MARKET BULLETIN

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Title	Changes to UK GAAP – guidance for managing agents
Purpose	To provide managing agents with guidance on the forthcoming changes to UK GAAP, for particular reference when preparing syndicate annual reports and QMA
Type	Scheduled
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Related links	

You may be aware that there are changes to UK GAAP being implemented by the UK Financial Reporting Council (FRC) with effect from 2015. These changes will apply to the preparation of syndicate annual reports by managing agents, and will also impact the requirements of the Quarterly Monitoring Return Part A (QMA). This includes the provision of comparative data for 2014.

The purpose of this bulletin is to provide you with guidance with respect to the impact of these changes, attached at Annex 1. The guidance contains a summary of the main changes, and recommended actions for managing agents. It also contains an overview of the International Accounting Standards Board's (IASB) proposals on IFRS 4 'Insurance Contracts'.

Queries

Any queries or comments on this bulletin should be submitted via e-mail to George Maina (george.maina@lloyds.com) or Paul Appleton (paul.appleton@lloyds.com).

Paul Appleton

Annex 1

Changes to UK GAAP – Guidance for managing agents

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Section 1 – Background

1.1 Changes to UK GAAP

1.1.1 Since 2002, the UK Accounting Standards Board (ASB), and subsequently the Financial Reporting Council (FRC) have been conducting a review of UK GAAP, with a view to updating and rationalising it.

1.1.2 This work has culminated in the publication of three new Financial Reporting Standards (FRS), which replace the vast majority of existing UK GAAP with effect from 1 January 2015 i.e. FRS 100 ‘Application of Financial Reporting Requirements’, FRS 101 ‘Reduced Disclosure Framework’, and FRS 102, ‘The Financial Reporting Standard Applicable in the UK and Republic of Ireland’. FRS 102 contains the accounting requirements, and this was published in final form in March 2013.

1.1.3 FRS 101 provides a reduced disclosure framework for qualifying subsidiaries of entities otherwise reporting under full EU endorsed IFRS. It is accordingly not relevant to the circumstances of Lloyd’s syndicates.

1.1.4 Given the specialist nature of the industry, the FRC decided to consult on a separate standard for insurance contracts, draft FRS 103. The FRC’s consultation on this standard (as FRED 49) concluded at the end of October 2013. The final form of this standard is expected to be published by the FRC in early 2014. In the meantime, any commentary in this guidance is based on the draft as consulted on by the FRC. It is proposed that this standard will apply with effect from 1 January 2015, to align with the other new UK GAAP requirements.

1.1.5 A link to the FRC’s ‘The Future of UK GAAP’ project page is available here.

1.2 FRS 102 - ‘The Financial Reporting Standard Applicable in the UK and Republic of Ireland’

1.2.1 The purpose of FRS 102 is to replace virtually all of the existing set of UK GAAP (although not for accounting for insurance contracts) and provide the revised accounting requirements in a single volume of around 300 pages, in a consistent and updated text.

1.2.2 FRS 102 is based on International Financial Reporting Standards (IFRS) for Small and Medium-sized Entities (SMEs) issued in 2009 and is designed for all UK entities which are not applying EU-adopted IFRS, FRS 101 or the Financial Reporting Standard for Smaller Entities (FRSSE).

1.2.3 Given that FRS 102 is based on IFRS for SMEs, the basis of accounting is generally similar to current UK GAAP (which has adopted much of IFRS over time), although there are changes to accounting options regarding foreign currency and certain additional disclosure requirements regarding capital and investments. These are considered further in Section 3 of this guidance.

1.3 Draft FRS 103 – ‘Insurance Contracts’

1.3.1 The FRC has proposed a separate standard for accounting for insurance contracts (FRS 103), which is based on the current IFRS 4 ‘Insurance Contracts’. However, given the particular reporting requirements for life insurers, elements of FRS 27 are also included. Furthermore, some sections from the current ABI SORP on Insurance Contracts have been reflected in the draft standard.

1.3.2 The FRC’s approach to draft FRS 103 is that it should enable insurers using UK GAAP to broadly continue to account as they do currently. This is because the FRC consider that the draft standard may be in place for only a few years, until the IASB’s ‘Insurance Contracts’ project is finalised (see section 1.4 below). In addition, the requirements of Solvency II, now likely to start from 2016, may impact FRS 103.

1.3.3 While the actual numbers reported in the accounts may remain unchanged for entities using UK GAAP, there are some additional disclosure requirements relating to reconciliations of changes in key items and the requirement to show claims development. The detail of this is considered in Section 4 of this guidance.

1.4 IASB's 'Insurance Contracts' Project

1.4.1 The International Accounting Standards Board (IASB) has, since 1997, been working on a project to develop a globally consistent standard for accounting for insurance contracts. An initial milestone was achieved with the publication of the current IFRS 4 'Insurance Contracts' in 2004, although this still allows a wide variety of accounting treatments to be applied. Subsequently, the IASB issued an Exposure Draft of a new standard in 2010. This generated an enormous amount of feedback from the global insurance industry and consulting firms. This has resulted, after a considerable period of engagement with the industry, in the IASB issuing a revised Exposure Draft for consultation earlier this year, the deadline for responses having been 25 October 2013.

1.4.2 At this time it is unclear when the new IFRS 4 will become mandatory for use within IFRS. It is clear that, once again, this consultation has generated a substantial amount of inconsistent and varied feedback for the IASB to consider. It is unlikely that a final standard will be published before late 2014. The IASB have indicated that there will be a period of three years after publication before mandatory adoption, so it is unlikely that this will take place before 2018.

1.4.3 The FRC have stated their intention, once the final standard is available, to incorporate elements of this into FRS 103, where considered appropriate and proportionate given that FRS 103 is intended for entities not using full IFRS. Therefore ultimately this will have an impact on UK GAAP, although mandatory adoption is not expected until 2018 at the earliest.

1.4.4 The proposals contained within the Exposure Draft are complex and in particular provide for a radically different basis of measuring insurance contract liabilities, or reserves, from the basis used currently in UK GAAP. Reserves will be determined using a building block approach (which has some similarities to Solvency II) although in certain circumstances a simpler approach known as the premium allocation approach may be available. There are also changes to the basis of presentation and additional disclosure. It is not the purpose of this guidance to consider the Exposure Draft in detail but an overview is provided in Section 5 of this guidance.

1.4.5 A link to the IASB's 'Insurance Contracts' project page is available here.

1.5 Lloyd's engagement with accounting developments

1.5.1 Lloyd's has been closely following developments on accounting standards, and has engaged with the LMA, managing agents and auditors working in the Lloyd's market via the Lloyd's/LMA Accounting Policy Working Group.

1.5.2 As part of this work, Lloyd's has responded to both the FRC and IASB consultations, the responses of which having been contributed to and reviewed by the Working Group. Lloyd's response to the FRC on draft FRS 103 may be found here, and to the IASB on the draft 'Insurance Contracts' ED here.

1.5.3 The Working Group has also reviewed this guidance. Lloyd's shall continue to monitor developments on the FRC and IASB proposals and provide further guidance to managing agents as set out in paragraph 6.2, below.

1.6 Status of this document

1.6.1 This document has been issued to provide managing agents with guidance on the impact of the changes to UK GAAP as well as an overview in respect of the IASB's 'Insurance Contracts' proposals.

1.6.2 It should be treated as a working document and will be reviewed when FRS 103 and the revised IFRS 4 are finalised. In this context any feedback on the document is encouraged. This should be sent by email to either paul.appleton@lloyds.com or george.maina@lloyds.com.

Section 2 – Requirements for managing agents – general

2.1 Basis of preparation of syndicate annual reports

2.1.1 Currently, managing agents must prepare an annual report for each Lloyd's syndicate using UK GAAP in accordance with the requirements of the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 ('the Regulations'). This position will continue for the foreseeable future and there are no plans for Lloyd's to adopt full IFRS for the syndicate accounts. Therefore, and in order to ensure that a consistent approach is applied by managing agents for the purpose of Lloyd's Aggregate Accounts (see 2.2.1 below):

- For the 2014 year end, syndicate accounts must be prepared in accordance with current UK GAAP; and

- For the 2015 year end, syndicate accounts must be prepared in accordance with the revised UK GAAP ie in particular FRS 102 and FRS 103. This may require the restatement of 2014 comparatives in respect of the treatment of foreign currency, and will require the additional disclosures arising from the introduction of FRS 102 and FRS 103. The detail of these areas is considered further in Sections 3 and 4.

2.2 Impact on Lloyd's Society accounts and additional data collection from managing agents

2.2.1 The Lloyd's Aggregate Accounts, prepared by the Corporation, are required in accordance with the Regulations to be an aggregation of the relevant financial information reported in the syndicate annual reports. In practice the Aggregate Accounts are prepared from returns submitted via the Core Market Returns (CMR) system in respect of each syndicate, which are certified by the managing agent as being the same numbers as reported in the syndicate annual report.

2.2.2 Accordingly, it will be necessary to collect this additional data from syndicates via the CMR system to enable the Aggregate Accounts to comply with the revised requirements:

- Revised comparatives for 2014 to collect any changes arising from the treatment of foreign currency in accordance with FRS 102

- Additional reconciliations of the movement on key items (including comparatives) as required by FRS 103

- Claims development triangles by underwriting year as required by FRS 103.

Revised comparatives as described above shall also be needed for the purpose of the 2015 interim and annual Lloyd's Market Results, which are also prepared under UK GAAP.

Amendments to the CMR system to enable the collection of this data will be made by Lloyd's and made available for agent user acceptance testing by end 2014. Lloyd's shall decide by the end of 2014, whether to collect the 2014 comparative information as a separate exercise in 2015 or to collect this data with the 31 December 2015 QMAs. However, the Q1 2015 QMA and subsequent QMAs should be prepared based on the revised UK GAAP.

2.3 Accounts for corporate members

2.3.1 Most classes of Lloyd's corporate members are required to prepare their accounts in accordance with Schedule 3 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008. In the case of corporate members that are aligned or dedicated capital providers, they may, as now, determine their accounting policies in accordance with those of the holding company or group, and shall prepare their accounts accordingly. Lloyd's shall continue to provide the 'central Schedule 3 facility', primarily intended to help corporate members participating as spread members – typically private limited members, Namecos etc. The outputs provided to subscribers to this facility will, from the 2015 year end, include the additional quantitative information required under FRS 103 as collected from syndicates in the QMAs, as described above. This will also include revised comparative data for the 2014 year end, to be provided with the 2015 year end outputs.

Section 3 – FRS102 - The Financial Reporting Standard Applicable in the UK and Republic of Ireland

3.1 Overview

3.1.1 FRS 102 replaces virtually all current UK GAAP (although not in respect of accounting for insurance contracts). It is based on IFRS for SMEs with certain modifications. A link to FRS 102 is provided here.

3.1.2 Generally, FRS 102 allows the continuation of current UK GAAP reporting and disclosure. The format of the accounts will stay the same, including a balance sheet, income statement and cashflow. However there are three changes which are of particular relevance to syndicates: the options for accounting for foreign currency, additional disclosures on capital and additional disclosures on financial instruments. These are considered further below.

3.2 Accounting for foreign currency

3.2.1 FRS 102's requirements in respect of foreign currency are set out in Chapter 30, pages 183 to 187.

3.2.2 FRS 102 applies the concept of a functional currency to UK GAAP as a mandatory requirement. The functional currency is: 'the currency of the primary economic environment in which the entity operates' (FRS 102 30.2). 'The primary economic environment in which an entity operates is normally the one in which it primarily generates and expends cash' (30.3). Although for many Lloyd's syndicates, this will be GBP, there will be a significant number of Lloyd's syndicates where this will be USD or possibly another currency. This means that for some syndicates, the functional currency may be different to the reporting currency, which will continue to be GBP for virtually all syndicates (a few syndicates prepare their annual reports in US dollars).

3.2.3 FRS 102 will require all foreign currency transactions to be translated into the functional currency at the historic rate of exchange. At the period end, the monetary foreign currency items must be translated at the closing rate with any difference being allocated to the profit and loss account (see 30.6 to 30.11). **The practice used currently by some syndicates of booking such differences through the STRGL (or other comprehensive income) based on 'branch accounting' will no longer be permitted.**

3.2.4 When translating items from the functional to the reporting (or presentation) currency, FRS 102 requires that (30.18):

'An entity…shall translate its results and financial position into a different presentation currency using the following procedures:

(a) assets and liabilities for each statement of financial position presented (ie including comparatives) shall be translated at the closing rate at the date of that statement of financial position;

(b) income and expenses for each statement of comprehensive income (ie including comparatives) shall be translated at exchange rates at the dates of the transactions; and

(c) all resulting exchange differences shall be recognised in other comprehensive income (ie the STRGL).

3.2.5 An illustrative disclosure in relation to change in accounting policy for foreign currency potentially required by FRS 102 section 30 is provided at Appendix A.

3.3 Capital disclosures

3.3.1 FRS 102 mandates that certain disclosures be made in respect of capital for financial institutions, in accordance with the provisions of FRS 102 section 34.31. These disclosures apply to Lloyd's syndicates.

3.3.2 Specifically, FRS 102 34.31 requires that:

'A financial institution shall disclose information that enables users of its financial statements to evaluate the entity's objectives, policies and processes for managing capital. A financial institution shall disclose the following:

(a) Qualitative information about its objectives, policies and processes for managing capital, including:

(i) a description of what it manages as capital;

(ii) when an entity is subject to externally imposed capital requirements, the nature of those requirements and how those requirements are incorporated into the management of capital; and

(iii) how it is meeting its objectives for managing capital.

(b) Summary quantitative data about what it manages as capital. Some entities regard some financial liabilities (eg some forms of subordinated debt) as part of capital. Other entities regard capital as excluding some components of equity (eg components arising from cash flow hedges).

(c) any changes in (a) and (b) from the previous period.

(d) Whether during the period it complied with any externally imposed capital requirements to which it is subject.

(e) When the entity has not complied with such externally imposed capital requirements, the consequences of such non-compliance.

A financial institution bases these disclosures on the information provided internally to key management personnel.'

3.3.3 Further guidance is provided at section 34.32 which states:

'A financial institution may manage capital in a number of ways and be subject to a number of different capital requirements. For example, a conglomerate may include entities that undertake insurance activities and banking activities and those entities may operate in several jurisdictions. When an aggregate disclosure of capital requirements and how capital is managed would not provide useful information or would distort a financial statement user's understanding of the financial institution's capital resources, the financial institution shall disclose separate information for each capital requirement to which the entity is subject.'

3.3.4 Accordingly, the requirements are principles based and are to be complied with taking into account the structure of the entity and the supervisory capital requirements to which it is subject.

3.3.5 At Lloyd's, the capital requirements imposed by both the PRA and by Lloyd's itself are focused on meeting member level and Lloyd's overall capital requirements. Syndicate level capital requirements are thus only relevant in helping to determine these. Accordingly, we consider that the nature of the disclosures provided in the syndicate annual report should be generic in nature, describing Lloyd's capital setting process and how the syndicate capital number (SCR) fits into this. It is not expected that the syndicate will have to disclose its SCR.

3.3.6 It is the responsibility of each managing agent to determine the disclosures necessary to comply with FRS 102 34.31 and 34.32. However, for guidance, an illustrative text of such disclosures which would be the minimum appropriate for a Lloyd's syndicate is attached at Appendix B. The illustrative text assumes that Solvency II is applicable from 1 January 2016 and thus reflects Solvency II 'language' in the text.

3.4 Financial instruments disclosures

3.4.1 FRS 102 requires financial institutions to make additional disclosures in respect of financial instruments held and these disclosures are based on IFRS 7, 'Financial Instruments: Disclosures'.

3.4.2 These additional disclosures would impact those syndicates that have not already adopted the current FRS 29.

Section 4 – Draft FRS 103 – Insurance Contracts

4.1 Overview

4.1.1 Draft FRS 103 will be the new UK GAAP to deal with accounting for insurance contracts. Draft FRS 103 is complementary to, and sits alongside, FRS 102.

4.1.2 As noted above, draft FRS 103 is based on IFRS 4, but incorporates elements of FRS 27 for life insurance and the ABI SORP on Insurance Contracts.

4.1.3 A link to the draft FRS 103 may be found here.

4.1.4 Generally, FRS 103 allows insurers to continue with their existing accounting policies. However, given that it is based on IFRS 4, it introduces some new disclosure requirements into UK GAAP. These are:

- reconciliations of changes in insurance liabilities, reinsurance assets and any related deferred acquisition costs; and
- claims development triangulations at whole account level.

4.2 Additional reconciliations of movements in key items

4.2.1 Draft FRS 103 requires at sections 4.3 to 4.5:

"(4.3) An insurer shall disclose information that identifies and explains the amounts in its financial statements arising from insurance contracts.

"(4.4) To comply with paragraph 4.3 an insurer shall disclose:

(a) [not used]
(b) the recognised assets, liabilities, income and expense (and, if it presents its statement of cash flows using the direct method, cash flows) arising from insurance contracts. Furthermore, if the insurer is a cedant, it shall disclose:
   (i) gains and losses recognised in profit or loss on buying reinsurance; and
   (ii) if the cedant defers and amortises gains and losses arising on buying reinsurance, the amortisation for the period and the amounts remaining unamortised at the beginning and end of the period.
(c) The process used to determine the assumptions that have the greatest effect on the recognised amounts described in (b). When practicable, an insurer shall also give quantified disclosure of those assumptions
(d) The effect of changes in assumptions used to measure insurance assets and insurance liabilities, showing separately the effect of each change that has a material effect on the financial statements.
(e) reconciliations of changes in insurance liabilities, reinsurance assets and, if any, related deferred acquisition costs.

4.2.2 The only new requirement introduced to UK GAAP is the reconciliations referred to in sub paragraph (e) above, which is a reconciliation in the movement in reserves during the year. This is required at a whole syndicate level only, but comparatives will be required.

4.3 Risk disclosures: Claims development triangles

4.3.1 Sections 4.6 to 4.8 of draft FRS 103 set out disclosure requirements with respect to 'the nature and extent of risks arising from insurance contracts'. These are consistent with current UK GAAP requirements but there is an additional requirement to show information on claims development, as set out in draft FRS 103 4.7 (c) (iii):

"actual claims compared with previous estimates (ie claims development). The disclosure about claims development shall go back to the period when the earliest material claim arose for which there is still uncertainty about the amount and timing of the claims payments, but need not go back more than ten years. An insurer need not disclose this information for claims for which uncertainty about the amount and timing of claims payments is typically resolved within one year."

However, there is a transitional arrangement on adoption of FRS 103. Paragraph 6.3 states that 'In applying paragraph 4.7(c) (iii), an entity need not disclose information about claims development that occurred earlier than five years before the end of the first financial year in which it applies this [draft] FRS'. Given adoption in 2015, this means that 2011 would be the earliest year reported separately where a syndicate utilises this provision.

This information is required at whole pure underwriting year level in the reporting currency (generally converted sterling), reporting net claims incurred including IBNR.

A suggested approach to the conversion of foreign currency items is: Paid claims are accounted for at historical exchange rates for each calendar year with the reserves at each year end retranslated using the latest reporting date exchange rate so as to prevent foreign exchange fluctuations obscuring the view of the claims development. We would welcome views from managing agents as to whether alternative approaches should be considered.

Information on cumulative premiums is not required.

4.3.2 To ensure a consistent approach among Lloyd's syndicates, Lloyd's expects that where a syndicate has been in existence for more than five years, the syndicate shall as a minimum disclose the claims development in respect of the last five pure underwriting years separately on adoption in 2015, ultimately extending to the full ten years. Claims development in respect of earlier years would be shown in aggregate. So as at 31 December 2015, when this information is reported, the syndicate would report the development on claims for each of the 2011 to 2015 pure underwriting years of account separately, with claims development on the 2010 and earlier pure underwriting years of account shown in aggregate. Historic claims development analysis going back to the first year of the oldest year to be separately reported, ie for each calendar year from 2011 to 2015 for each of the 2011 to 2015 pure underwriting years of account shall be required.

4.3.3 In the case of RITC to/from another syndicate (both inwards and outwards), the ceding syndicate should only report claims incurred up to the date of the RITC while the reinsuring syndicate should provide claims incurred information after that date plus the historical information relating to underwriting years accepted through the RITC (as previously reported by the ceding syndicate). The ceding syndicate should restate the historical data in the first reporting date after the RITC so as to eliminate incurred claims related to underwriting years now RITC'ed into another syndicate. For example, in the case of RITC as at 31 December 2015 into another syndicate, the ceding syndicate should report claims incurred information as at 31 December 2015. However, when preparing the accounts for the following year, as at 31 December 2016, the historical data should be adjusted to remove the incurred claims amount relating to underwriting years transferred through the RITC as at 31 December 2015. This historical information will be required to be reported by the reinsuring syndicate from 31 December 2016 onwards, by underlying pure year of account.

4.3.4 An illustrative example of a claims development disclosure as at 31 December 2015, utilising the transitional provisions, is provided at Appendix C.

Section 5 – Future Developments – IFRS 4 'Insurance Contracts'

5.1 Overview

5.1.1 The IASB, in its continuing work on its insurance contracts project, has published for consultation an Exposure Draft (ED).

5.1.2 A link to the ED may be found here.

5.1.3 Currently, there is no confirmed implementation date but the IASB have advised that there will be a gap of three years from publication of the final standard until mandatory implementation. It is expected that the final standard will not be made available before late 2014, thus mandatory implementation is unlikely before 2018.

5.1.4 Although this is IFRS rather than UK GAAP, the FRC have indicated that once a final standard is available, they shall seek to incorporate this into FRS 103 to the extent that it is appropriate and proportionate to do so given that FRS 103 is aimed at SMEs.

5.1.5 The IASB's proposals are significantly more complex than the current requirements for accounting for insurance contracts or those (essentially the same) proposed under draft FRS 103. It is not the purpose of this paper to provide a detailed analysis of these proposals – this will not be provided until late 2014 at the earliest – but a summary is provided below of the key changes proposed.

5.2 Valuation of insurance contract liabilities

5.2.1 Under the IASB's proposals, the measurement of insurance contract liabilities (ie technical provisions or reserves) will change from the current undiscounted reserve, often with an element of implicit and/or explicit prudence, to a much more complex 'building blocks' approach (BBA). However, in certain circumstances a simpler 'premium allocation' approach (PAA) shall also be available.

5.2.2 The BBA requires a four part approach to the valuation of insurance contract liabilities:

Element	Description
Best estimate	This is a probability–weighted best estimate of inwards and outwards future cash flows. No provision for 'prudence' is permitted.
Discount	The best estimate cash flows are discounted to reflect the time value of money. The discount rate may be selected by the insurer as that which most appropriately reflects the insurer's circumstances, and may be a 'top down' or 'bottom up' approach.
Risk margin	This provides an explicit provision for prudence. The risk margin may be calculated using any reasonable basis.
Contractual service margin (previously known as the residual margin)	This is effectively the unearned profit on policies still in force, and is released over time based on the risk profile of these policies.

5.2.3 The PAA basis is available for use, only during the period of policy coverage (ie not during the run-off to extinction where the BBA is mandatory) for certain types of business:

- Where the contract length is no more than one year; or
- Where the outcome of the measurement of the liability would be similar using either the BBA or PAA.

5.2.4 The PAA is essentially accounting on an unearned premium basis. As noted earlier, once the policy has expired the BBA must be used but this will be 'simpler' as there will be no contractual service margin. In addition, it is not mandatory to adjust future cash flows for the time value of money (discounting) if those cash flows are expected to be paid or received in one year or less.

5.2.5 Most business underwritten at Lloyd's is expected to qualify for the PAA. It is desirable that a consistent basis of accounting for insurance contracts is applied for all Lloyd's syndicates. Research will be undertaken in 2014 to see how this can best be effected. It is envisaged that guidance on this shall be provided to the market in late 2014 once the Standard has been finalised.

5.3 Income statement

5.3.1 The ED proposes some modifications to the income statement compared with that currently used. A simplified example is set out below:

	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

5.3.2 Currently, the IASB anticipates that the net unwinding of the discount will be reported in profit and loss in 'interest expense on insurance liability' but the impact of any change caused by a reassessment of discount rates after initial assessment would be recognised in other comprehensive income (OCI). This is one of the specific areas on which IASB have consulted and there has been considerable feedback opposing the mandatory usage of OCI in this way. It is possible, therefore, that the treatment of this may be changed in the final draft.

5.4 Further guidance

5.4.1 Lloyd's shall provide further guidance to managing agents with respect to the implications of the IASB's proposals, once a final standard and implementation timetable has been agreed. This is unlikely to have occurred before late 2014.

Section 6 – next steps for managing agents

6.1 Actions for managing agents

6.1.1 Managing agents shall need to prepare syndicate annual reports in accordance with the 'new' UK GAAP ie FRS 102 and FRS 103 with effect from 31 December 2015. In addition, they will be required to provide some additional data in the QMA to enable Lloyd's to incorporate the necessary additional information within the Lloyd's Aggregate Accounts, Lloyd's Market Results and provide to corporate members subscribing to Lloyd's central Schedule 3 facility. Comparative data shall be required for 2014, both as at 30 June 2014 (for the 2015 interim Lloyd's Market Results) and 31 December 2014.

6.1.2 Although managing agents should have ready access to the additional information required, they need to consider the procedures which will need to be put in place to capture and present this information, to fit into the timescales, approval process and audit of the QMA and the syndicate annual report.

6.1.3 Accordingly, during 2014, managing agents should:

- Review FRS 102 and FRS 103 (once published in final form, expected in early 2014) and determine any additional data requirements
- Review internal systems and plan to upgrade these to extract the necessary data
- Prepare 'dry run' revised disclosure notes for internal review
- Discuss revised reporting requirements and procedures with their auditors
- Participate in the user acceptance testing (UAT) of the additional forms provided in the QMA, expected to be made available to agents late 2014.

6.2 Next steps by Lloyd's

6.2.1 Lloyd's shall, in 2014:

- Review the guidance contained in this paper once the final FRS 103 is published (early 2014)
- Include guidance on the 'new' UK GAAP as part of the Solvency II Pillar 3 workshops to be held in June 2014
- Make available the expanded QMA available for UAT by late 2014
- Update and expand guidance on IFRS 4 'Insurance Contracts' once the final standard is available (not before late 2014)

6.3 Timescales for new reporting requirements

6.3.1 2014 Comparatives: Lloyd's will in due course need to collect the 2014 comparative data in the QMA for use in the 2015 Aggregate Accounts, Lloyd's Market Results and Lloyd's central Schedule 3 facility. This shall be collected via the QMA either in 2015 or (only for the 31 December 2014 comparatives) alongside the 31 December 2015 QMA in February 2016. Lloyd's shall review the approach to be taken and advise the market by late 2014.

6.3.2 2015 Reporting: managing agents will be required to prepare the QMA in accordance with the 'new' UK GAAP from Q1 2015, and likewise the 31 December 2015 syndicate annual reports, thus including the additional information and disclosures required, to timescales similar to those currently in place.

Appendix A

Illustrative disclosure in relation to change in accounting policy for foreign currency potentially required by FRS 102 section 30

Basis of accounting note

Foreign currencies

Under previous UK GAAP, the definition of a foreign branch included assets and liabilities accounted for in a foreign currency. FRS 102 requires that a foreign operation must be an entity. Hence, assets and liabilities denominated in a foreign currency no longer constitute a foreign operation and are not retranslated at the closing rate with exchange differences reported through the statement of recognised gains and losses (STRGL). Instead, monetary items are retranslated at the closing rate with exchange differences reported through the non-technical account and non-monetary items (for example, DAC and UPR) are not retranslated.

Non-monetary assets and liabilities, including deferred acquisition costs and unearned premiums are translated into the functional currency using monthly average rates of exchange prevailing at the time of the transaction as a proxy for the transactional rates. This is a change in accounting policy from [2014] when the non-monetary assets and liabilities were retranslated at closing rate of exchange with resulting exchange differences disclosed in the STRGL. The impact of this change in accounting policy is shown in Note [x].

The results and financial position of the syndicate are translated into the presentation currency as follows:

a) assets and liabilities are translated at the closing rate at the balance sheet date;

b) income and expenses are translated at the average rate of exchange during the year; and

c) all resulting exchange differences are recognised in the STRGL.

Prior year adjustment note

During the year, the Syndicate has made an amendment to its foreign exchange accounting policy to ensure compliance with FRS 102 Chapter 30 'Foreign Currency Translation' with respect to:

- the allocation of foreign exchange gains / losses between the profit & loss account and the STRGL; and

- the use of monthly average rates as a proxy for transaction rates when determining the prevailing foreign exchange rate for non-monetary assets and liabilities where these items are held at historical rates of exchange.

In accordance with FRS 102 section 3.12, the applicable comparative figures in the primary statements and notes have been restated to reflect the uniform application of the new policy outlined above.

The financial effect of restating the prior year amounts for the changes in accounting policy is as follows:

	£m
Opening members' balances at 1 January 2014 effect	-
Result for the year ended 31 December 2014 increased	5.0
Statement of total recognised gains and losses 31 December 2014 decreased	(5.0)
Closing members' balances at 31 December 2014 effect	-

Appendix B

Illustrative capital disclosure note for Syndicate XXXX

(Assumes Solvency II starts at 1 January 2016)

Capital framework at Lloyd's

The Society of Lloyd's (Lloyd's) is a regulated undertaking and subject to the supervision of the Prudential Regulatory Authority (PRA) under the Financial Services and Markets Act 2000 and in accordance with [Solvency II legislative references].

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

Although, as described below, Lloyd's capital setting processes use a capital requirement set at syndicate level as a starting point, the requirement to meet Solvency II and Lloyd's capital requirements apply at overall and member level only respectively, not at syndicate level. Accordingly the capital requirement in respect of Syndicate XXXX is not disclosed in these financial statements.

Lloyd's capital setting process

In order to meet Lloyd's requirements, each syndicate is required to calculate its Solvency Capital Requirement (SCR) for the prospective underwriting year. This amount must be sufficient to cover a 1 in 200 year loss, reflecting uncertainty in the ultimate run-off of underwriting liabilities (SCR 'to ultimate'). The syndicate must also calculate its SCR at the same confidence level but reflecting uncertainty over a one year time horizon (one year SCR) for Lloyd's to use in meeting Solvency II requirements. The SCRs of each syndicate are subject to review by Lloyd's and approval by the Lloyd's Capital and Planning Group.

A syndicate may be comprised of one or more underwriting members of Lloyd's. Each member is liable for its own share of underwriting liabilities on the syndicate(s) on which it participating but not other members' shares. Accordingly, the capital requirement that Lloyd's sets for each member operates on a similar basis. Each member's SCR shall thus be determined by the sum of the member's share of the syndicate SCR 'to ultimate'. Where a member participates on more than one syndicate, a credit for diversification is provided to reflect the spread of risk, but consistent with determining an SCR which reflects the capital requirement to cover a 1 in 200 year loss 'to ultimate' for that member. Over and above this, Lloyd's applies a capital uplift to the member's capital requirement, known as the Economic Capital Assessment (ECA). The purpose of this uplift, which is a Lloyd's not Solvency II requirement, is to meet Lloyd's financial strength, licence and ratings objectives. The capital uplift applied for 2016 was [35%] of the member's SCR 'to ultimate'.

Provision of capital by members

Each member may provide capital to meet its ECA either by assets held in trust by Lloyd's specifically for that member (funds at Lloyd's), held within and managed within a syndicate (funds in syndicate) or as the member's share of the members' balances on each syndicate on which it participates.

Accordingly [adjust where appropriate if the syndicate has FIS] all of the assets less liabilities of the syndicate, as represented in the members' balances reported on the balance sheet on page x, represent resources available to meet members' and Lloyd's capital requirements.

Appendix C

Illustrative claims development triangulations – per draft FRS 103 section 4.7 (c) (iii)

Syndicate XXXX - Claims development as at 31 December 2015							
Pure underwriting year	2010 and prior	2011	2012	2013	2014	2015	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Estimate of net claims incurred:							
After one year		18,000	13,000	11,000	18,000	15,000	
After two years		22,500	12,800	11,100	19,500		
After three years		26,000	12,600	11,000			
After four years		27,500	12,500				
After five years		27,000					
As at 31 December 2015	18,000	27,000	12,500	11,000	19,500	15,000	103,000
Less net claims paid	15,000	25,000	9,500	7,000	13,500	6,000	76,000
Net reserves	3,000	2,000	3,000	4,000	6,000	9,000	27,000
Total all underwriting years							
Net reserves recognised							27,000
Amounts recovered from reinsurers							33,000
Gross reserves included in the balance sheet							60,000

Notes

- The table above utilises the transition provisions available on adoption
- The analysis is required by pure underwriting year, at whole account level only
- The analysis is required in respect of net incurred claims, including IBNR
- The total 'net reserves' must reconcile to the balance sheet (claims outstanding minus reinsurers' share)
- The analysis is shown in the syndicate's presentational (reporting) currency, which will generally be GBP
- A suggested approach to the conversion of foreign currency items is: Paid claims are accounted for at historical exchange rates for each calendar year with the reserves at each year end retranslated using the latest reporting date exchange rate so as to prevent foreign exchange fluctuations obscuring the view of the claims development. We would welcome views from managing agents as to whether alternative approaches should be considered.
- No information on premiums development by pure underwriting year is required