf of the market, centrally Lloyd's would look to lead and coordinate the majority of external communication with key stakeholders. Communication would breakdown mainly into the two broad categories: (1) Initial or immediate and; (2) Ongoing.

A wide range of external communication would need to be prepared and executed. The following list is an illustration and is not exhaustive:

- PRA / local regulators – Lloyd's would need to immediately have to have an open line of communication with the PRA and local regulators where the MTE has impacted. The form of communication would be Lloyd's initial view on the MTE itself and the associated impacts. The line of communication would be strongly maintained as further details materialises about the event. Lloyd's would be very keen to keep a close dialogue with local regulators, and in particular where impacts to trust fund requirements could be seen.
- Lloyd's market (mainly Managing Agents) – providing details of key contacts and actions required; understanding where support and guidance may be required from the Corporation
- Rating agencies / investor relations – Lloyd's would coordinate and provide relevant information required by rating agencies on behalf of all syndicates
- Media – Lloyd's would liaise with media and answer questions / interviews as required

4 In principle, Lloyd's will follow its prescribed procedures for syndicates that are not able to trade forwards, these are described in the Corporation's byelaws and bulletins.

# Opportunities following an MTE

## 4. Principle 4 – Support to the market

**Support will be given to the market in responding to opportunities arising from an MTE which ultimately supplies capacity to clients. Where possible, activities in support of existing businesses may be prioritised ahead of new entrants.**

## 5. Principle 5 – Accelerated key processes

**Lloyd's approach will be commercial and pragmatic. This may include the use of an accelerated version of syndicate business and capital plan review/ approval process.**

## 6. Principle 6 – Lloyd's priorities

Corporation staff will focus on supporting the market in response to the event – potentially all other non-essential[2] central activities will be temporarily suspended

# 8. Opportunities following an MTE

8.1 **4.** **Principle 4 – Support to the market**
Support will be given to the market in responding to opportunities arising from an MTE which ultimately supplies capacity to clients. Where possible, activities in support of existing businesses may be prioritised ahead of new entrants.

8.2 **5.** **Principle 5 – Accelerated key processes**
Lloyd's approach will be commercial and pragmatic. This may include the use of an accelerated version of syndicate business and capital plan review/ approval process.

### 8.2.1 Business and capital plan approval

Lloyd's would aim to condense its review and agreement process of business and capital plans to support syndicates in taking advantage of the opportunities available following an MTE.

1. **Immediate approval of increased premium (within existing levels)**

   Syndicates can be free, without any prior approval from Lloyd's, to immediately increase premium volumes in business classes where they identify a supply / demand imbalance following an MTE.

   With appropriate underwriting resource and experience, the increase would be permitted up to pre-approved SBF GWP levels and within the whole account limit.

   Capital to support underwriting will be charged by Lloyd's at the new improved premium rates observed.

2. **Approval of increased premium (outside existing levels)**

   If syndicates seek to take opportunity of improved premium rates which exceed their current whole account SBF premium levels then additional capital would be needed which would be charged by Lloyd's at the new improved premium rates observed.

3. **Opportunities in new lines of business**

   Syndicates may see opportunities to write new business where they may not necessarily have the underwriting resource or experience. Immediately Lloyd's will actively support syndicates to register on Consortium arrangements in these classes to help facilitate writing extra new business.

   Longer term Lloyd's will look to fast track business plan applications where the appropriate underwriting resource and experience is in place.

**Notes:**
In all three instances above, if there is a material change in business mix - Lloyd's will review on a case-by-case basis and apply appropriately deemed capital loads.
Managing Agents would be assessed on merit, with the capability of delivery being considered as part of approval and any conditions or controls attached to that approval.

4. **High level conditions needed for a quicker approval process**

   In order to assist Lloyd's in condensing the business and capital plan approval process for syndicates, it would be beneficial to syndicates:

   – To provide Lloyd's with comfort that they are solvent and able to trade forwards

   – Ensure contingency plans have already been shared and there is evidence of actions being taken in line with these plans e.g. capital replenishment

   – Ensure additional capital is provided through existing approved member(s)

5. **Syndicate submissions for business and capital planning**

   Condensed Syndicate Business Forecast ("SBF") and Lloyd's Capital Return ("LCR") templates would form the basis of the submissions as follows:

   – The SBF submission would consist of the 'High Level Plan' template, an illustration of the fields which are likely to be requested are provided in the Appendix. A full SBF submission will be required 3 months after the initial High Level Plan submission.

   – The LCR submission would consist of the 'MTE template', illustrations of the fields which are likely to be requested are provided in the Appendix. A full LCR submission will be required 3 months after the initial MTE template submission.

   Note: the templates could change depending on the specific MTE; Lloyd's will issue the templates to syndicates at the time of the MTE providing detailed guidance and instructions.

6. **Lloyd's condensed timescales**

   The Capital and Planning Group (CPG) will aim to conduct its review / approval process within the condensed timeframe between 2 to 3 weeks.

**Note:** these timings are indicative and only act as a guide for syndicates.

### 8.2.2 New capital (management and provision)

**Type of new capital**
The type of capital to support either the replenishment of solvency deficits, increased underwriting of new syndicates or the underwriting of new SPAs would need to be of an appropriate quality which enables Lloyd's to meet aggregate tiering requirements defined under Solvency II rules.

Members should at a minimum plan on providing tier 1 capital to replenish solvency deficits or converting existing tier 2 assets. Those who wish to submit tier 2 forms of capital (e.g. letters of credit) to support increased underwriting as detailed above will be subject to the appropriate Ancillary Own Funds approval process required under Solvency II.

**Note:** Currently work is underway centrally to look at various options with regards to capital planning actions which could be implemented now to further increase flexibility in accepting tier 2 forms of capital post an MTE.

Collateralised reinsurance will be considered as an option as an acceptable form of new capital. Collateral levels and any basis risk will be need to be considered, as well as the possibility for giving credit for cessions from GWP.

**New members**
The preferred route of new capital for syndicates is via existing approved corporate members or part approved members.

Capital in the form of Insurance Linked Securities (ILS) will be considered in light of the basis risk between the capital offered and risk assumed.

Managing Agents should consider how any new members can support future underwriting i.e. the point in time of the year of the MTE would play a significant part in this consideration in order to support new year of account underwriting.

In order to shorten the approval time and process of new members, Managing Agents can ensure that they have 'shelf' corporate members' part approved by Lloyd's. This will enable an efficient process to be followed for new capital for syndicates who are wishing to take advantage after an MTE and write new or more business. Currently there are number of mandatory checks required (e.g. anti-money laundering) when setting up a new member – getting some of these completed in advance of an MTE will be an advantage to syndicates and new members willing to invest in Lloyd's syndicates.

**Use of Special Purpose Arrangements ('SPAs')**
To support syndicates in quickly responding to take advantage of hardening rates, SPAs can act as the vehicle for new capital.

Syndicates can apply for an SPA to support new investment capital to support post MTE underwriting subject to the following conditions:

- The host syndicate is unable to increase intake of capital through the existing approved corporate member structure
- Lloyd's would need to be comfortable with the overall strategy the syndicate is adopting which would be validated through the CPG process

Following a market turning event, Lloyd's will be flexible in the level of retention required under an SPA.

**SPA Application Process:**
The approval times for SPAs will be brought in line with business plan approval as set out in the section 8.2.1 above – CPG would be responsible for SPA approval (as opposed to the NEAG, Lloyd's Executive Committee and Franchise Board).

While SPA's will initially be considered subject to 'High Touch' status, once approved by CPG those established in response to a MTE will be only subject to an abbreviated Making It Happen process (see table below).

**Release of capital**
The release of members' surplus funds will be based on the release test statements which are produced bi-annually. There will be no change to this process following a market turning event.

**Current SPA Application Process**

**Stage 1:** Enquiry – Proof of concept

**Stage 2:** High Level Pitch (HLP)

**Stage 2a**: Model indicative capital requirement

**Stage 3:** Detailed Plan presentation to the New Entrant Assessment Group (NEAG)

**Stage 3a:** Capital and Planning Group (CPG) reviews initial Business (Underwriting) Pl

**Stage 4:** Lloyd's committee request 'in principle approval from Lloyd's Executive Team and Franchise Board

**Stage 5:** Making it Happen (may include a review of compliance with Lloyd's Minimum Standards)

**Stage 6a:** Business Plan and Economic Capital Assessment (ECA) (capital) agreement – Capital and Planning Group

**Stage 6b:** Agree output of Minimum Standards Review – Standards Assurance Group

**Stage 6c:** Formal approval – New Entrant Assessment Group

**Stage 7:** Post-approval – 'High touch' status

**MTE SPA Application Process**

**Stage 1:** Enquiry – Proof of Concept – High Level Pitch – Model of Capital Requirement (addressed toCPG and MRC respectively)

**Stage 2:** Capital and Planning Group (CPG) reviews and gives 'approval' in the appropriate instance to initial Business (Underwriting) Plan and Economic Capital Assessment (ECA)

**Stage 3:** Abbreviated Making It Happen process (may include Minimum Standards evaluation)

**Stage 4:** Post-approval – 'High touch' status and submission of revised ECA for the Host.

## 8.3 6. Principle 6 – Lloyd's priorities

Corporation staff will focus on supporting the market in response to the event – potentially all other non-essential[5] central activities will be temporarily suspended

Following an MTE, the Lloyd's main priority will be to ensure the stability of the market. All non-essential activities which are conducted centrally will be temporarily suspended. Lloyd's will communicate with Managing Agents specific details of requirements following an event.

### 8.3.1 Mandatory reporting during an MTE

Syndicates prepare a number of returns to enable Lloyd's to exercise the required level of oversight and report solvency and financial information to the PRA and other stakeholders. Obtaining the information needed to enable Lloyd's to continue to exercise oversight and meet its reporting obligations will continue to be a priority as such the following returns will continue to be collected from the market.

**Critical (i.e. to determine solvency)**

- Quarterly Solvency Return
- Quarterly Asset Data

**Collected as part of Lloyd's oversight of Managing Agents (list not exhaustive)**

**Note:** Lloyd's will provide further details and guidance following the MTE about submission of the following returns. Depending on the time of the year the MTE occurs, some returns could be deferred

- Quarterly Monitoring Return Part A
- Quarterly Monitoring Return Part B
- Lloyd's Capital Return
- Performance Management Data Return
- Realistic Disaster Scenarios
- Lloyd's Catastrophe Model returns
- Syndicate Reinsurance Structure
- Actuarial Function Report
- Statement of Actuarial Opinion
- Technical Provisions Data
- Syndicate ORSAs

5 Non-essential being not business critical or legal requirements

# Appendices

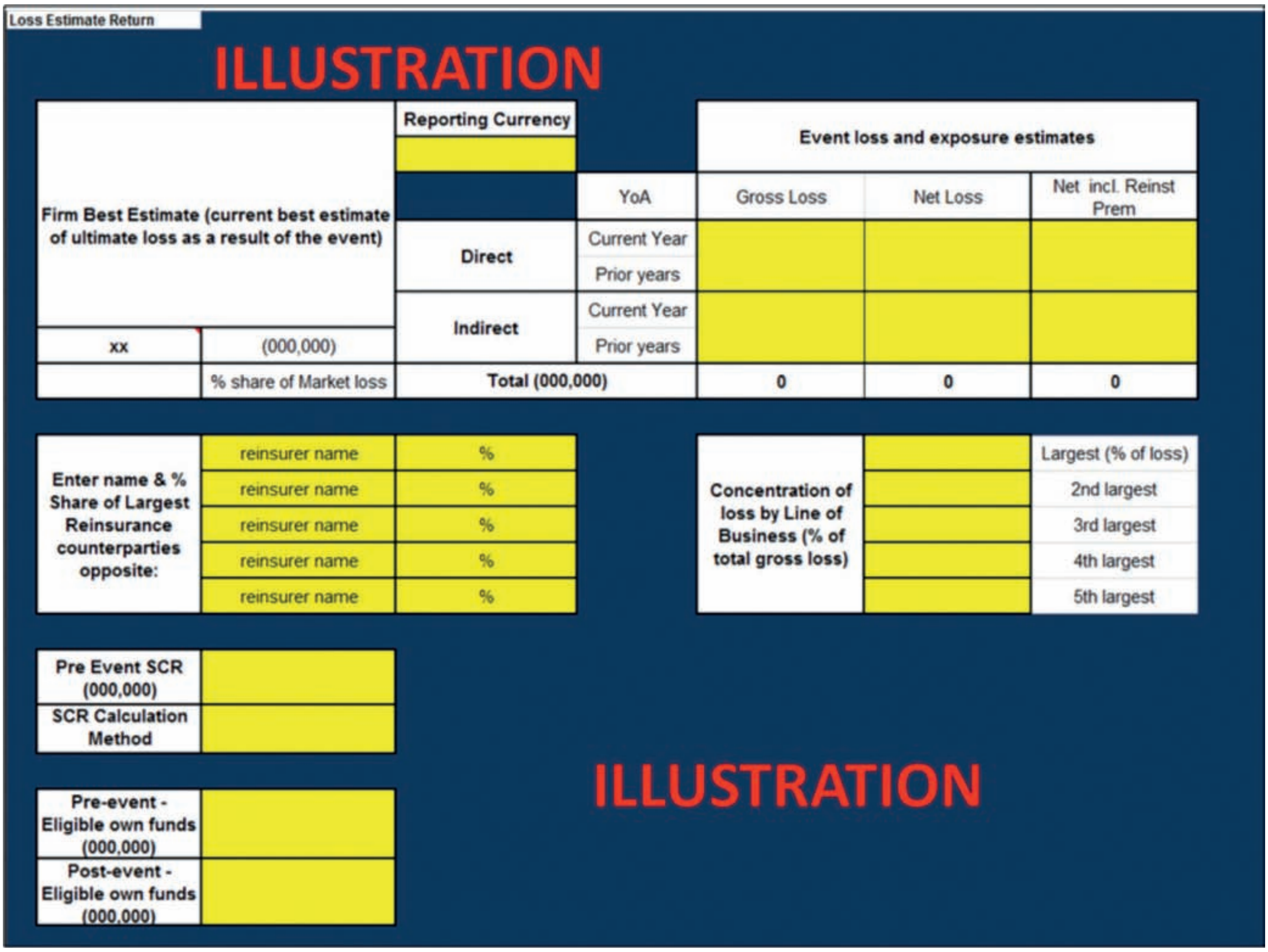
# 9. Appendix – MTE template illustration

The following is an illustration of the template used to collect MTE information from syndicates. In efforts to try and avoid duplication, it is based on the MTE template included in the PRA supervisory statement on MTE issued in July. Following an MTE, the creation of this template will be coordinated between Lloyd's and the PRA and will be communicated with syndicates.

Page 1 – Cover sheet:

| | |
|---|---|
| Agent Name: | |
| Syndicate Number: | |
| Signed off by (Name): | |
| Signed off by (Role): | |
| Signed off date: | |
| Completed by / Contact Name: | |
| Contact Telephone Number: | |
| Date of Completion: | |

Page 2 – illustration of loss estimate data to be collected (based on PRA supervisory statement)



Loss Estimate Return

ILLUSTRATION

| | | | | Event loss and exposure estimates | | |
|---|---|---|---|---|---|---|
| Firm Best Estimate (current best estimate of ultimate loss as a result of the event) | | Reporting Currency | YoA | Gross Loss | Net Loss | Net incl. Reinst Prem |
| | | Direct | Current Year | | | |
| | | | Prior years | | | |
| xx | (000,000) | Indirect | Current Year | | | |
| | | | Prior years | | | |
| | % share of Market loss | Total (000,000) | | 0 | 0 | 0 |

| Enter name & % Share of Largest Reinsurance counterparties opposite: | | |
|---|---|---|
| | reinsurer name | % |
| | reinsurer name | % |
| | reinsurer name | % |
| | reinsurer name | % |
| | reinsurer name | % |

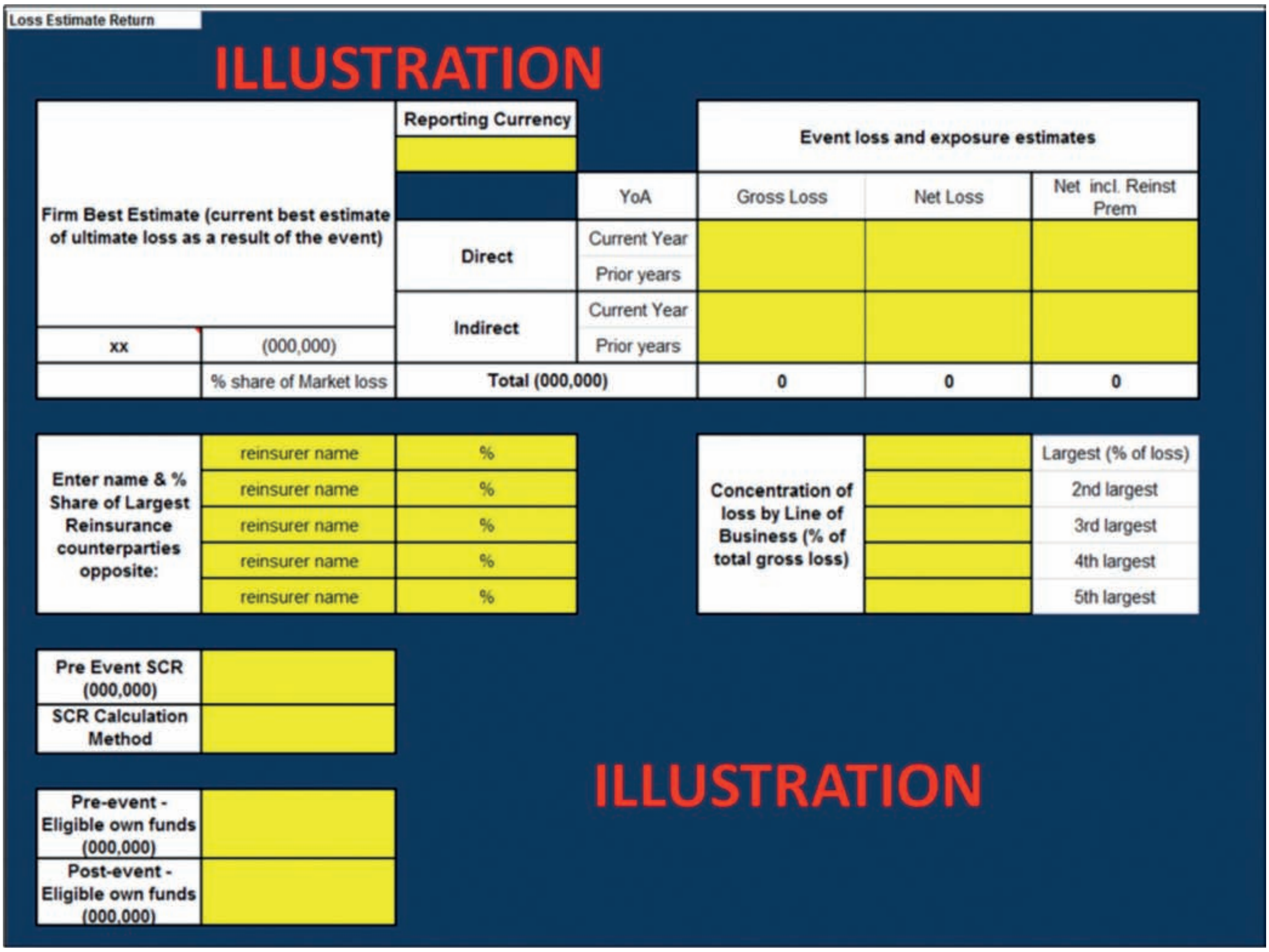
| Concentration of loss by Line of Business (% of total gross loss) | | |
|---|---|---|
| | | Largest (% of loss) |
| | | 2nd largest |
| | | 3rd largest |
| | | 4th largest |
| | | 5th largest |

| | |
|---|---|
| Pre Event SCR (000,000) | |
| SCR Calculation Method | |

| | |
|---|---|
| Pre-event - Eligible own funds (000,000) | |
| Post-event - Eligible own funds (000,000) | |

ILLUSTRATION

Page 3 – examples of qualitative / supplementary questions (based on PRA supervisory statement)



Loss Estimate Return

ILLUSTRATION

| | | | | | | |
|---|---|---|---|---|---|---|
| Firm Best Estimate (current best estimate of ultimate loss as a result of the event) | | Reporting Currency | | Event loss and exposure estimates | | |
| | | | YoA | Gross Loss | Net Loss | Net incl. Reinst Prem |
| | | Direct | Current Year | | | |
| | | | Prior years | | | |
| xx | (000,000) | Indirect | Current Year | | | |
| | | | Prior years | | | |
| | % share of Market loss | Total (000,000) | | 0 | 0 | 0 |

| | | |
|---|---|---|
| Enter name & % Share of Largest Reinsurance counterparties opposite: | reinsurer name | % |
| | reinsurer name | % |
| | reinsurer name | % |
| | reinsurer name | % |
| | reinsurer name | % |

| | | |
|---|---|---|
| Concentration of loss by Line of Business (% of total gross loss) | | Largest (% of loss) |
| | | 2nd largest |
| | | 3rd largest |
| | | 4th largest |
| | | 5th largest |

| | |
|---|---|
| Pre Event SCR (000,000) | |
| SCR Calculation Method | |

| | |
|---|---|
| Pre-event - Eligible own funds (000,000) | |
| Post-event - Eligible own funds (000,000) | |

ILLUSTRATION

Page 4 – illustration of capital information (additional items requested by Lloyd's)

Data to be provided on a one-year balance sheet to balance sheet basis and on an ultimate basis

| Insurance Risk | |
|---|---|
| 1 | Total: After diversification between Premium and Reserve Risk |
| 2 | Split: Premium Risk |
| 3 | Split: Reserve Risk |
| Credit Risk | |
| 4 | Total: After diversification between Reinsurance Credit Risk and Other Credit Risk |
| 5 | Split: Reinsurance Credit Risk |
| 6 | Split: Other Credit Risk |
| 7 | Market Risk |
| 8 | Operational Risk |
| 10 | Diversification credit between risk categories |
| 11 | Diversified total |

# 10. Appendix – High level plan

As described in section 6, the High Level Plan template will be used as the initial SBF submission from syndicates followed up by a full SBF return 3 months later. The below fields are indicative of the information that syndicates would need to provide in the High Level Plan

| | |
|---|---|
| Gross Written Premium (GWP): | |
| Gross Ultimate Loss Ratio (GULR %): | |
| RI Spend % GWP: | |
| Net Ultimate Loss Ratio (NULR %): | |
| Admin % GWP: | |
| Acquisition Cost % GWP: | |
| Combined Ratio %: | |
| Net underwriting Result: | |
| Capacity: | |

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