Market wide liquidity stress testing exercise

February 2025

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1 Introduction

1.1 Background

The Principles for doing business at Lloyd's ("The Principles") are at the heart of Lloyd's oversight framework and set out the fundamental responsibilities that are expected of all managing agents. Principle 9, liquidity, requires managing agents to ensure that syndicates have contractual access to sufficient liquidity in order to withstand a severe liquidity event (defined by Lloyd's), underpinned by a robust liquidity risk management framework.

Consequently, a requirement has been introduced for all syndicates to be able to withstand the liquidity stress arising from a 1-in-200 year US windstorm or the syndicate's most severe 1-in-200 liquidity risk event (whichever presents the maximum risk, as appropriate to the nature of the syndicate and its risk profile) and a simultaneous diminution in the valuation of its asset portfolio.

The revised framework, through a combination of market-level and Society level risk appetites, aims to ensure that syndicates are self-reliant with respect to managing liquidity risks. This aims to reduce the size and likelihood of calls on the Central Fund to alleviate liquidity strain, and ensure that the Central Fund is able to equitably support the entire market.

1.2 Market wide liquidity stress test

In order to evaluate whether this appetite is satisfied by all syndicates, a 3-yearly market wide liquidity stress testing exercise is conducted. The next market-wide stress test is due to take place at 2025 year-end. Certain syndicates may, however, be required to complete the template for 2024 year-end, if they: are new syndicates in the 2024 or 2025 year of account; failed the 2023 year-end stress test; are RITC syndicates; or have experienced a material change in their risk profile. Affected syndicates will be contacted by Lloyd's in advance.

Those who are requested to complete the exercise for 2024 will be required to apply a stress event to the cash flow forecasts reported in the 31 December 2024 QMA 350u and report the results to Lloyd's. The stress to be applied is a 1-in-200 year US windstorm or the syndicate's most severe liquidity risk event (as appropriate to the nature of the syndicate and its risk profile) and a simultaneous diminution in the valuation of its asset portfolio. The scenario should also assume some delays in payment of recoveries by reinsurers. Further details are provided in section 2.3.

Lloyd's expects that syndicates can withstand this stress using existing resources and committed or contractual sources of funding. Syndicates that cannot withstand the stress will be subject to greater oversight and will be expected to take remedial action to strengthen their liquidity risk resilience.

1.3 Next steps

- Requested syndicates to complete the liquidity stress testing exercise and report results – by 30 April 2025
- Evaluation of results by Lloyd's and follow up discussions with syndicates not able to withstand the stress – 1 May to 30 June 2025
- Remediation by syndicates not able to withstand the stress completed – 31 July 2025

2 Completion of the liquidity stress test template

2.1 Introduction

The stress test template is attached in the appendix. For the avoidance of doubt, one template is required per syndicate.

2.2 31 December 2024 QMA position

The tab "31 Dec 2024 QMA position" of the template should be prepared consistently with the QMA 350u that was reported in the Q4 2024 QMA return.

All lines in the template are to be reported at 31 December 2024 exchange rates.

Completion notes

All yellow cells in the template are to be completed.

Basic information

Please complete the syndicate number, name, managing agent, date completed and QMA date fields.

Capital position

Please enter the latest syndicate uSCR and uECA, as per the latest Lloyd's Capital Return. Please also indicate the syndicate's view of its allocation of Funds At Lloyd's (FAL) and Funds In Syndicate (FIS). (Lloyd's notes that the syndicate view of its total FAL may differ from Lloyd's view due to Lloyd's access to the diversification benefit afforded to members who participate across multiple syndicates, but wishes to obtain the syndicate's view nonetheless for cross-reconciliation purposes).

Asset and liquidity breakdown from QMA form 201

Please split the total assets reported on the QMA form 201 as at 31 December 2024 between restricted assets, illiquid assets and liquid assets / free funds.

Cashflow position from QMA350

The forecasting columns represent a 12 month cash flow from the 31 December 2024 balance sheet. Therefore, the closing free funds in the 31 December 2024 column will be the opening free funds for the forecast (i.e. for the cells under heading "Cashflow position from QMA Form 350" B1=A16, C1=B16 etc). This line is populated using formulae.

Gross premium income is to be gross of acquisition costs, and net operating expenses are to include acquisition costs.

For the purpose of this form, free funds should only include those funds readily available to pay all claims and syndicate expenses. These are in line with the instructions to QMA350u that are issued for QMA reporting. e.g. the sterling PTF, Canadian PTFs (excluding LCTF-reg), and LDTF. It should exclude Central Fund and ASL loans, assets held in the CRTF or SLTF as well as any funds restricted by covenants such as collateralisation for letters of credit.

Note the following:

- Any reinsurance deposit payments and/or collateral withdrawals included in reinsurance recoveries, row 3 of Form 350 of the QMA / estimated in future cashflow, should be split out into row 3a of this form. The total of rows 3 and 3a in this form should equal row 3 within the QMA. Please provide a description of the reinsurance deposit payments and/or collateral withdrawals received/(repaid), and also a description of the reinsurance contract terms that were triggered to allow such to occur, in the NB1 comments field below the main table.
- Any cash call receipts/(Distributions) included in row 13 of Form 350 of the QMA / estimated in future cashflow which relate to FAL / FIS draw/ (repayment) should be split out into row 13a of this form. The total of rows 13 and 13a in this form should equal row 13 within the QMA.

2.3 1-in-200 stressed scenario

Completion notes

All yellow cells in the template are to be completed.

Basic information

Please complete the syndicate number, name, managing agent, date completed and QMA date fields.

Loss summary

Identify the region / peril and 1-in-200 gross loss that is most appropriate to the syndicate. Where this is not a US Windstorm, please document in the NB1 comments field at the bottom of the tab. Select the reinsurance recoveries expected on the gross loss, and the net loss.

Top 10 reinsurers' summary

From the total reinsurance recovery, the top 10 reinsurers in terms of value should be identified and disclosed. Please complete: reinsurer's legal title, reinsurer's LORS code, total reinsurance recovery in GBP, collateral available for recovery and the percentage of the total recovery provided by the reinsurer in question.

Asset and liquidity breakdown and cashflow position

These should be prepared assuming that the liquidity stress event described in section 1.2 takes place on 28 February 2025 and requires the forecast cash flow and balance sheet positions to be updated as at the date of the loss and in respect of the first, second and third months following the event, as well as the second, third and fourth quarter-ends following the event.

Each line item should be prepared consistently with those on the 31 December 2024 tab, but updated for the impact of the stress as appropriate, by applying the assumptions set out below.

Assumptions to be applied

Forecast cash flows should take into account the syndicate's latest approved business plan for the 2025 year of account.

In most cases, it should be assumed that there is a US funding requirement for your estimated ultimate loss (if a US event is selected), which must be funded 60 days following the end of the quarter in which the loss occurs.

For US reinsurance business, please apply the most appropriate funding requirement, given the changes to SITUS affecting the CRTF for business written since 1 October 2022.

If the most appropriate loss selection relates to policies written prior to 1 October 2022 that are subject to the CRTF, the funding requirement should be assumed to be 100% of syndicate estimated liabilities, net of any credit taken for withheld premiums (which should not be more than 10%). This assumption can be reduced in those instances where the syndicate has entered into a contractual agreement with a cedant at inception to provide upfront collateral of 20% of estimated liabilities, and where such an arrangement is permitted by a US state to remove the reinsurers requirement to fund at 100%.

If the most appropriate loss selection relates to policies that were written after 1 October 2022 for US reinsurance business, then no US funding requirement can be assumed.

For US surplus lines business (subject to the SLTF), there have been no changes to the funding requirements. The funding requirement should be assumed to be in a tiered scale as follows:-

- Liabilities up to $200m = 30% reserves
- Liabilities $200m - $500m = 25% reserves
- Liabilities $500m - $1bn = 20% reserves
- Liabilities xs $1bn = 15% reserves

Assume three reinsurers, with the largest financial shares of the total estimated reinsurance recoveries, dispute their liability for both funding and/or settlement. For two of the reinsurers, the dispute takes 60 days longer than usual contractual terms to resolve and for the other reinsurer, the dispute takes 90 days longer than usual contractual terms. Settlement should therefore be reflected 60 and 90 days respectively after the usual contractual settlement terms.

In addition, assume that a diminution in asset values occurs as a result of a forced sale of assets, applying the following haircuts in line with the Basel III High Quality Liquid Asset framework:

Liquid asset	**Haircut**
Cash: overnight cash deposits & mutual funds	0%
Cash: commercial paper & term deposits	15%
Bonds: UK & US government	0%
Bonds: other government, corporate and covered bonds rated AA- or better	15%
Bonds: RMBS	25%
Bonds: corporate bonds rated A+ to BBB	50%
Developed market equities	50%

Please record the impact of the asset shock as occurring in February 2025, in row 1b of the 1-in-200 stressed scenario tab.

In row 2, “premium income”, in the stress scenario cashflow, assume that there is no increase in premium income compared to the “31 Dec 2024 QMA position” tab as a result of rate increases following the loss, or for any other reason.

In the event that the loss triggers a reinstatement premium payable on outwards reinsurance policies, please record this in row 7, “outwards reinsurance premiums”. Reinstatement premium on inwards reinsurance policies may be recorded in row 2, “premium income”.

Please additionally provide a justification in the NB3 comments field of the payment pattern assumptions used for the gross loss in row 6, gross claims paid. Please also indicate the source of this data. Lloyd's starting assumption for US Windstorm losses is that the payment pattern assumptions applied to the first 10 months after the gross loss should be at least equal to that experienced in the 2017 HIM losses.

Free funds should align with the definition in the QMA, however syndicates are also expected to consider the extent to which the free funds can be used to meet the cashflows in the specific scenario. For example, balances held in Canadian Trust Funds would not be expected to be able to be available to settle a US Windstorm event. Ultimately, this means that syndicates might have to rely on external funding sources if all of the free funds cannot be used in the scenario chosen.

Funding / management actions
The additional columns in this tab relating to funding and management actions are intended to give Lloyd’s a view of the contingency arrangements that are available to the syndicate.
Please split the possible contingency funding sources as follows:

- Funding from reinsurers
- Funding from banks
- Funding from parent / group
- Cash call receipts
- Funding from other sources
- FAL / FIS draw
- Loan to Central Fund

Where credit facilities are disclosed in the stress scenario, these should be committed facilities only. The definition of a committed facility is as follows:

“A committed facility is a credit facility whereby terms and conditions are clearly defined by the lending institution and imposed upon the borrowing company. In committed facilities, the borrowing company must meet specific requirements set forth by the lending institution in order to receive the stated funds”.

Any committed facilities disclosed should have been negotiated and signed prior to 31 December 2024. No uncommitted facilities should be recognised in the stress scenario (ie. short-term credit facilities which are subject to the discretion of both the borrower and the lender).

Funding that is anticipated from group/parent companies should only be included where the syndicate is able to demonstrate beyond all doubt that the syndicate would be able to access the liquidity in any hypothetical scenario. For example, cash pooling arrangements that multiple subsidiaries within a group are able to access would not be expected to meet this definition. If group/parent company funding is disclosed, please provide details in the NB4 comments field justifying why management is certain that this would be available upon request at all times.

2.4 Qualitative questionnaire

The “Qualitative questionnaire” tab requests further detail about the committed facilities that the syndicate has disclosed in the stress scenario tab. It also requests detail about any uncommitted facilities and / or parent / group support that management may anticipate would be available, as additional information.

Further questions relate to the extent that FAL is considered as source of liquidity in the syndicate’s risk management framework, and any live liquidity concerns or issues.

3 Reporting results and timetable

3.1 Reporting results

Completed templates should be submitted to: LLoyds-SolvencyReturns@lloyds.com

3.2 Timetable

All completed templates must be submitted to Lloyd's by 30 April 2025. As with all Lloyd's reporting, late returns will be considered within the governance, risk management and reporting dimension of the syndicate's Rio assessment.

3.3 Questions

If managing agents have questions on the preparation of the liquidity stress template, please contact: LLoyds-SolvencyReturns@lloyds.com

4 Governance and sign-off

4.1 Governance and sign-off

All completed templates submitted to Lloyd's must be signed off by a director of the managing agent.

5 Template for completion

The template is available on the Lloyd's website at this link:

https://www.lloyds.com/conducting-business/regulatory-information/solvency-ii/tools-and-resources/syndicate-workstreams/reporting-and-disclosure

The name of the template is "Liquidity Stress Test Template_December 2024".