SOLVENCY II BALANCE SHEET – MARKET WORKSHOPS
11 & 12 JUNE 2013

AGENDA

- Introduction
- December 2012 exercise
  - Quantitative review
  - Qualitative feedback
- Table discussion
- Looking forward
- The broader Pillar 3 scene
- Questions

LLOYD'S APPROACH TO PILLAR 3 REFLECTS UNCERTAIN SOLVENCY II START DATE

- Solvency II delay certain – our planning approach assumes a 2016 start
  - Lloyd's applying soft landing for qualitative requirements…
  - …with Solvency II models now being used to set capital
- Pillar 3 dry run in 2013 scaled back
- Solvency II balance sheet key to supporting SCR
- LIM asset data also key
- Dry run of other forms deferred until 2014 at earliest
  - But are available for agent testing and review
  - Will be impacted by EIOPA interim measures

QMC DESIGNED TO PROVIDE CONSISTENT PLATFORM AND HELP WITH RECONCILIATION

- Solvency II data collection incorporated into Core Market Returns
  - QMC implemented as at 31 December 2012
  - QMC002 Solvency II balance sheet
  - QMC210 Reconciliation of changes in technical provisions

- Reconciliation of reserve adjustments seen as a key issue
  - QMC210 is there to help agents work through this…
  - …to explain to their auditors…
  - …and help Lloyd's understand too!

QMC CHALLENGES ACKNOWLEDGED

- Timetable for submission
- Calculation of technical provisions
- Completion of QMC210
- Engagement between Finance and Actuarial teams
- Audit requirements

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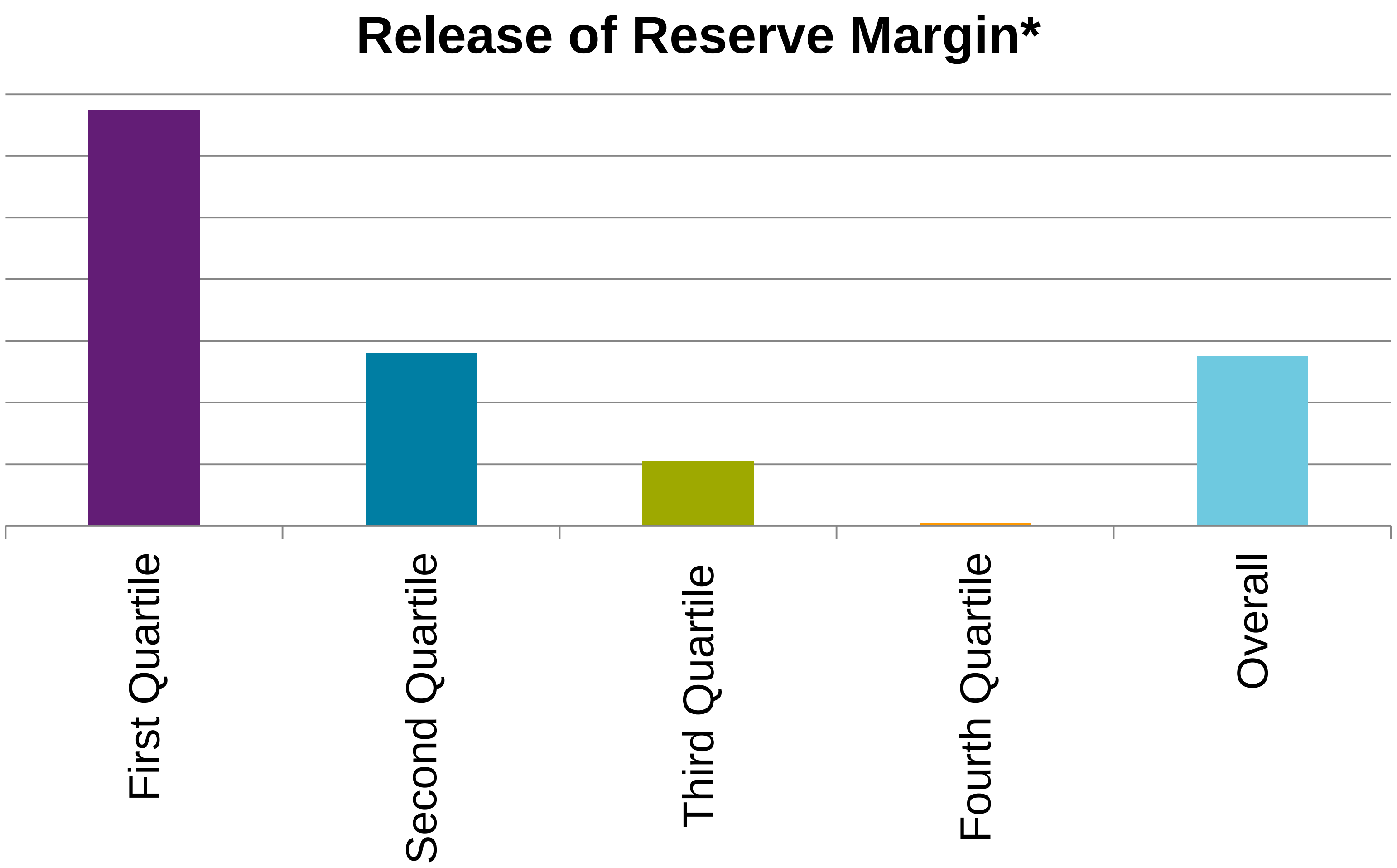
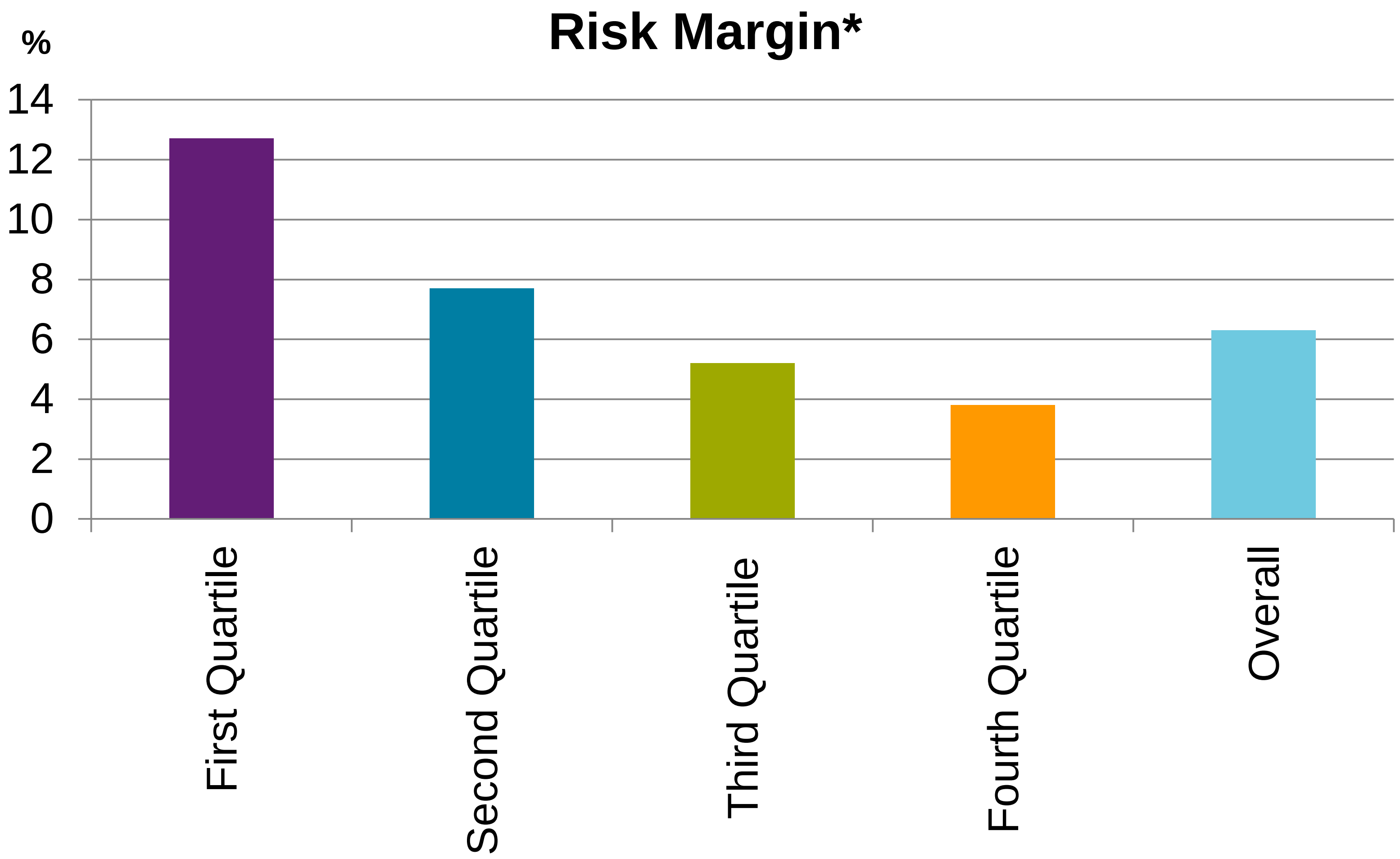
THE IMPACT OF THE RELEASE OF RESERVE MARGIN VARIES WIDELY…



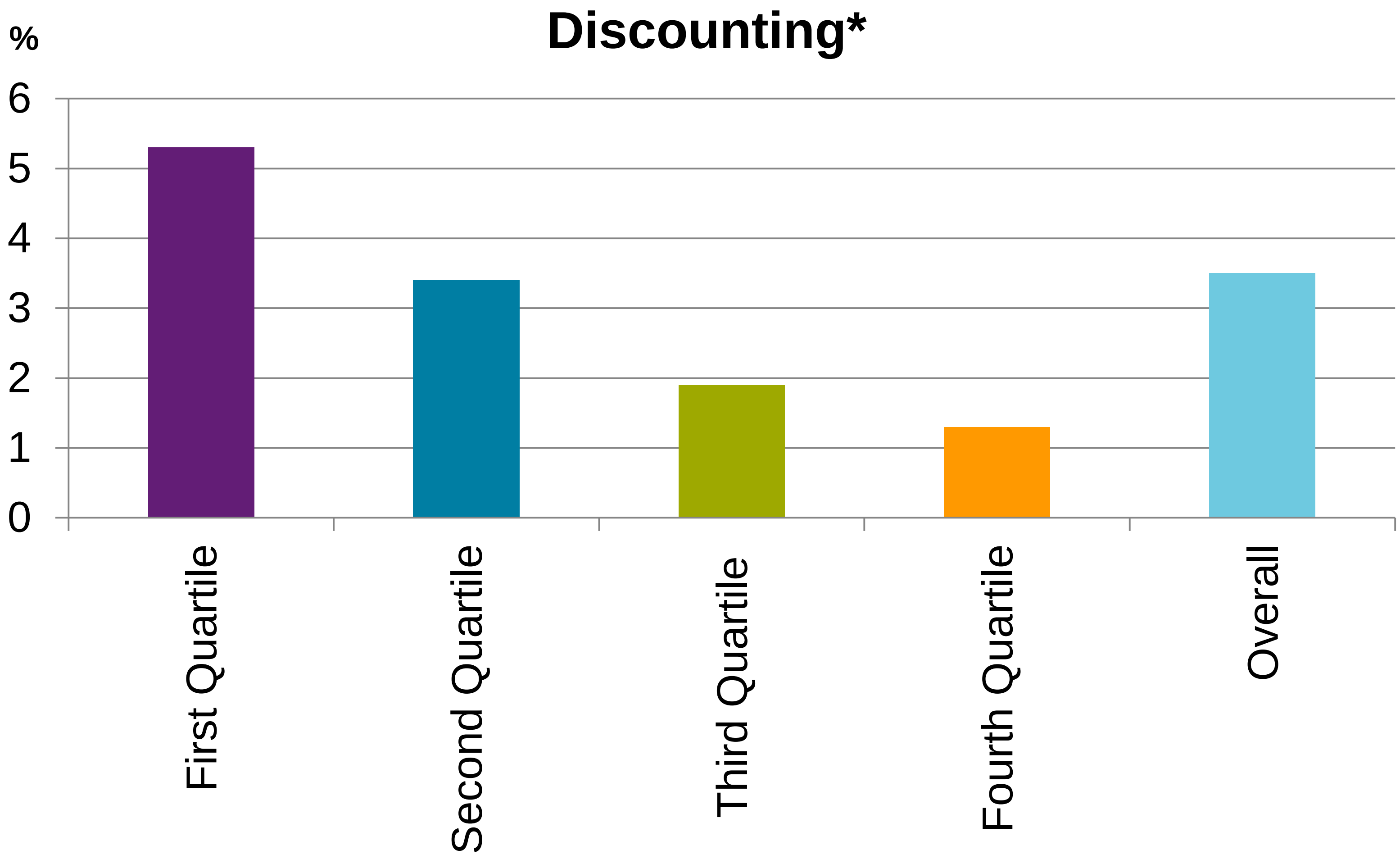
*% of UK GAAP net technical provisions (excluding UPR)

… AS DOES THE IMPACT OF THE RISK MARGIN



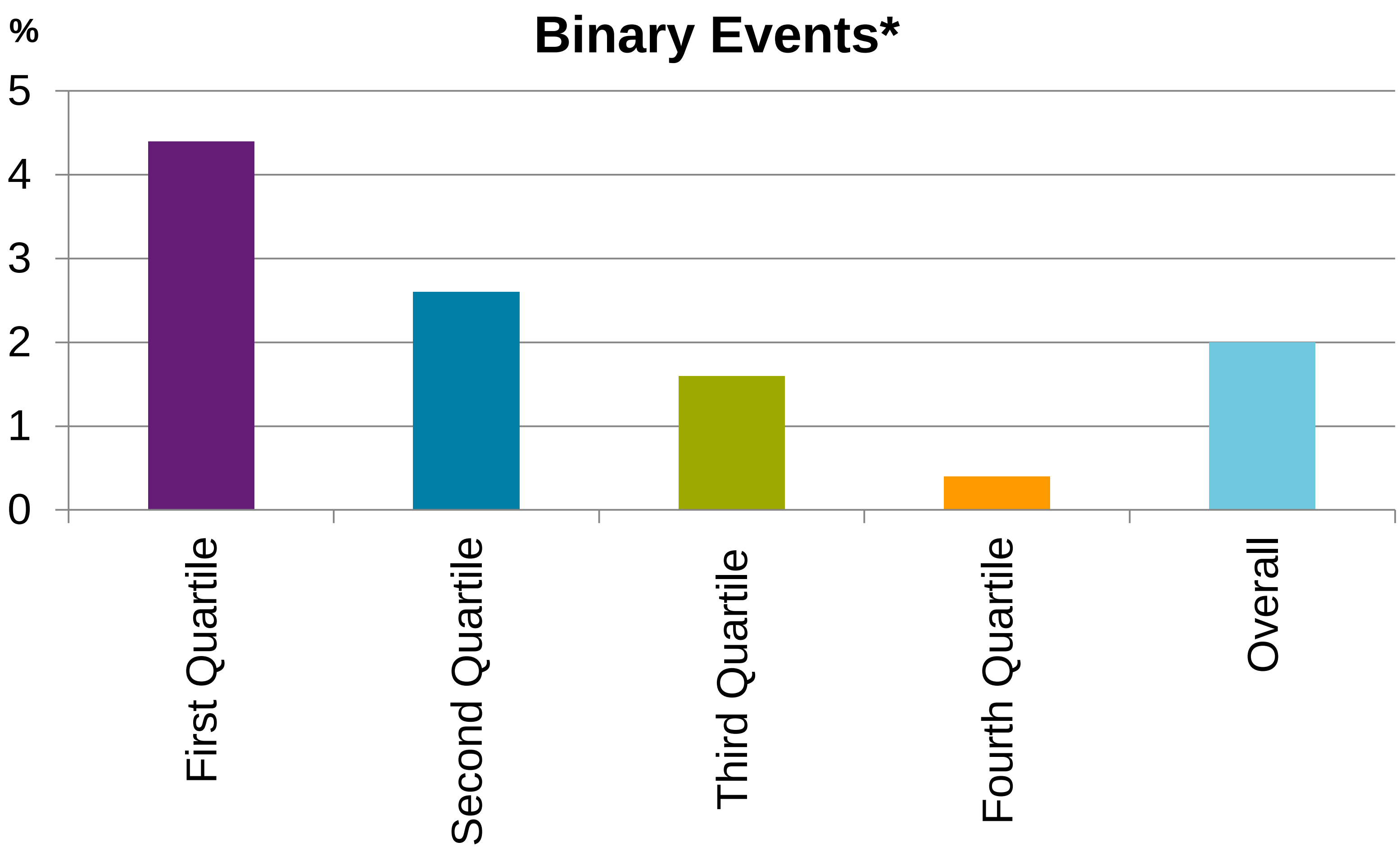
*% of Solvency II net best estimate

A SIMILAR PICTURE FOR DISCOUNTING...



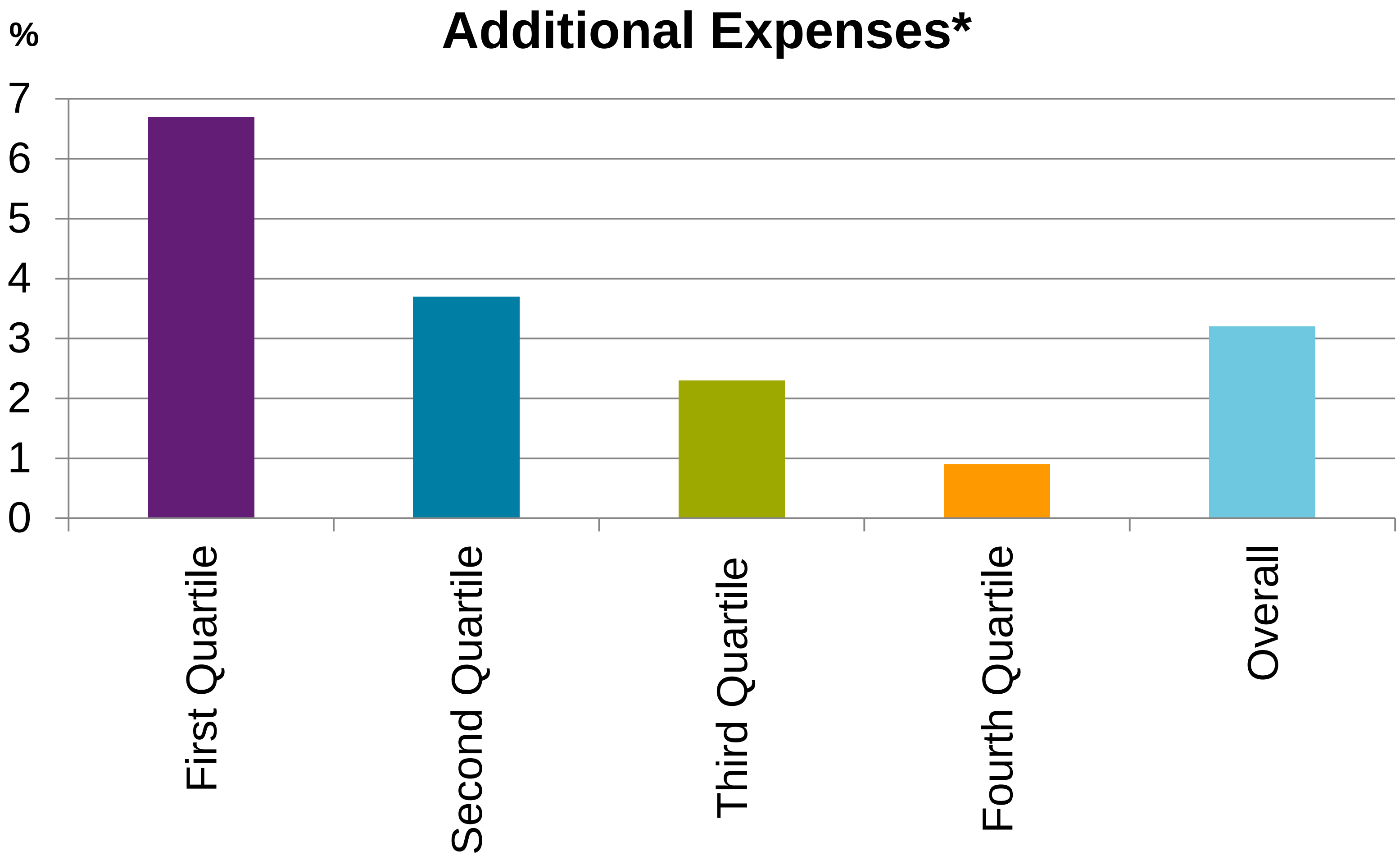
*% of Solvency II net technical provisions (undiscounted)

… BINARY EVENTS…



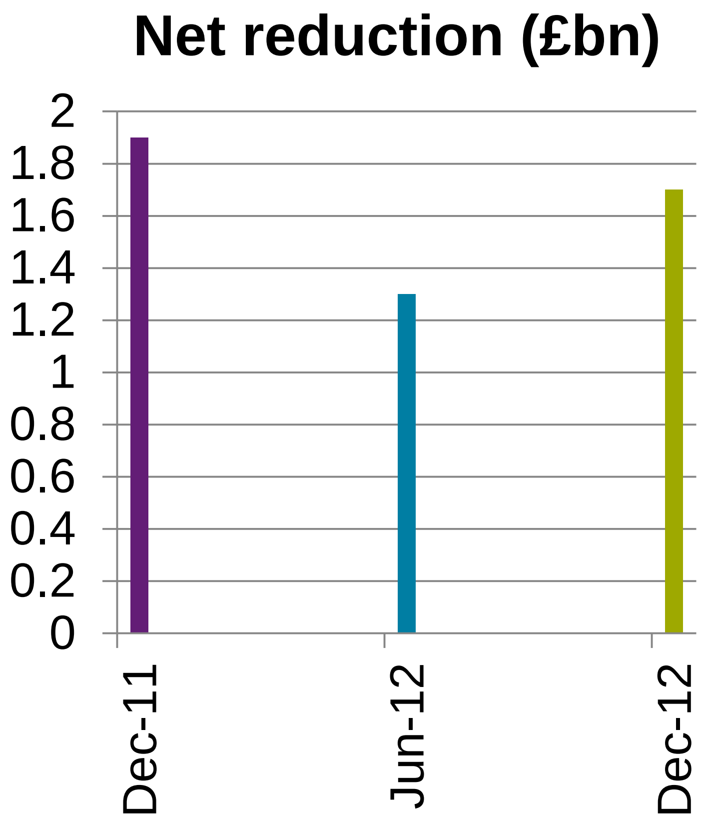
*% of UK GAAP net technical provisions (excluding UPR)

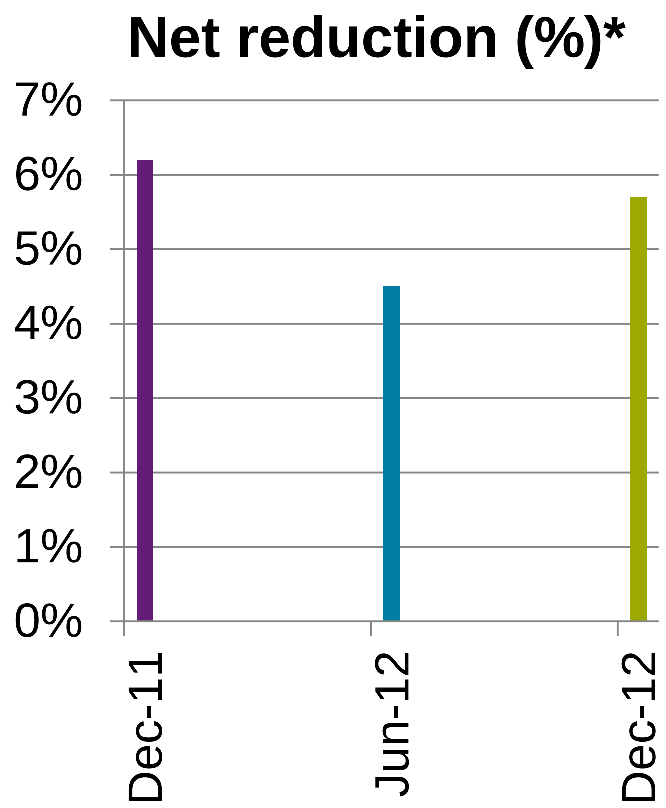
… AND ADDITIONAL EXPENSES



*% of UK GAAP net technical provisions (excluding UPR)

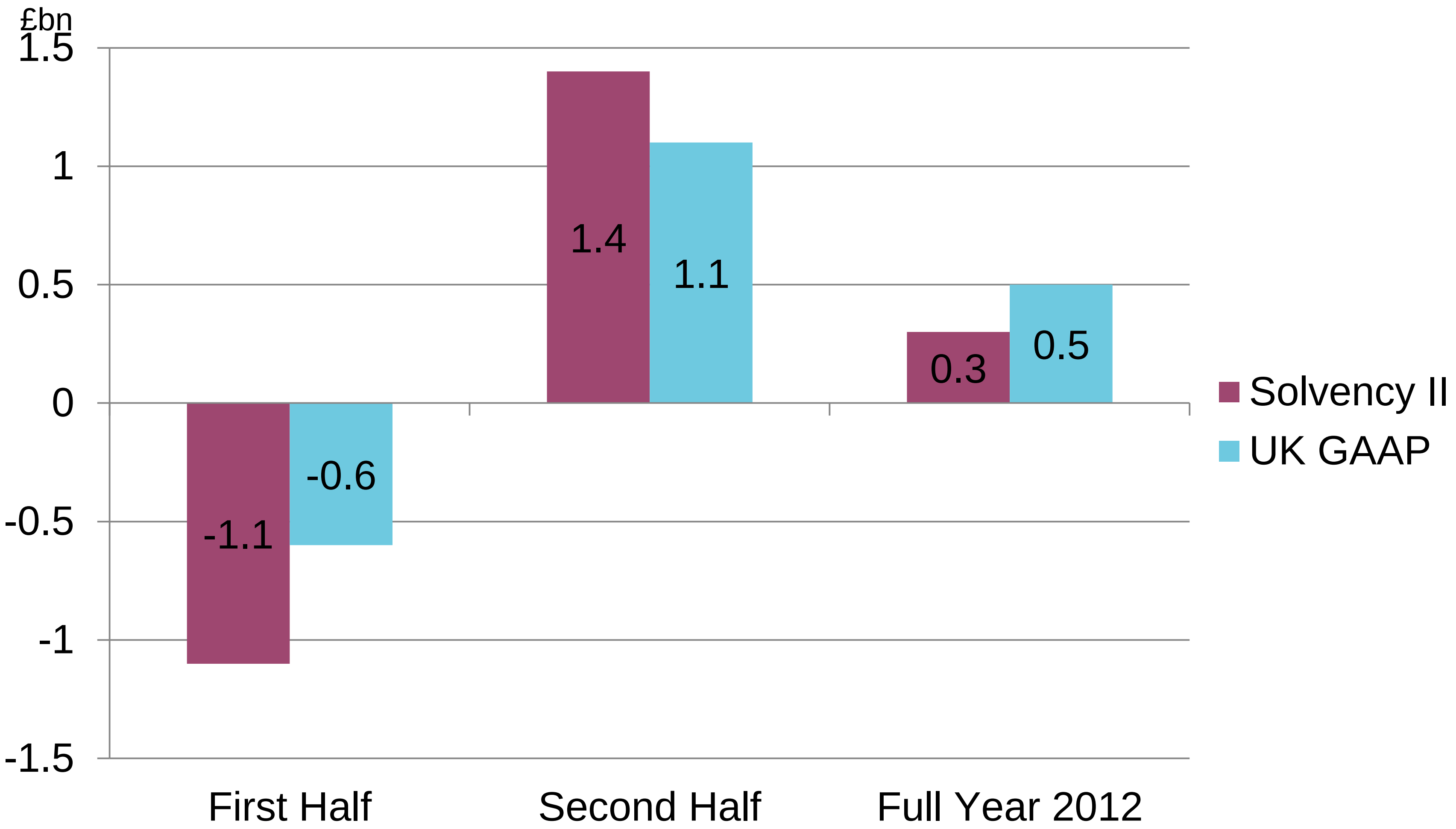
SOLVENCY II RESERVES CONSISTENTLY LOWER THAN UK GAAP





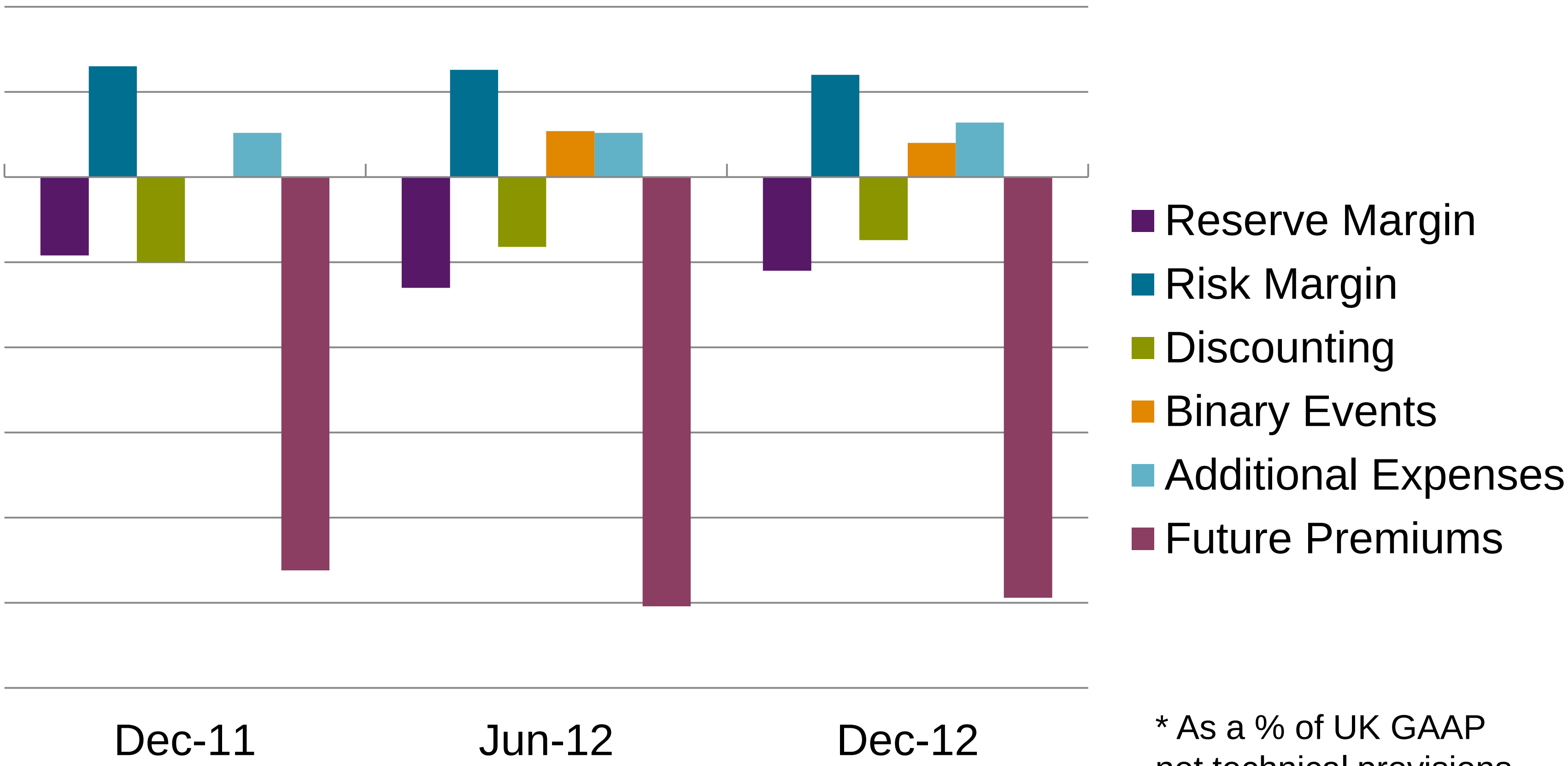
* v UK GAAP net technical provisions (excluding UPR)

SOLVENCY II RESULT TRACKS UK GAAP RESULT IN CALENDAR YEAR 2012



* Aggregate syndicate results, 2012 (net of cash calls and distributions made during the year)

A CONSISTENT PATTERN OF IMPACT OF ADJUSTMENTS*



* As a % of UK GAAP net technical provisions. A positive % indicates an increase in provisions.

Note: No information available on binary events as at December 2011

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GOOD PROGRESS ON IMPLEMENTING SOLVENCY II BALANCE SHEET IN BAU

- Third time that we have asked agents to complete Solvency II balance sheet
  - Although first time for mandating supporting reconciliation
  - QMC appears to have worked well for agents
- Relatively low level of queries from agents and auditors
- QMCs submitted (generally) by the deadline
  - Compliance with the deadline is **critical** for Lloyd’s capital tests

SOME ASPECTS WORKED BETTER THAN OTHERS

Numbers reported generally in line with expectations

- ✓ Solvency II balances appeared reasonable v UK GAAP
- ✓ QMC210 reconciliation items sensible
- ✓ Queries raised by Lloyd’s on less than 1/3 syndicates

Some areas need more focus

- ✗ Inconsistencies with TPD
- ✗ Excess release beyond Statement of Actuarial Opinion (SAO) reserve margin
- ✗ Incorrect calculation of notional managing agents’ profit commission on Solvency II result

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QMC SHOULD BE CONSISTENT WITH TPD

- Inconsistencies noted between QMC002, 210 and TPD
  - Future premiums
  - Allocations between years of account
- Engagement needed between Finance and Actuarial teams on areas traditionally calculated by Finance teams
  - LCA balances

RELEASE OF MARGIN SHOULD NOT BE GREATER THAN THAT IN SAO

- Best estimate required for Solvency II – no margins
- However, Lloyd's requires that release should not be greater than margin reported in SAO
  - To maintain equivalent strength in capital stack as before
- Treated explicitly in the instructions*…
  - "Lloyd's does not expect the impact of the release of reserve margin…to be greater than the amount of the reserve margin reported in the SAO"
  - "Where Lloyd's considers the 'release'...to be excessive…Lloyd's will either ask the managing agent to resubmit the QMC to adjust for this, or alternative to increase the syndicate's SCR by the 'excess' amount"
- 9 syndicates originally reported releases materially bigger than margin reported in SAO

* Page 5, QMC instructions 31 December 2012

TRANSFER OF SOLVENCY II ADJUSTMENTS PERFORMED PROPERLY…

- UK GAAP and Solvency II balance must be same for closing year
  - Just one agent mis-statement
- Impact of Solvency II revaluations correctly transferred to reinsuring syndicate years
- However adjusted managing agent profit commission often looked odd
  - Notional PC must be determined on the revalued result for Solvency II
  - Including impact of ‘transfer in’ of Solvency II adjustments for prior years
  - No cumulative negative PC should be recognised
- Unexpected changes in PC were noted in 14 syndicates
  - Only one where the Solvency II result was overstated

…BUT CALCULATION OF SOLVENCY II PC ADJUSTMENT LESS SO

OTHER LLOYD'S REVIEW POINTS RELATIVELY FEW…

Item	Occurrences
QMC start point does not agree to QMA	2
No adjustment made against (re)insurance receivables and payables on QMC002	1
Where this adjustment was made, difference between QMC002 and QMC210	16
Apparent negative reserve margin	3
No provision reported for binary events	3
No provision or negative provision for future expenses	4
Negative risk margin	1
UPR eliminated on QMC inconsistent with QMA	1

WHAT DO THE AUDITORS THINK?

- Stop start process
  - Review QMA – stop – Review QMC
  - Would be more efficient if work could be done together
- Management review time should be built in
- There are many reconciliation errors occurring
- Co-ordination between agent Finance and Actuarial teams needs improvement
- Reporting process not automated and also not fully embedded into existing finance and actuarial systems/processes
- Further integration work is required to ensure consistency with the Solvency II internal model

WHY DOES LLOYD'S REQUIRE AN AUDIT REVIEW?

- QMC provides results for use in members' capital tests
  - Same as UK GAAP results (ie QMA) used previously

- Reasonable for Lloyd's to rely on same level of audit review as QMA
  - Review opinion at 30 June
  - Full audit at 31 December

- Lloyd's has sought to keep costs down
  - No audit required of risk margin

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WHAT DO AGENTS FIND MOST CHALLENGING ABOUT THE QMC?

- Timetable for submission
- Calculation of technical provisions
- Completion of QMC210
- Engagement between Finance and Actuarial teams
- Audit requirements

- What can Lloyd's do to help?
  - What should the SREP workshops in September cover?

WHAT DO YOU FIND MOST CHALLENGING ABOUT THE QMC?

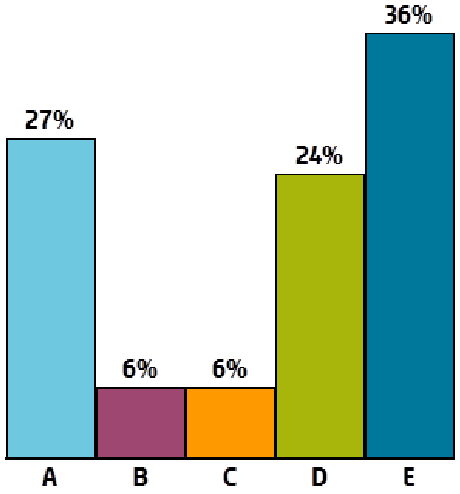
A. Timetable for submission

B. Calculation of technical provisions

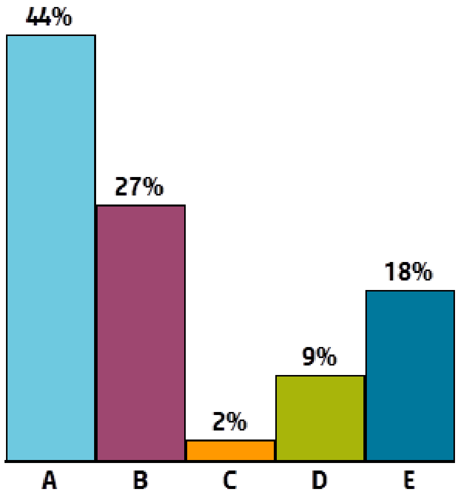
C. Completion of QMC210

D. Engagement between Finance and Actuarial teams

E. Audit requirements



TUESDAY 11 JUNE 2013



WEDNESDAY 12 JUNE 2013

DO YOU UNDERSTAND THE RELATIONSHIP BETWEEN QMC AND TPD?

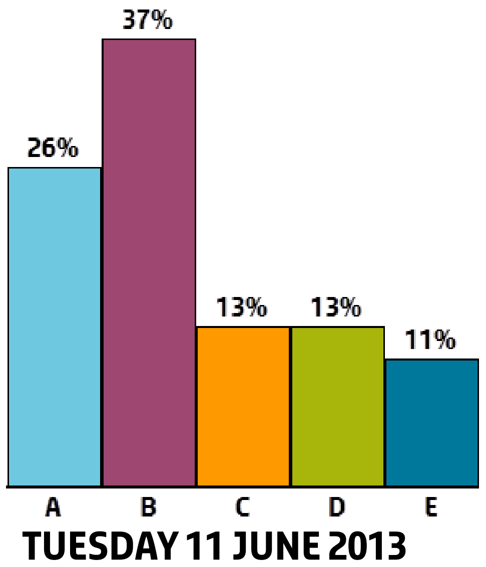
A. Yes, fully

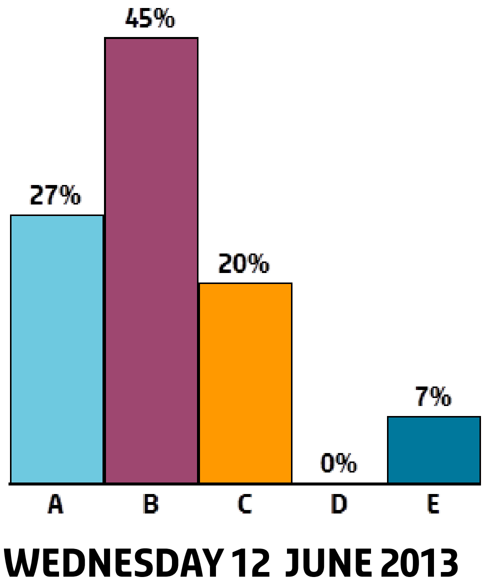
B. On the whole, although instructions could be more explicit about link

C. Only to an extent

D. No, I find linking the two difficult

E. The actuaries fill out the TPD – we didn't look at this





DID THE QMC210 HELP?

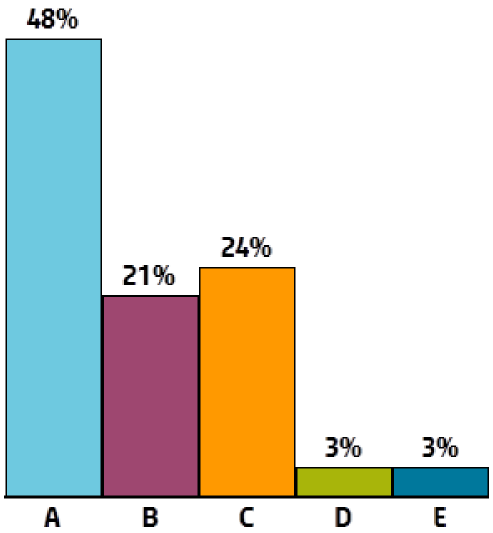
A. Yes, it helped me to work through the adjustments needed, and explain it to the Board/auditors

B. It is helpful although would benefit from slight change in format/layout

C. It is useful although does invite a lot more questions from the Board/auditors

D. No, just made the return even more confusing

E. Just another pointless form to fill out for Lloyd's



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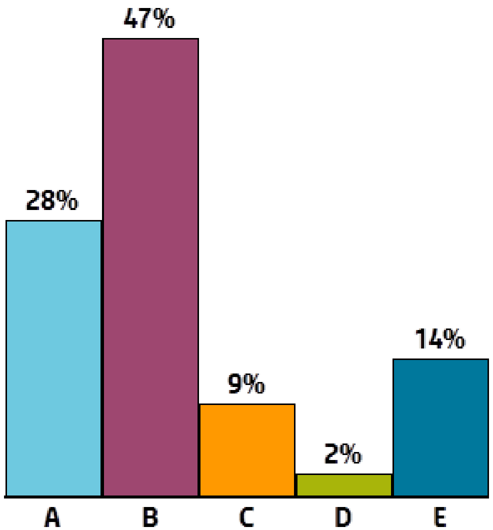


WEDNESDAY 12 JUNE 2013

WHAT SHOULD THE SEPTEMBER SREP WORKSHOPS COVER?

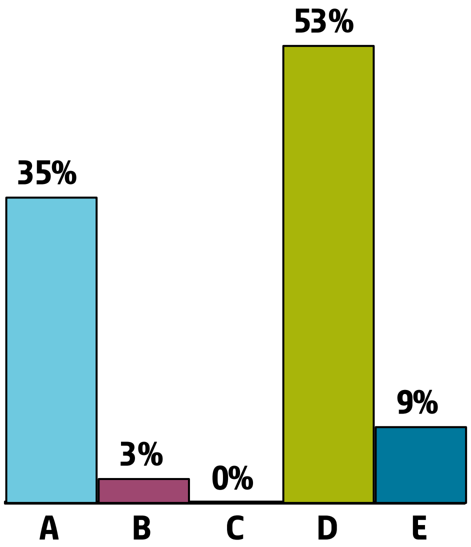
A. Year end requirements (including QMC) and planned Pillar 3 work for 2014

B. QAD live data collection at 30 September 2013

C. What the Pillar 3 interim measures will mean in practice

D. All of the above

E. No need for any more workshops at this time



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COMING UP LATER IN 2013…

- QAD (asset data) dry run as at 31 December 2012
  - Due for submission 13 June (this Thursday!)
- Interim reporting at 30 June 2013
  - QMA due 8 August (unaudited), 22 August (audited)
  - QMC due 5 September
- SREP workshops 17/18 September
- QAD ‘live’ submission as at 30 September 2013
  - Due for submission 1 November
- Update on interim measures – by end 2013 (hopefully)

NO CHANGES FOR JUNE 2013

- QMA (UK GAAP)
  - Initial submission four weeks before QMC
  - Final submission two weeks before QMC

- QMC required with review opinion, as for 30 June 2012
  - QMC completion requirements same as for 31 December 2012

- Plan now for QMC submission:
  - Prepare draft numbers from QMA initial submission
  - Update for QMA final submission
  - Agree audit review times and finalisation meetings
  - Organise Board sign-off
  - Board can delegate authority to a sub-group (but 2 directors sign-off required)

PLAN NOW FOR DECEMBER 2013

- QMA (UK GAAP) Thursday 20 February 2014

- QMC (Solvency II balance sheet) Thursday 6 March 2014
  - Two week gap to be maintained

- Again, plan now for QMC submission:
  - Plan availability of Finance and Actuarial teams
  - Ensure that sufficient management review time is included
  - Agree audit review times and finalisation meetings
  - Organise Board/sub-group meetings ready for sign-off

QAD GOES LIVE AS AT 30 SEPTEMBER 2013

- Lloyd's will provide feedback to agents on the dry run in the summer
- Data collection requirements in live data collection unchanged from dry run
- Managing agent sign-off (QAD990) will be required
- Ratings/investment house licences are required
  - Licence required waived for dry run
  - Each managing agent must secure licences with appropriate providers
  - See email sent to Solvency II contacts, 31 May 2013
  - Queries to Lloyd's Treasury: Debbie Sallas (Debbie.Sallas@lloyds.com) or Tony Cullum (Tony.Cullum@lloyds.com)

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INTERIM MEASURES PROPOSED TO HARMONISE INSURERS' PREPARATIONS

- EIOPA proposals cover Pillar 2, Pillar 3 and IMAP
- Consultation ends 19 June
- Final measures will be published by end 2013
- Lloyd's involved with consultation
  - Feedback received from market via LMA
  - Initial response made via Insurance Europe
  - Further engagement with PRA, CFO Forum and CRO Forum
  - Final response to be made to EIOPA

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 WE ARE LOBBYING TO REDUCE THE BURDEN

- Only one set of quarterly reporting…
  - …and allow 12 weeks rather than 8 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

- Make it explicitly clear that ‘best efforts’ is permitted
  - Both firms and supervisors should use this as a ‘learning experience’

LLOYD'S WOULD LINK COMPLIANCE WITH PILLAR 3 DRY RUN

- Four new Solvency II returns in Core Market Returns (CMR):
  - ASR, QSR (all except asset data)
  - AAD, QAD (asset data)
  - Currently available for UAT
- No Pillar 3 dry run in 2013 except for QAD (part needed for LIM)
- 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, probably in Summer 2014
- Qualitative reporting will only dry run to align with interim measures
  - Detailed 'worked example' will be provided in 2014

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