



**SOLVENCY II PILLAR 3
MARKET WORKSHOPS
17 & 18 SEPTEMBER 2013**

AGENDA

- ▶ **Introduction**
- ▶ **Asset data collection (QAD)**
 - **Feedback on submission at Dec 2012**
 - **Requirements for submission at Sept 2013**
- ▶ **SII Balance Sheet (QMC) at June 2013**
- ▶ **Table discussion**
- ▶ **2013 year end requirements**
- ▶ **EIOPA Pillar 3 interim measures**
- ▶ **Future accounting developments**

SOLVENCY II PROJECT UPDATE

- ▶ 2013 “**Soft Landing**” approach
- ▶ Quantitative requirements apply immediately to support use of Solvency II models
- ▶ Hard Test submissions treated as BAU and should comply with all relevant requirements
 - SCR
 - TPD return
 - GQD return
 - Solvency II Balance Sheet (QMC)
 - LIM Asset Return (QAD)

SOLVENCY II PROJECT UPDATE

- ▶ Qualitative requirements phased in over 2013 to 2016
- ▶ Soft Test submissions should be made on a best efforts basis
 - ORSA
 - Actuarial Function Report
 - Model Change Report
 - Validation Report

SOLVENCY II PROJECT UPDATE

PHASING OF SOLVENCY II WORKSTREAMS UNDER "SOFT LANDING"

WORKSTREAM/ELEMENT	2013	2014	2015	2016	RATIONALE
INTERNAL MODEL SCR					
IMSCR Insurance risks					Ult SCR req'd for capital setting/ 1 yr number soft test
IMSCR Other risks					Ult SCR req'd for capital setting/ 1 yr number soft test
IMSCR Aggregate SCR					Ult SCR req'd for capital setting/ 1 yr number soft test
VALUATION AND BALANCE SHEET					
VBS Valuation of assets & liabilities (excluding technical provisions)					required to use SII models for capital setting
TECHNICAL PROVISIONS AND STANDARD FORMULA					
SFSCR Standard formula SCR					Caveat re pot'l data requests from FSA/EIOPA
TP Valuation process					Full Solvency II TPs needed
TP Valuation methodology					Full Solvency II TPs needed
TP Data					Apply to current level/standards
TP Assumptions					Apply to current level/standards
TP Validation					Apply to current level/standards
MODEL VALIDATION					
SQS Probability distribution forecast and risk ranking					L1 aligns with ICAS principles - L2 addtl granularity
SQS Methodological adequacy					L1 aligns with ICAS principles - L2 addtl granularity
SQS Methodological consistency and credibility					L1 aligns with ICAS principles - L2 addtl granularity
SQS Assumptions					L1 aligns with ICAS principles - L2 addtl granularity
SQS Data directory and data policy					Aligns with ICAS principles - some addtl
SQS Dependencies					L1 aligns with ICAS principles - L2 addtl granularity
SQS Risk mitigation techniques					L1 aligns with ICAS principles - L2 addtl granularity
SQS Fincl gtees and options, future mgmt actions and non cont pymts					L1 aligns with ICAS principles - L2 addtl granularity
CVP Calibration					Reconciliation of 1 year and ultimate SCR
CVP Validation					Solv II process should continue/system maintained
CVP Profit and loss attribution and backtesting					backtesting under ICAS- defer P&L
CVP Model robustness and stress and scenario testing					L1 aligns with ICAS principles - L2 addtl granularity
EMD External models and data					In scope & validation requirements - Cat & ESG
GOVERNANCE, RISK MANAGEMENT AND USE					
SOG General governance requirements					Already BAU/good risk mgmt practice
SOG Fit and proper					Already BAU/good risk mgmt practice
SOG Risk management					Already BAU/good risk mgmt practice - RMF addtl
SOG Internal control					Already BAU/good risk mgmt practice
SOG Internal audit					Already BAU/good risk mgmt practice
SOG Actuarial function					Required to support TPs but not UW/RI til 2016
SOG Outsourcing					Already BAU/good risk mgmt practice - some addtl
MSG Risk coverage					Aligns with ICAS principles - some addtl
MSG Use test					partial ICAS requirement - significantly increased
MSG Model governance					Solv II process should continue/system maintained
MSG Model change policy					Solv II process should continue/system maintained
ORSA ORSA process					Solv II process should continue/system maintained
ORSA ORSA documentation					Solv II process should continue/system maintained
ORSA ORSA outcomes					Solv II process should continue/system maintained
REPORTING AND DISCLOSURE					
SREP Supervisory reporting and disclosure					Remain in project phase through 2013/2014
DOCUMENTATION AND FINAL APPLICATION					
DOC Documentation process					Solv II process should continue/system maintained
DOC Design and operational details					Aligns with ICAS principles - some addtl
DOC Theory, assumptions, mathematical and empirical basis					Aligns with ICAS principles - some addtl
DOC Circumstances where the model does not work effectively					Aligns with ICAS principles - some addtl
DOC Model change documentation					Solv II process should continue/system maintained
APP Final application pack					Further final applic may be needed pre implem'n



Hard requirement



Required to current level - ICAS/Solv1/Lloyds min standards (Solv II development to continue)



Full Solv II hard requirement - must meet standards with full formal submissions as appropriate



Solv II soft requirement - should be operational and Lloyd's will review submissions and provide feedback/guidance



Solv II slow down/remains in "project" status



n/a



Project status

PRESSURE IN EUROPE TO AGREE OMNIBUS II...

- ▶ Pressure to finalise Omnibus II
 - Long Term Guarantee Package is main remaining issue
 - European Parliament vote now likely early 2014
 - 2016 Solvency II start date can still be achieved
 - But 2017 should not be ruled out

- ▶ Level 2 measures will follow Omnibus II
 - Likely publication Spring 2014
 - 6 months for European Parliament to consider

... MEANS SOLVENCY START OF 2016 CAN STILL BE MET

EIOPA AND PRA PROVIDING STEPPING STONES TO SOLVENCY II

- ▶ EIOPA Interim Measures cover Pillar 2 and Pillar 3
 - Final measures due to be published late 2013 following consultation earlier this year
 - Phased introduction of Pillar 2 measures from 2014, consistent with Lloyd's current approach
 - Pillar 3 requirements likely to apply from 31 December 2014

- ▶ PRA moving towards ICAS+
 - Capital setting using Solvency II internal models and balance sheets consistent with Lloyd's approach
 - Potential impact of 'Early Warning Indicators' unclear and of concern

MANY ASPECTS OF SOLVENCY II BAU AT LLOYD'S

- ▶ Solvency II models and balance sheets used to set capital
- ▶ Calculation of Solvency II technical provisions well established
- ▶ Solvency II standard risk management practices being embedded
- ▶ Use Test requirements being reflected in governance processes

- ▶ Completion of Pillar 3 work is main remaining task

FEEDBACK FROM LAST WORKSHOP IN JUNE

- ▶ Agents said that the September workshop should cover:
 - QAD live data collection at 30 Sept 2013
 - Year end requirements (including QMC)
 - Planned Pillar 3 work for 2014
 - Pillar 3 interim measures

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THE QAD 'DRY RUN' WAS A SUCCESS....

- ▶ The Quarterly Asset Data (QAD) was collected in June, as at 31 December 2012:
 - Submissions were received from all applicable syndicates
 - New Core Market Returns (CMR) templates were used
 - Templates incorporated three of the EIOPA asset data templates and the requirements of the LIM
- ▶ Lloyd's provided the security level analysis for all Lloyd's managed investment funds and the primary sweep accounts
- ▶ Lloyd's has liaised with external asset managers to support the provision of asset data to market participants

... BUT THERE WERE SOME COMMON ISSUES...

- ▶ Reporting of Lloyd's Managed Investment Funds (LMIF):
 - Use the valuations which will be provided to agents by Lloyd's within 10 business days of quarter end
 - Provide a single line entry in both the main investment data form (QAD230) and the investment fund form (QAD236); look through level of 'O'
 - All values must be reported in GBP equivalent
- ▶ Reporting of investment funds (non-LMIF):
 - A single line entry in the QAD230 and the look through in the QAD236; funds must appear in both forms
 - All values must be reported in GBP equivalent
 - Asset ID Code should be unique to each fund; no duplicate IDs to be submitted

... BUT THERE WERE SOME COMMON ISSUES (CONT'D)...

- ▶ Completing the derivatives template:
 - All values in GBP equivalent (Notional Amount and Total Solvency II Amount)
 - Notional Amount should be populated as an absolute number, the direction (-/+ of the transaction will be driven by the Long or Short Position field
 - Forward Foreign Exchange contracts to be entered as two rows with the same Notional Amount, reporting the profit or loss in the Total Solvency II Amount fields
 - Asset ID Code needs to be unique to each transaction
 - For worked examples please email Lloyds-SolvencyReturns@lloyds.com

... AND SOME UNEXPECTED ENTRIES

- ▶ Lloyd's managed investment funds (LMIF) reported at **security level**
 - LMIFs to be reported as a single line entry with an 'O' level of look through and Lloyd's will provide the security level look through
- ▶ Assets identified as 'Mortgages and Loans' of more than £500m
 - CIC XX84 is designed for the issuer of mortgages; ABS and MBS should be classified as either Structured Notes XX5X or Collateralised Securities XX6X
- ▶ 20 submissions included investment funds with no look through; making it impossible for us to assess the risk

QAD GOES LIVE AS AT 30 SEPTEMBER 2013

- ▶ QAD now available in UAT – any comments by 20 September please
 - Please email lloyds-solvencyreturns@lloyds.com
- ▶ The first live collection is as at 30 September 2013, due in on 1 November 2013
- ▶ Data requirements in live data collection unchanged from ‘dry run’
- ▶ Changes to CMR validations to support data quality
- ▶ Managing agent sign-off (QAD910) will be required

- ▶ There will be a subsequent collection as at 31 December 2013, provisionally set for March 2014

WE ARE AWARE THAT DATA LICENCING HAS BEEN AN ISSUE

- ▶ Lloyd's investigated data licencing issues in an attempt to identify a coordinated approach for the Lloyd's Market, but this has not proved possible
- ▶ Each managing agent is responsible for ensuring they have licences with appropriate providers to support the provision of data to Lloyd's
 - See email sent to Solvency II contacts, 31 May 2013
- ▶ Queries to Lloyd's Treasury & Investment Management: Debbie Sallas (Debbie.Sallas@lloyds.com) or Tony Cullum (Tony.Cullum@lloyds.com)

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RELATIVELY FEW QUERIES RAISED BY AGENTS AND AUDITORS ON 30 JUNE QMC...

- ▶ All returns received on time
 - Much appreciated given **very** tight timescales for Lloyd's capital setting process
- ▶ Reduction in 'odd looking' adjustments on
 - Risk margin
 - Notional profit commission
- ▶ **Further evidence that process is moving towards BAU**

...BUT MORE RAISED BY LLOYD'S ON TREATMENT OF RESERVE MARGINS

- ▶ Starting position is that the SAO position is maximum allowed for solvency
- ▶ If implied release per QMC is materially higher than SAO:
 - Lloyd's requests supporting evidence from agents
- ▶ Where evidence is not provided Lloyd's will require either:
 - A revised QMC eliminating the 'excess' release or
 - Apply a loading to the syndicate SCR to eliminate this

KEY POINTS FOR 2013 YEAR END

- ▶ Release of reserve margins **must not** exceed those in SAO
- ▶ Solvency II technical provisions must be consistent with TPD
- ▶ Other key points
 - Completion of QMC002, column A must be consistent with QMA
 - Binary event amounts must be explicitly disclosed in QMC210 line 10
 - Provisions in UK GAAP TPs must be included in reserve margin release on QMC210 line 4 and added back in line 10
 - Correspondence principle must be applied in reporting of RI cashflows
- ▶ **Apply an integrated approach to completion of QMA, QMC and TPD**

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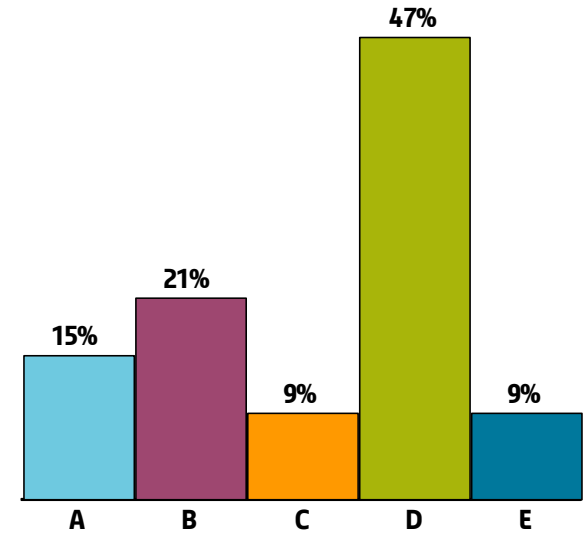
WHAT ARE YOUR MAIN PILLAR 3 CONCERNS?

- ▶ QAD
- ▶ QMC
- ▶ Familiarisation with overall Pillar 3 requirements
- ▶ Preparing for EIOPA interim measures
- ▶ Meeting qualitative reporting requirements

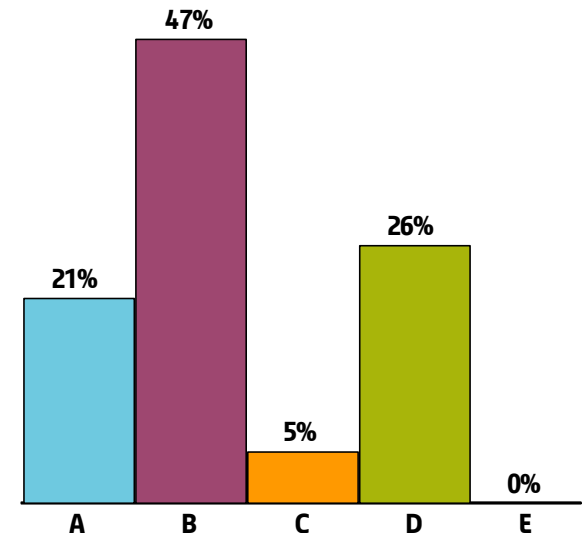
- ▶ What can Lloyd's do to help further?

HOW CAN WE MAKE THE QAD EXPERIENCE BETTER?

- A. Make instructions clearer
- B. Provide worked examples
- C. Provide QAD 'drop in' centre
- D. Maximise central completion of data
- E. Other



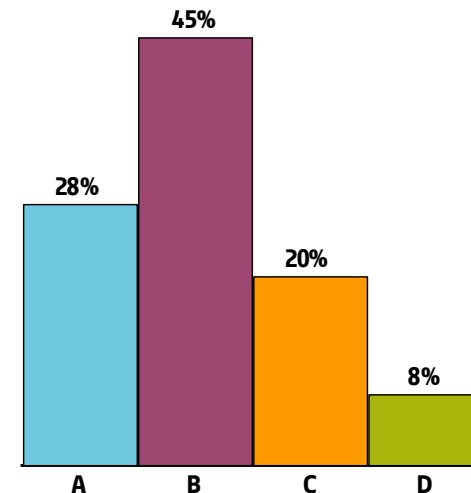
TUESDAY 17TH SEPT 2013



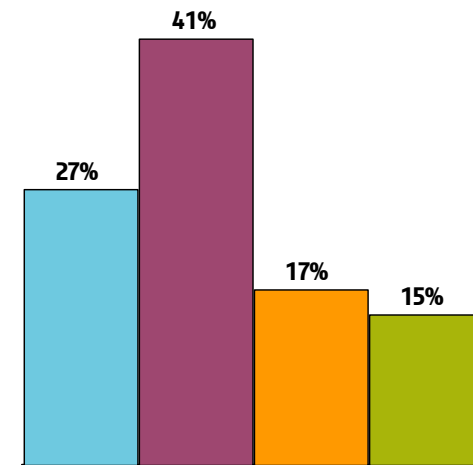
WEDNESDAY 18TH SEPT 2013

WHEN SHOULD WE COLLECT THE YEAR END QAD?

- A. February
- B. March
- C. April
- D. Deadline not a major issue (unless it's January!)



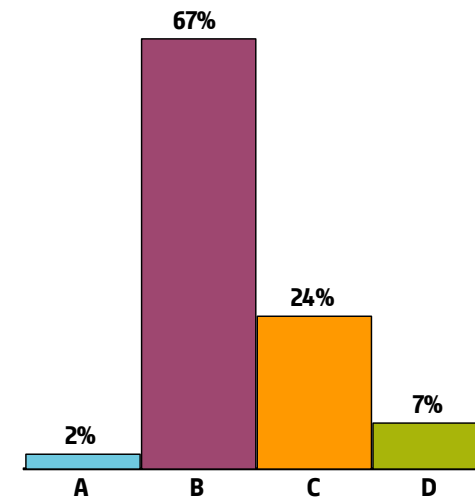
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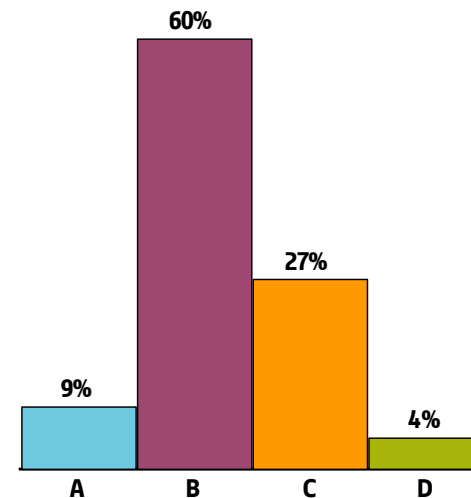
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HOW CAN THE 2013 QMC EXERCISE BE MADE EASIER?

- A. Provide QMC 'surgeries'
- B. Make link between QMC, SAO and TPD more explicit in instructions
- C. Lloyd's engage with auditors to ensure consistent approach to audit
- D. Already a smooth process – no further action needed!



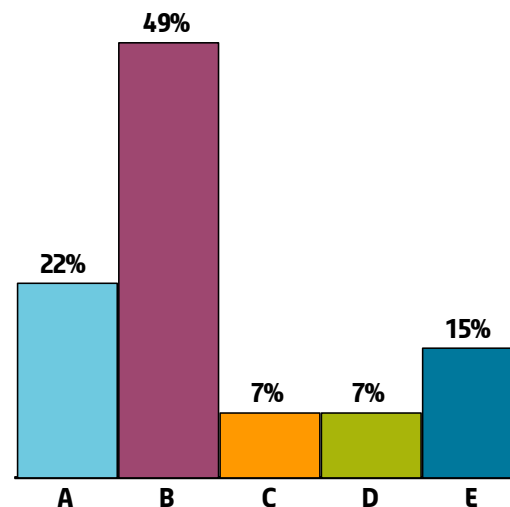
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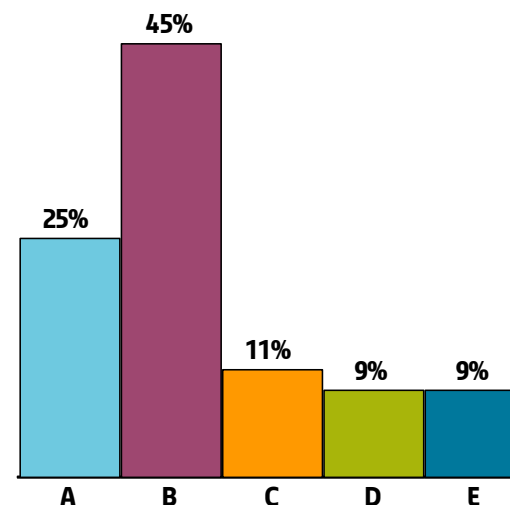
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HOW CAN LLOYD'S HELP AGENTS PREPARE FOR PILLAR 3 IN GENERAL?

- A. Provide workshops on Pillar 3 CMRs
- B. Prepare an illustrative completed set of Pillar 3 CMRs
- C. Issue a pro forma template to address qualitative requirements
- D. Conduct broader dry run to link with EIOPA interim measures
- E. Leave us alone – no more Pillar 3 for the time being please!



TUESDAY 17TH SEPT 2013



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YEAR END REQUIREMENTS

- ▶ 2013 year end requirements similar to 2012
 - Timetable for QMA and gap to QMC unchanged
 - QAD required at 31 December 2013
 - No new Pillar 3 requirements

PLAN NOW FOR YEAR END DECEMBER 2013

Return	Description	Due date
QMA	UK GAAP	Thursday 20 February
QMC	SII Balance Sheet	Thursday 6 March
QAD	LIM Asset Data	TBA – late March

QMC AND QAD STILL A 'LEARNING CURVE' FOR AGENTS AND US!

- ▶ For **QMC**:
 - Plan availability of Finance and Actuarial teams
 - Agree audit review times and finalisation meetings

- ▶ For **QAD**:
 - Engage with internal Treasury team and external investment managers

- ▶ For **both**:
 - Ensure that sufficient management review time is included
 - Organise Board/sub-group meetings ready for sign-off

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PILLAR 3 PROPOSALS ARE SUBSTANTIAL...

- ▶ Annual reporting at 31 December 2014
 - 22 templates covering balance sheet, assets, technical provisions, own funds, SCR and MCR
 - Narrative reporting on system of governance, capital management, valuation for solvency purposes and reporting policy
 - Deadline 20 weeks after year end (shorter deadline for syndicates to Lloyd's)

- ▶ Quarterly reporting at 30 September 2015 (and implied at 31 December 2015)
 - 9 templates covering balance sheet, assets, technical provisions, own funds, SCR and MCR
 - Deadline 8 weeks quarter year end (shorter deadline for syndicates to Lloyd's)

- ▶ Current regulatory reporting requirements will still apply

... BUT LLOYD'S PROPOSALS TO REDUCE THE BURDEN REFLECTED IN RESPONSES TO EIOPA

- ▶ Lloyd's participated in PRA, Insurance Europe and CFO Forum working groups in formulating their responses to EIOPA
- ▶ Lloyd's focus was to propose pragmatic modifications to ease the burden:
 - Only one set of quarterly reporting
 - Allow 12 weeks rather than 8 for the quarterly reporting as it is a 'dry run'
 - IMAP firms should only have to provide summary SCR standard formula information, not have to complete 7 EIOPA templates
 - Should be made clear that 'best efforts' is permitted
 - Both firms and supervisors should use this as a 'learning experience'

LLOYD'S WILL LINK COMPLIANCE WITH PILLAR 3 DRY RUN

- ▶ Four new Solvency II returns in Core Market Returns (CMR):
 - Currently available for UAT
 - Guidance on completion of Solvency II CMRs available on lloyds.com
- ▶ Timings for dry run of full suite of returns dependent on EIOPA interim measures
 - If 'best efforts' permitted, will be conducted as part of interim measures
 - Alternatively, an earlier 'dry' run may be needed, no earlier than Q3 2014
 - Agent requirements for 2014 will be published with 2014 Plan and Guidance Notes
- ▶ Qualitative reporting will only dry run to align with interim measures
 - Detailed 'worked example' will be provided in 2014

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FORTHCOMING CHANGES TO ACCOUNTING REQUIREMENTS WILL AFFECT SYNDICATES

- ▶ Changes to UK GAAP...
 - FRS102 ‘Financial Reporting Standard in UK and Republic of Ireland’
 - FRS103 (FRED49) ‘Insurance Contracts’
 - Applicable from 1 January 2015 (comparatives for 2014)

- ▶ ... and IFRS
 - IFRS4 Phase 2 ‘Insurance Contracts’
 - Revised exposure draft out now
 - Final standard expected late 2014/2015
 - Applicable three years after final standard...2018?

FRS102 IS BROADLY THE SAME AS TODAY'S UK GAAP...

- ▶ Streamlining and consolidation of existing set of UK GAAP
- ▶ A few modifications based on IFRS for small and medium enterprises
- ▶ One key impact on translation of foreign currency:
 - All foreign currency transactions to be translated into the functional currency
 - Monetary items translated at closing rates
 - Non-monetary items such as DAC and UPR translated at historic rates
 - Option to book differences through STRGL **removed**
 - Will affect result and thus tax position for capital providers
 - Restatement of comparatives will affect opening balances at 1 January 2014

...BUT WITH A KEY CHANGE ON FX ACCOUNTING

FRS103 INTENDED TO ALLOW INSURERS TO CONTINUE THEIR CURRENT ACCOUNTING POLICIES...

- ▶ Based on current IFRS4 'Insurance Contracts' but incorporating elements of
 - ABI SORP
 - FRS27 for life business
- ▶ Numbers will be the same as current UK GAAP
- ▶ As FRS103 is based on IFRS4, there are additional disclosures:
 - Reconciliations of changes in insurance liabilities, reinsurance assets and any related deferred acquisition costs
 - Claims development triangulations at whole account level
 - Qualitative information about objectives, policies and processes for managing capital as well as a summary of capital managed.

...BUT WILL REQUIRE MORE DISCLOSURE

IMPACT OF UK GAAP CHANGES ON LLOYD'S

- ▶ Syndicate annual accounts
 - FRS102 impact on treatment of foreign currency
 - Additional disclosures arising from FRS103
- ▶ Lloyd's accounts
 - Aggregate accounts must reflect additional disclosures
 - Additional forms in QMA to collect additional quantitative disclosure
- ▶ Corporate member accounts prepared under Schedule 3 Companies Act 2006
 - Lloyd's will modify central Schedule 3 facility outputs to provide additional quantitative disclosures
- ▶ 2014 comparatives will require restatement to reflect FRS102 foreign currency change

IS IFRS4 PHASE II FINALLY REACHING A CONCLUSION?

- ▶ IASB has been working on 'Insurance Contracts' project since 1997
 - Intention to provide a globally consistent standard for accounting for insurance contracts
 - Current IFRS4 implemented 2004 – allows a wide diversity of insurance accounting
 - Discussion paper 'Preliminary Views on Insurance Contracts' issued 2007
 - First Exposure Draft issued 2010

- ▶ Revised Exposure draft issued July 2013
 - Consultation open until 25 October
 - Final standard expected late 2014/Spring 2015
 - Standard applicable 2018?

MULTI-PART VALUATION OF INSURANCE CONTRACTS SIMILAR TO SOLVENCY II...

Building block element	Comparison with Solvency II
Probability-weighted best estimate (no prudence built in)	Scope of coverage is different under Solvency II (which includes bound but not incepted)
Discount to reflect the time value of money	IFRS allows the insurer to choose discount rate appropriate for its circumstances – Solvency II requires a prescribed rate for all insurers
Explicit risk margin to reflect uncertainty within the best estimate	IFRS allows any reasonable basis with the equivalent confidence level disclosed – Solvency II mandates cost of capital basis
Contractual service margin , ie the unearned profit	Unearned profit not a concept in Solvency II

...BUT NOT THE SAME

NEW EXPOSURE DRAFT REVERTS TO A RECOGNISABLE INCOME STATEMENT

	20XX
Insurance contracts revenue (A)	X
Incurred claims (B)	(X)
Operating result (C = A+B)	X
Investment income (D)	X
Interest expense on insurance liability (E)	(X)
Investment result (F = D+E)	X
Profit or loss (G = C+F)	X
Effect of discount rate changes (H)	X/(X)
Total comprehensive income (I = G+H)	X

Allocation to OCI rather than P&L
being consulted on by IASB

CONSULTATION PROCESS

- ▶ FRS103 (FRED49) – deadline date for comments to FRC 31 October
- ▶ IFRS ‘Insurance Contracts’ – responses to IASB by 25 October

- ▶ Lloyd’s / LMA Accounting Policy Working Group
 - Lloyd’s and LMA
 - Managing agents
 - Audit firms
 - Spread capital providers

- ▶ Group will:
 - Consider impact of accounting changes on Lloyd’s, syndicates and corporate members
 - Review Lloyd’s responses to FRC and IASB
 - Input on guidance on accounting changes to be provided to the market by end 2013

- ▶ Any comments on either consultation to paul.appleton@lloyds.com

COMING UP LATER IN 2013...

Submissions	
Validation Report	26 September
GQD Return	10 October
Board Confirmation Statement	25 October
QAD as at 30 September 2013	1 November

COMING UP LATER IN 2013...

Workshops	
Director's Briefings	15/16 October
ORSA/ Model Change	12/15 November
Risk Assurance	11/12 December

- ▶ Update on interim measures – by end 2013 (hopefully)
- ▶ Draft Solvency II timetable for 2014 to be published later in 2013
- ▶ Slides will be made available on lloyds.com after both sessions

QUESTIONS?

