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Syndicate 1856

Annual Accounts

31 December 2020

ARCUS 1856

CONTENTS

DIRECTORS AND ADMINISTRATION

Arch Managing Agency Limited (Formerly Barbican Managing Agency Limited)

Directors

S Bashford	(Appointed 30 April 2020)
N Denniston	(Appointed 30 April 2020)
J Kittinger	
P Leoni	(Appointed 30 April 2020)
P Martin	(Resigned 12 January 2021)
J Mentz	(Appointed 30 April 2020)
P Storey	(Appointed 30 April 2020)
H Sturgess	
M Hammer-Dahinden	(Appointed 30 April 2020)
A Flanagan	(Appointed 1 January 2021)
D Booth	(Resigned 30 April 2020)
W Canageretna	(Resigned 8 January 2021)
H Colthurst	(Resigned 30 April 2020)
A Elliott	(Resigned 30 April 2020)
J Heap	(Resigned 30 April 2020)
R Johnson	(Resigned 30 April 2020)
R Keers	(Resigned 30 April 2020)
L Tucker	(Resigned 30 April 2020)

Managing Agent's Registered Office

60 Great Tower Street
London
EC3R 5AZ

Managing Agent's Registered Number

06948515

Company Secretary

Z L Nattress	(Resigned 19 June 2020)
P A Ralph	(Appointed 1 November 2020)

Syndicate Active Underwriter

A Shepherd

Bankers

Lloyds Bank plc
Citibank NA
RBC Investor and Treasury Services

Auditor

Ernst & Young LLP
25 Churchill Place
Canary Wharf
London
E14 5EY

REPORT OF THE DIRECTORS OF THE MANAGING AGENCY

The Directors of the Managing Agent ("the Agency") present their annual report and accounts for Syndicate 1856 ("the Syndicate"), for the year ended 31 December 2020.

The annual accounts are prepared using the annual basis of accounting as required by Statutory Instrument No 1950 of 2008, The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 ("Lloyd's Regulations 2008").

Managing Agent

The Managing Agent of the Syndicate since its inception on 1 January 2016 is Arch Managing Agency Limited ("the Agency") formally known as Barbican Managing Agency Limited.

Principal Activity

The principal activity of the Syndicate is the transaction of general insurance and reinsurance business as described below in the Review of the Business.

Capacity of the Syndicate for the 2020 year of account is £109.2m (2019 year of account: £104.9m), The capital providers continue to be Iris Low Volatility Plus Corporate Member Limited, Iris Balanced Corporate Member Limited and Humboldt Corporate Member Limited (known collectively as "Corporate Members").

The result for calendar year 2020 is a loss of £49.88m (2019: £1.8m Loss).

Key Performance Indicators

The Syndicate's key financial performance indicators during the year were as follows:

	2020 £000	2019 £000
Gross premiums written	78,958	106,530
Gross premiums earned	76,217	104,299
Net premiums earned	34,115	70,053
Net claims incurred	(54,541)	(48,737)
Investment return	984	1,638
Operating expenses	(31,520)	(25,157)
Realised and unrealised movements on foreign exchange	1,083	359
Loss for the year	(49,879)	(1,844)
Claims ratio	159.9%	69.6%
Expense ratio	92.4%	35.9%
Combined ratio	252.3%	105.5%

Review of the Business

For 2020 Year of Account the Syndicate capacity was £109.2m (2019: £104.9m). It underwrote for third party investors who supported the overall Syndicate underwriting activity through its Corporate Members.

The Syndicate wrote six classes of business in 2020 amounting to £128m gross written premium (2019: £106.5m). In addition, a return premium of £49m net was paid to Syndicate 1955 in relation to the commutation of the whole account quota share on the 2017 & prior years of account. This reduced the gross written premium in the year to £79m. For 2021 gross written premium of £144m is forecasted.

The loss for the year is the result of several medium sized events in 2020 which were largely under the attachment point of our catastrophe outwards protections and therefore a net loss to the syndicate. In particular hurricanes Laura and Sally, the Iowa Derecho and the hailstorm in Alberta caused significant losses. The net combined ratio is heavily affected by the premium transfer to syndicate 1955. Without this transfer the NCR would be at 134%.

The overall gross COVID-19 reserve for the syndicate is £10.9m, while the net reserve is £9.8m with the majority coming from the Property Treaty account.

Property Reinsurance

2020 gross written premium was £49m (2019: £55.2m). 2021 gross written premium forecast £59m.

The portfolio is 65% US and 35% ex US. For the US account, there is increased impetus to refocus on the Super Regional and Regional portfolios and to move away from the Nationwide accounts, helping to reduce our peak exposures. The International account focuses on Japan, Europe, Australasia, and Canada. The account focuses on long-standing relationships with clients and brokers. Analytics forms the backbone of the underwriting process. Following several loss affected years there has been sustained, year on year rate increases. North American Treaty Catastrophe rates are expected to increase circa 5-10%. International Treaty rates are expected to be flat to +5% although encouragingly the wind layers in Japan are looking to be up between 5-10%.

Energy

2020 gross written premium £12m (2019: £16.1m). 2021 gross written premium forecast £15m.

The Upstream portfolio will consist of clients from all areas of the hydrocarbon extraction business. We will look to insure clients focused on exploration through to field development and the onward production phase. Target clients will be concentrated around the oil and gas operating companies which would range from National and Multinational Oil companies through to independent single location entities. The Downstream portfolio will include onshore energy and power covering all parts of the downstream chain from extraction to final product. Limited exposure to Nat Cat perils including very limited GOM wind exposure for Upstream Energy. The Upstream portfolio will prefer open market, facultative direct business through the Lloyd's brokers. There will be limited appetite for broker lines slips and facilities. The Downstream portfolio will achieve a balanced portfolio through quota share participations and a preference for higher layers on non-proportional placements. The Upstream market saw a 5%-7.5% positive rate change in Q1 2021 on average and we anticipate this to continue for the full year. The Downstream market continues to experience increasing market rates with a continued double digit rating environment on top of the 15% experienced in 2019 and 25% in 2020.

Space

Gross written premium in 2020 was £10m (2019: £4m). For 2021 the syndicate will no longer be writing the Space class of business. This is largely due to historical poor performance.

Cyber

Gross written premium in 2020 was £17m (2019: £12.9m). Gross written premium forecast £20m for 2021.

This class has grown in a considered manner over the last few years. We have only ever looked to have a small number of relationships where we can provide capacity on a binding authority or consortium basis. During 2020 we have added two such relationships. At the 1st January 2021 we have not renewed two contracts. One which had poorer experience relative to the other contracts in the book coupled with the highest level of acquisition costs; the non-renewal of this accounts also materially reduces the aggregation clash of the portfolio. The other due to the presence of a specific facility that we were unable to remove. We see the management of line sizes and retentions as a key tool against the increasing trend of losses and this is a feature that is monitored for the facilities that we support. The cyber market's losses have also been relatively indiscriminate by industry sector – with sectors such as education, manufacturing and municipalities being the targets of numerous ransomware events - so Arcus maintains its strategy of seeking a diversified portfolio. The facilities supported in 2021, are forecasting anticipated RARC of between +10% and 20%.

Property Insurance

2020 gross written premium £26m (2019: £13.5m). 2021 gross written premium £35m.

The property delegated insurance portfolio currently comprises 24 in-force binding authority contracts, all exclusively with US-based exposure. All the portfolio is written on an Excess & Surplus basis, with most of the portfolio commercial lines focused with homeowners' business a smaller component. Risk appetite to date has been very much to write catastrophe exposed business. Our aim is to maintain low volatility from a per-risk basis. Average max line for big ticket commercial of $2.3m, mid-market commercial $1.9m, SME $1.1m and homeowners of $390k. The current portfolio is closely aligned with our appetite to take on low volatility occupancies. The existing philosophy for the delegated portfolio has been based on the key principles to partner with those with sophistication, scale and emerging technology at the core of their business model. We have focused our attention with partners who display superiority in all facets of the risk lifecycle. That is pre-eminence in risk selection, portfolio management, and claims handling. Our partners are best placed to profit from the shift to data driven underwriting. Second to this, where those qualities exist within a cover holder, we have sought to partner with those with a wide distribution base, access to risk whether via the wholesale market or direct to retailer. A continuation of positive rate momentum seen over the last 24 months is forecast for 2021, access to better risk improves as domestic E&S carriers continue remediation work on their own portfolios, and tighter underwriting guidelines for cover holders has refined risk appetite to lower hazard occupancies. With this in mind, we believe both on a CAT and AOP expected loss ratios will continue to show improvement. Risk adjusted rate change of +13% achieved at 1st Jan. 4% reduction in acquisition costs year on year. The largest rate increases were seen in peak CAT exposures in Florida, and specifically Tri-County. In Tri-County we have seen up to 20% rate increases. Underlying terms and conditions have also shown improvement. Bolt-on additional coverages although not completely removed have had some coverages have been scaled back. As well as rate there has been a positive upward movement on percentage wind/hail deductibles, and increased AOP deductibles are being achieved.

Property Proportional

2020 gross written premium £14m (2019: £0m). 2021 gross written premium £15m.

The property proportional book comprises 6 active contracts, of which all except TOA Reinsurance Company are solely USA exposed. The class of business is very much run-in conjunction with the property insurance portfolio to access specific risk segments. This is not a traditional quota share book. It is a reinsurance of insurance books with cedants being primary carriers and in certain cases MGAs. The key focus is forming partnerships on a proportional reinsurance basis where the underlying portfolios are managed with the same sophistication as the insurance book. That being partners who hold sophistication, scale, and use emerging technology at the core of their business model. As we focus on the US E&S market, we anticipate similar expected rate growth as the insurance book in 2021. The portfolio is very much focused on writing low attritional occupancy classes in CAT exposed areas of the US. The bulk of the portfolio sits within two main contracts. The former of these focuses on full value commercial SME and homeowners' business whilst the latter is all excess of loss on commercial business (ranging from SME to mid-market). The approximate split between full value and excess of loss exposures on the book is 65:35. We look to form relationships with clients who display a cautious approach to their underwriting around All Risk perils, and display balance and aptitude at pricing the CAT components of risk. We avoid medium to heavy industry commercial classes and are keen to avoid business that does not have a CAT element to the risk. Florida is our largest component of the book and we have looked to diversify the Tropical Cyclone footprint outside of Florida in other Tier 1 and 2 counties from Texas to Maine. The 5% component of the book that is earthquake exposed is based in California predominately.

Investment Returns

The Syndicates total investable funds at the end of 2020 were £54.4m which is a reduction of £26.4m (2019: £80.8m), this is principally due to the return premium of £49m transferred to Syndicate 1955 in relation to the whole account Quota share 2017 & prior years of account contract commutation. The reduction has also been impacted by a high volume of claims in 2020, this has reduced the funds available to invest resulting in a lower investment yield in the year.

Investment yield decreased overall in 2020 to 1.47% (2019: 2.11%). The 2020 investment return of £1.0m is below prior year (2019: £1.6m) due to decrease of funds and short-term deposits.

Principal Risks and Uncertainties

The Board of the Agency ("Agency Board") sets risk appetite annually as part of the Syndicate's business planning and individual capital assessment process.

The Agency Board has developed a risk and control framework which is built on an Enterprise Risk Management Model that aims to integrate existing risk programmes into a more holistic, embedded risk and capital management framework. This is reviewed annually as part of the Syndicate Business Forecast ("SBF") and Solvency Capital Requirement ("SCR") process.

The UK has now left the European Union, accordingly the legal and operational changes emanating from that decision have generated an elevated level of risk for Lloyd's and the London Market. To compensate the Syndicate has been utilising Lloyd's Brussels to mitigate these new risks.

Further analysis of the principal risks and uncertainties can be found in Note 19 in the Notes to the Annual Accounts.

Insurance Risk

Insurance risk includes the risks that a policy will be written for inadequate premium or provide inappropriate cover (underwriting risk), that the frequency or severity of insured events will be higher than expected (claims risk), and that estimates of claims subsequently prove to be insufficient (reserving risk). The Agency Board overseas insurance risk by agreeing its appetite for these risks annually and managing this primarily through the business plan, which sets out targets for volumes, pricing, line sizes and retention by class of business. The Agency Board then monitors performance against the business plan regularly throughout the year. Catastrophe modelling software is used to model maximum probable losses from catastrophe-exposed business. Reserve adequacy is monitored through a quarterly review by the Syndicate actuary and reviewed annually by an independent firm of actuaries.

Credit Risk

The key aspect of credit risk is the risk of default by one or more of the Syndicate's reinsurers. The Agency Board's policy is that the Syndicate generally reinsures with businesses rated A- or higher by one or more rating agencies. The Syndicate only uses reinsurers with lower ratings or unrated reinsurers where collateral or a claim paying guarantee from a parent undertaking is provided. As at 31 December 2020, the Syndicate had £83.4m of collateral (2019: £63.8m).

Currency Risk

The key aspect of currency risk is the risk of losses on foreign exchange movements as a result of mismatches between the currencies in which assets and liabilities are denominated. The Agency Board's policy is to maintain all assets and liabilities in the core currencies in which they were received or paid. Any surplus or deficit in a core currency is subject to review by the Agency Board, which may result in surplus currencies being sold to make good a deficit on other currencies.

Liquidity Risk

This is the risk that the Syndicate will not be able to meet its liabilities as they fall due, owing to a shortfall in cash. To mitigate this risk, the Agency Board reviews cash flow projections regularly and ensures the Syndicate holds adequate liquid investments in its portfolios. The Syndicate produces an 18 month cash flow forecast to assist with liquidity monitoring.

Group Risk

Group risk is the possibility that the operation of one part of the Arch Group, of which the Managing Agency is a member, adversely affects another.

Group risk includes negative publicity, inadequate communication within the organisation, undue influence from fellow subsidiaries, holding companies or stakeholders, financial pressures to make funds available to the Group, and financial restraint leading to shortcomings in core activities such as reinsurance purchasing.

The Agency Board's strategy is to minimise any Group risk by ensuring that there are clear lines of authority and communication between related parties, that intra-Group reinsurance is placed on arm's length terms and that any intra-Group agreements are clearly understood and observed by all parties.

Operational Risk

This is the risk that errors caused by people, processes or systems lead to losses to the Syndicate. The Agency Board seeks to manage this risk through the use of policies, procedures, management controls, risk-based compliance monitoring, and a structured programme of testing processes and systems by internal audit. Business continuity and disaster recovery plans are in operation and are regularly updated.

Regulatory Risk

The Agency is required to comply internally with the requirements of the Financial Conduct Authority ("FCA"), the Prudential Regulation Authority ("PRA"), and the Society of Lloyd's (Lloyd's). Lloyd's requirements include those imposed on the Lloyd's market by overseas regulators, particularly in respect of US Situs business and certain EU regulators. Regulatory risk is the risk of regulatory intervention owing to a breach of regulatory requirements or failure to respond to regulatory change. The Agency Board has appointed the Agency Compliance Officer to monitor regulatory developments, assess the impact on the Agency's policies and processes and report to the Agency Board.

Market Risk

Market risk is the risk or uncertainty arising from possible market price movements and their impact on the future performance of a Syndicate.

Future Developments

For the 2021 year of account, capital to support the syndicate's underwriting changed from funds managed by Credit Suisse ILS to ERS' corporate member. Support is for the currently approved business plan. But it is likely that early in the year, a resubmission to Lloyd's will be made that increases the capacity and introduces new classes of business. This is in line with ERS' ambition to build a diverse, scaled Lloyd's operation as part of their overall strategy for the business. It is also the intention that later in 2021 management of the syndicate will novate from Arch to ERS. At that stage the syndicate, managing agency and corporate member will be fully aligned.

Disclosure of Information to the Auditor

So far as each person who was a Director of the Agency at the date of approving this report is aware, there is no relevant audit information, being information needed by the auditor in connection with its report, of which the auditor is unaware. Having made enquiries of fellow Directors of the Agency and the Syndicate's auditor, each Director has taken all the steps that he is obliged to take as a Director in order to make himself aware of any relevant audit information and to establish that the auditor is aware of that information.

Jason Kittinger
Agency Finance Director
11 March 2021

MANAGING AGENT'S RESPONSIBILITIES STATEMENT

The Agency is responsible for preparing the Managing Agent Report and Syndicate Annual Accounts in accordance with applicable law and regulations.

The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 require the Agency to prepare Syndicate Annual Accounts at 31 December each year in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The Syndicate Annual Accounts are required by law to give a true and fair view of the state of affairs of the Syndicate as at that date and of its profit or loss for that year. In preparing the Syndicate Annual Accounts, the Agency is required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the notes to the Syndicate Annual Accounts; and
- prepare the Syndicate Annual Accounts on the basis that the Syndicate will continue to write future business unless it is inappropriate to presume that the Syndicate will do so.

The Agency is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Syndicate and enable it to ensure that the Syndicate Annual Accounts comply with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008. It is also responsible for safeguarding the assets of the Syndicate and hence for taking reasonable steps for prevention and detection of fraud and other irregularities.

The Agency is responsible for the maintenance and integrity of the corporate and financial information included on the business' website. Legislation in the United Kingdom governing the preparation and dissemination of Annual Accounts may differ from legislation in other jurisdictions.

INDEPENDENT AUDITOR’S REPORT TO THE MEMBERS OF ARCUS SYNDICATE 1856

Opinion

We have audited the syndicate annual accounts of syndicate 1856 (‘the syndicate’) for the year ended 31 December 2020 which comprise the Income Statement, the Statement of Comprehensive Income, the Statement of Members’ Balances, the Statement of Financial Position, the Statement of Cash Flows and the related notes 1 to 24, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards including FRS 102 ‘The Financial Reporting Standard applicable in the UK and Republic of Ireland’ and FRS 103 ‘Insurance Contracts’ (United Kingdom Generally Accepted Accounting Practice).

In our opinion, the syndicate annual accounts:

- give a true and fair view of the syndicate’s affairs as at 31 December 2020 and of its loss for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of The Insurance Accounts Directive (Lloyd’s Syndicate and Aggregate Accounts) Regulations 2008.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor’s responsibilities for the audit of the syndicate annual accounts section of our report. We are independent of the syndicate in accordance with the ethical requirements that are relevant to our audit of the syndicate annual accounts in the UK, including the FRC’s Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In auditing the syndicate annual accounts, we have concluded that the managing agent’s use of the going concern basis of accounting in the preparation of the syndicate annual accounts is appropriate.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the syndicate’s ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from when the syndicate annual accounts are authorised for issue.

Our responsibilities and the responsibilities of the managing agent with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the syndicate’s ability to continue as a going concern.

Other information

The other information comprises the information included in the annual report set out on pages 3 to 9, other than the syndicate annual accounts and our auditor’s report thereon. The directors of the managing agent is responsible for the other information contained within the annual report.

Our opinion on the syndicate annual accounts does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the syndicate annual accounts or our knowledge obtained in the course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the syndicate annual accounts themselves. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the managing agent's report for the financial year in which the syndicate annual accounts are prepared is consistent with the syndicate annual accounts; and
- the managing agent's report has been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the syndicate and its environment obtained in the course of the audit, we have not identified material misstatements in the managing agent's report.

We have nothing to report in respect of the following matters where The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 requires us to report to you, if in our opinion:

- the managing agent in respect of the syndicate has not kept adequate accounting records; or
- the syndicate annual accounts are not in agreement with the accounting records; or
- certain disclosures of the managing agents' emoluments specified by law are not made; or

we have not received all the information and explanations we require for our audit.

Responsibilities of the managing agent

As explained more fully in the Statement of Managing Agent's Responsibilities set out on page 9, the managing agent is responsible for the preparation of the syndicate annual accounts and for being satisfied that they give a true and fair view, and for such internal control as the managing agent determines is necessary to enable the preparation of the syndicate annual accounts that are free from material misstatement, whether due to fraud or error.

In preparing the syndicate annual accounts, the managing agent is responsible for assessing the syndicate's ability to continue in operation, disclosing as applicable, matters related to its ability to continue in operation and using the going concern basis of accounting unless the managing agent either intends to cease to operate the syndicate, or has no realistic alternative but to do so.

Auditor's responsibilities for the audit of the syndicate annual accounts

Our objectives are to obtain reasonable assurance about whether the syndicate annual accounts as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these syndicate annual accounts.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below. However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the managing agent and management.

Our approach was as follows:

- We obtained a general understanding of the legal and regulatory frameworks that are applicable to the syndicate and determined that the most significant are direct laws and regulations, related to elements of Lloyd’s Byelaws and Regulations, and the financial reporting framework (UK GAAP), and requirements referred to by Lloyd’s in the instructions. Our considerations of other laws and regulations that may have a material effect on the syndicate annual accounts included permissions and supervisory requirements of Lloyd’s of London, the Prudential Regulation Authority (‘PRA’) and the Financial Conduct Authority (‘FCA’).
- We obtained a general understanding of how the syndicate is complying with those frameworks by making enquiries of management, internal audit, and those responsible for legal and compliance matters of the syndicate. In assessing the effectiveness of the control environment, we also reviewed significant correspondence between the syndicate, Lloyd’s of London and other UK regulatory bodies; reviewed minutes of the Board and Risk Committee of the managing agent; and gained an understanding of the managing agent’s approach to governance.
- For direct laws and regulations, we considered the extent of compliance with those laws and regulations as part of our procedures on the related syndicate annual accounts’ items.
- For both direct and other laws and regulations, our procedures involved: making enquiry of the directors of the managing agent and senior management for their awareness of any non-compliance of laws or regulations, inquiring about the policies that have been established to prevent non-compliance with laws and regulations by officers and employees, inquiring about the managing agent’s methods of enforcing and monitoring compliance with such policies, inspecting significant correspondence with Lloyd’s, the FCA and the PRA.
- The syndicate operates in the insurance industry which is a highly regulated environment. As such the Senior Statutory Auditor considered the experience and expertise of the engagement team to ensure that the team had the appropriate competence and capabilities, which included the use of specialists where appropriate.

Our audit procedures included:

- Reviewing accounting estimates for evidence of management bias. Supported by our Actuaries, we assessed if there were any indicators of management bias in the valuation of gross IBNR reserves and the recognition of estimated premium income.
- Evaluating the business rationale for significant and/or unusual transactions.
- Testing the appropriateness of journal entries recorded in the general ledger, particularly in respect of judgemental areas including gross IBNR reserves and estimated premium income.

In addition, we considered the impact of Covid-19 on the Syndicate, including an assessment of the consistency of operations and controls in place as they transitioned to operating remotely for a significant proportion of 2020, making enquiries with management via the use of video conferencing. We performed analytical review procedures to assess for unusual movements throughout the year. Our audit procedures also incorporated unpredictability into the nature, timing and extent of our testing.

A further description of our responsibilities for the audit of financial statements is located on the Financial Reporting Council's website at https://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Use of our report

This report is made solely to the syndicate's members, as a body, in accordance with The Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008. Our audit work has been undertaken so that we might state to the syndicate's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the syndicate and the syndicate's members as a body, for our audit work, for this report, or for the opinions we have formed.

Robert Bruce (Senior statutory auditor)

for and on behalf of Ernst & Young LLP, Statutory Auditor

London

11 March 2021

INCOME STATEMENT

Technical Account – General Business

For the year ended 31 December 2020

	Notes	2020 £000	2019 £000
Gross premiums written	2	78,958	106,530
Outward reinsurance premiums		(38,332)	(37,399)
Net premiums written		40,626	69,131
Change in the provision for unearned premiums:			
- Gross amount		(2,741)	(2,231)
- Reinsurers' share		(3,770)	3,153
Change in the net provision for unearned premiums	10	(6,511)	922
Earned premiums, net of reinsurance		34,115	70,053
Allocated investment return transferred from non-technical account	3	984	1,638
Claims paid			
- Gross amount	11	(88,655)	(85,042)
- Reinsurers' share	11	24,054	38,085
Net claims paid		(64,601)	(46,957)
Change in claims outstanding			
- Gross amount		40,798	(5,511)
- Reinsurers' share		(30,738)	3,731
Change in the net provision for claims	11	10,060	(1,780)
Claims incurred, net of reinsurance	11	(54,541)	(48,737)
Net operating expenses	4	(31,520)	(25,157)
Balance on the technical account for general business		(50,962)	(2,203)

Non-Technical Account – General Business

For the year ended 31 December 2020

	Notes	2020 £000	2019 £000
Balance on the general business technical account		(50,962)	(2,203)
Investment income	3	846	1,324
Unrealised gains/(losses) on investments		49	206
Realised gains/(losses) on investments		123	128
Investment expenses and charges		(34)	(20)
		984	1,638
Allocated investment return transferred to general business technical account		(984)	(1,638)
Foreign exchange gain/loss		1,083	359
Loss for the year		(49,879)	(1,844)

STATEMENT OF CHANGES IN MEMBERS' BALANCES

For the year ended 31 December 2020

	2020	2019
	£000	£000
At 1 January	(17,779)	(15,741)
Loss for the year	(49,879)	(1,844)
Distribution Profit	-	(194)
Distribution Loss	6,639	-
Cash Call	9,992	-
At 31 December	(51,027)	(17,779)

STATEMENT OF FINANCIAL POSITION

ASSETS

As at 31 December 2020

	Notes	2020 £000	2019 £000
Investments			
Financial investments	8	46,230	62,766
Reinsurers' share of technical provisions			
Provision for unearned premiums	10	11,685	15,778
Claims outstanding	11	44,201	75,293
		55,886	91,071
Debtors			
Debtors arising out of direct insurance operations – intermediaries	16	20,840	16,445
Debtors arising out of reinsurance operations	14	23,225	37,111
Other debtors	18	280	626
		44,345	54,182
Other assets			
Cash at bank and in hand	12	5,700	16,638
Other deposits	8	2,512	1,413
		8,212	18,051
Deferred acquisition costs	13	11,037	9,098
Total assets		165,710	235,168

STATEMENT OF FINANCIAL POSITION

MEMBERS' BALANCES AND LIABILITIES

As at 31 December 2020

	Notes	2020 £000	2019 £000
Members' balances and liabilities			
Members' balances		(51,027)	(17,779)
Liabilities			
Technical provisions			
Provision for unearned premiums	10	45,502	46,268
Claims outstanding	11	142,225	184,673
Unexpired risk provision	11	2,000	-
		189,727	230,941
Creditors due within one year			
Creditors arising out of reinsurance operations	17	24,318	20,524
Other creditors	15	1,793	1,482
		26,111	22,006
Accruals and deferred income		899	-
Total liabilities		216,737	252,947
Total members' balances and liabilities		165,710	235,168

The Annual Accounts on pages 14 to 50 were approved by the Board of Arch Managing Agency Limited on 9 March 2021 and were signed on its behalf by

Jason Kittinger

Agency Finance Director

11 March 2021

STATEMENT OF CASH FLOWS

For the year ended 31 December 2020

	Notes	2020 £000	2019 £000
Cash flows from operating activities			
Loss for the financial year		(49,879)	(1,844)
Adjustments for			
Movement in general insurance unearned premiums and outstanding claims	10, 11	(41,214)	(495)
Movement in reinsurers' share of unearned premiums and outstanding claims	10, 11	35,185	(3,464)
Investment return	3	(984)	(1,638)
Movements in other assets/liabilities		13,062	15,823
Net cash from operating activities		(43,830)	8,382
Cash flows from investing activities			
Sale / (Purchase) of equity and debt instruments		17,757	(24,920)
Investment income received		824	1,613
Other		(2,320)	(951)
Net cash used in investing activities		16,261	(24,258)
Cash flows from financing activities			
Distribution loss/ open year cash calls made/ call not paid		16,631	-
Other		-	(6,216)
Net cash from financing activities		16,631	(6,216)
Net increase in cash and cash equivalents		(10,938)	(22,092)
Cash and cash equivalents at the beginning of the year		16,638	38,730
Cash and cash equivalents at the end of the year	12	**5,700**	**16,638**

NOTES TO THE ANNUAL ACCOUNTS

1. Significant Accounting Policies

a. Statement of Compliance

The annual accounts have been prepared in compliance with FRS 102 and FRS 103, being applicable UK GAAP accounting standards and the "Insurance Accounts Directive" (Lloyd's Syndicate Accounts) Regulations 2008.

The annual accounts are prepared under the historical cost convention except for certain financial instruments which are measured at fair value.

b. Basis of Preparation

The annual accounts for the year ended 31 December 2020 were approved for issue by the Board on 8 March 2020. The annual accounts are prepared in Sterling (rounded to the nearest £000) which is the presentational and functional currency of the Syndicate. The Syndicate has a whole account Quota Share contract consisting of business written by syndicate 1955 on a net basis (Net of reinsurance spend, claims and expenses) for 2018 and prior years of account. During the year, the syndicate commuted the 2017 and prior years whole account Quota Share with syndicate 1955 resulting in a premium refund of £49m, that has been settled during the year.

c. Judgements and Key Sources of Estimation Uncertainty

The preparation of the annual accounts requires management to make judgements, estimates and assumptions that affect the amounts reported for assets and liabilities as at the date of the annual accounts and the amounts reported for revenues and expenses during the year under review. However actual outcomes may differ from those estimates. The following are the key sources of estimation uncertainty:

Insurance Contract Technical Provisions

For insurance contracts, estimates are made for both the expected ultimate cost of claims reported at the reporting date and the expected ultimate cost of claims incurred, but not yet reported, at the reporting date (IBNR). It may take a significant period of time before the ultimate claims cost can be established with certainty, and for some type of policies IBNR claims form the majority of the liability reported in the annual accounts.

The ultimate cost of outstanding claims is estimated by using a range of standard actuarial claims projection techniques, such as Chain Ladder and Bornheutter-Ferguson methods. The main assumption underlying these techniques is that past claims development experience can be used to project future claims development and hence ultimate claims costs. As such, these methods extrapolate the development of paid and incurred losses, average costs per claim and claim numbers based on the observed development of earlier years and expected loss ratios. Historical claims development is mainly analysed by underwriting years, but can also be further analysed by geographical area, as well as by significant business lines and claim types. Large claims are usually separately addressed, either by being reserved at the face value of loss adjuster estimates or separately projected in order to reflect their future development. In most cases, no explicit assumptions are made regarding future rates of claims inflation or loss ratios. Instead, the assumptions used are those implicit in the historical claim's development data on which the projections are based.

Additional qualitative judgement is used to assess the extent to which past trends may not apply in future, (e.g. to reflect one-off occurrences, changes in external or market factors such as public attitudes to claiming, economic conditions, levels of claims inflation, judicial decisions and legislation, as well as internal factors such as portfolio mix, policy features and claims handling procedures) in order to arrive at the estimated ultimate cost of claims that present the most likely outcome from the range of possible outcomes, taking account of all the uncertainties involved.

A range of judgements and assumptions are used in assessing salvage and subrogation recoveries.

Similar judgements, estimates and assumptions are employed in the assessment of adequacy of provisions for unearned premium. Judgement is also required in determining whether the earnings methodology on an insurance contract requires amortisation of unearned premium on a basis other than time apportionment.

Estimates of Future Premiums

For certain insurance contracts, premium is initially recognised based on estimates of ultimate premiums. These estimates are judgemental and could result in misstatements of revenue being recorded in the annual accounts.

The main assumption underlying these estimates is that past premium development can be used to project future premium development.

d. Financial Instruments

As permitted by FRS 102, the Syndicate has elected to apply the recognition and measurement provisions of IAS 39 - Financial Instruments (as adopted for use in the EU) to account for all of its financial instruments.

All regular purchases and sales of financial assets are recognised on the trade date i.e. the date the Syndicate commits to purchase or sell the asset. Regular purchases or sales of financial assets require delivery of assets within the time frame generally established by regulation or convention in the marketplace.

Cash and Cash Equivalents

Cash and cash equivalents in the annual accounts comprise cash at banks and in hand and Shares and other variable yield securities with an original maturity date of three months or less. For the purpose of the cash flow statement, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

Fair Value of Financial Assets

The Syndicate uses the following hierarchy for determining the fair value of financial instruments by valuation technique:

- **Level 1:** The unadjusted quoted price in an active market for identical assets or liabilities that the Syndicate can access at the measurement date.
- **Level 2:** Inputs other than quoted prices included within Level 1 that are observable (i.e. developed using market data) for the asset or liability, either directly or indirectly.
- **Level 3:** Inputs are unobservable (i.e. for which market data is unavailable) for the asset or liability. Level 3 assets are valued at historic cost.

A fair value measurement is categorised in its entirety on the basis of the lowest level input that is significant to the fair value measurement.

See note 9 for details of financial instruments classified by fair value hierarchy.

Collateral Arrangements

The Syndicate has cash collateral held in third party trusts, in respect of reinsurance arrangements with unrated counterparties. The rights and obligations are not with the Syndicate, but with the provider of the collateral and as such are not recognised as financial assets. There are no non-cash collateral arrangements in place. The Syndicate is not required to provide collateral for counterparties for which it is acting as the reinsurer.

De-recognition of Financial Assets

A financial asset or, when applicable, a part of a financial asset is de-recognised when:

- The rights to the cash flows from the asset have expired; or

- The Syndicate retains the right to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass through' arrangement and either (a) the Syndicate has transferred substantially all the risks and rewards of the asset; or (b) the Syndicate has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Syndicate has transferred its right to receive cash flows from an asset or has entered into a pass-through arrangement and has neither transferred nor retained substantially all the risks and rewards nor transferred control of the asset, the asset is recognised to the extent of the Syndicate's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Syndicate could be required to repay. In that case, the Syndicate also recognises an associated liability.

Offsetting of Financial Instruments

Financial assets and financial liabilities are offset, and the net amount is reported in the statement of financial position if, and only if:

- There is a currently enforceable legal right to offset the recognised amounts; and
- There is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

Financial Liabilities

The Syndicate's financial liabilities include trade and other payables, borrowings and insurance payables.

All financial liabilities are recognised initially net of directly attributable transaction costs.

Trade and other payables and loans and borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the income statement when the liabilities are de-recognised as well as through the effective interest rate (EIR) method amortisation process.

Amortised cost is calculated by considering any discount or premium on acquisition and fee or costs that are an integral part of the EIR. The EIR amortisation is included in finance cost in profit or loss.

A financial liability is de-recognised when the obligation under the liability is discharged or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of the existing liability are substantially modified, such an exchange or modification is treated as a de-recognition of the original liability and the recognition of a new liability, and the difference in the respective amounts is recognised in profit or loss.

e. Investment Return

Investment return comprises of interest income.

Interest income is recognised on an accruals basis based on the effective interest rate.

The actual investment return on investments supporting the technical provisions is made from the non-technical account to the technical account. Investment return related to non-insurance business is attributed to the non-technical account.

f. Insurance Contracts

Product Classification

Insurance contracts are those contracts when the Syndicate (the insurer) has accepted significant insurance risk from another party (the insured) by agreeing to compensate the insured if a specified uncertain future event (the insured event) adversely affects the insured. As a general guideline, the agency determines whether it has significant insurance risk, by comparing benefits paid with benefits payable if the insured event did not occur. Insurance contracts can also transfer financial risk.

Once a contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly during this period, unless all rights and obligations are extinguished or expire.

Gross Premiums

Gross written premiums comprise the total premiums receivable for the whole period of cover provided by the contracts entered into during the reporting period, regardless of whether these are wholly due for payment in the reporting period, together with any adjustments to such premiums receivable arising in the reporting period in respect of business written in prior reporting periods. They are recognised on the date on which the policy commences. Additional or return premiums are treated as a re-measurement of the initial premium. Gross written premiums are stated gross of commission.

Gross written premiums include an estimate for pipeline premiums (i.e. premiums due but net yet received or notified to the Syndicate by intermediaries) relating only to those underlying contracts of insurance where the period of cover has commenced prior to the reporting date. The most significant assumption in this estimate is that current year experience will be consistent with prior year experience.

Under some policies, gross written premiums are adjusted retrospectively in the light of claims experience or where the risk covered cannot be assessed accurately at the commencement of cover. Where written premiums are subject to an increase retrospectively, recognition of any potential increase is deferred until the additional amount can be ascertained with reasonable certainty. Where written premiums are subject to a reduction, a re-measurement taking account of such a reduction is made as soon as there is an obligation to the insured.

Written premiums are recognised as earned over the period of the policy on a time apportionment basis having regard where appropriate, to the incidence of risk. The provision for unearned premiums is predominantly calculated on a monthly pro rata basis with some classes of business such as Energy and Space having more complex earnings profiles. The proportion attributable to subsequent periods is deferred as a provision for unearned premiums.

Reinsurance Premiums

Reinsurance premiums written comprise the total premiums payable for the whole cover provided by contracts entered into the period, including portfolio premiums payable, and are recognised on the date on which the policy incepts. Premiums include any adjustments arising in the accounting period in respect of reinsurance contracts incepting in prior accounting periods.

Under some policies, reinsurance premium payable is adjusted retrospectively in the light of claims experience or where the risk covered cannot be assessed accurately at the commencement of cover. Where written premiums are subject to an increase retrospectively, recognition of any potential increase is recognised as soon as there is an obligation to the insured.

Reinsurance premiums under a Risks Attaching During (“RAD”) contract are earned typically over two years based on inception and expiry dates. Year of Account allocation is based on the inception and expiry dates that the contract relates to. This results in a triangular earnings pattern, where earnings increase towards the middle of the policy period then decrease until the policy expires.

Reinsurance premiums under a Losses Occurring During (“LOD”) contract are earned on a straight-line basis over the period of the reinsurance contract, based on inception and expiry dates. Losses that occur during the length of the contract could relate to the current, prior or following year of account, therefore an allocation to Year of Account is applied to this type of policy. The allocation is based on historical class level monthly earnings for the underlying gross policies.

Fees and Commission Income

Insureds are charged for policy administration services, investment management services, policy surrenders and other contract fees. These fees are recognised as revenue over the period in which the related services are performed. If the fees are for services to be provided in future periods, then they are deferred and recognised over those future periods.

Claims

Claims include all claims occurring during the year, whether reported or not, related internal and external claims handling costs that are directly related to the processing and settlement of claims, a reduction for the value of salvage and other recoveries, and any adjustments to claims outstanding from previous years.

Reinsurance claims are recognised when the related gross insurance claim is recognised according to the terms of the relevant contract.

Technical Provisions

Technical provisions comprise claims outstanding, provisions for unearned premiums and provisions for unexpired risks.

Claims Outstanding

The outstanding claims provision is based on the estimated ultimate cost of all claims incurred but not settled at the reporting date, whether reported or not, together with related claims handling costs and reduction for the expected value of salvage and other recoveries. Delays can be experienced in the notification and settlement of certain types of claims and therefore, the ultimate cost of these claims cannot be known with certainty at the reporting date. The liability is calculated at the reporting date using a range of standard actuarial claim projection techniques, based on empirical data and current assumptions that may include a margin for adverse deviation. The liability is not discounted for the time value of money.

These methods generally involve projecting from past experience of the development of claims over time to form a view of the likely ultimate claims to be experienced for more recent underwriting, having regard to variations in the business accepted and the underlying terms and conditions. For the most recent years, where a high degree of volatility arises from projections, estimates may be based in part on output from rating and other models of the business accepted and assessments of underwriting conditions.

Technical Provisions

The reinsurers' share of provisions for claims is based on the amounts of outstanding claims and projections for IBNR, net of estimated irrecoverable amounts, having regard to the reinsurance programme in place for the class of business, the claims experience for the year and the current security rating of the reinsurers involved. A number of statistical methods are used to assist in making these estimates.

The two most critical assumptions as regards claims provisions are that the past is a reasonable predictor of the likely level of claims development and that the rating and other models used for current business are fair reflections of the likely level of ultimate claims to be incurred.

The Directors consider that the provisions for gross claims and related reinsurance recoveries are fairly stated on the basis of the information currently available to them. However, the ultimate liability will vary as a result of subsequent information and events and this may result in significant adjustments to the amounts provided. Adjustments to the amounts of claims provisions established in prior years are reflected in the Annual Accounts for the period in which the adjustments are made. The methods used, and the estimates made, are reviewed regularly.

Provisions for Unearned Premiums

Unearned premiums are those proportions of premiums written in a year that relate to periods of risk after the reporting date. Written premiums are recognised as earned over the period of the policy on a time apportionment basis having regard where appropriate, to the incidence of risk. The provision for unearned premiums is calculated on a monthly pro rata basis. The proportion attributable to subsequent periods is deferred as a provision for unearned premiums.

Unearned reinsurance premiums are those proportions of reinsurance premiums in a year that relate to periods of risk after the reporting date. Unearned reinsurance premiums are deferred over the term of the underlying direct insurance policies for risks-attaching contracts and over the term of the reinsurance contract for losses-occurring contracts.

Unexpired Risks

A liability adequacy provision (the unexpired risks provision) is made where the cost of claims and expenses arising after the end of the financial year from contracts concluded before that date, is expected to exceed the provision for unearned premiums, net of deferred acquisition costs, and premiums receivable.

The assessment of whether a provision is necessary is made by considering separately each category of business on the basis of information available at the reporting date, after offsetting surpluses and deficits arising on products which are managed together. Investment income is taken into account in calculating the provision.

At 31 December 2020 we included unexpired risk provision of £2m (2019 is Nil).

Deferred Acquisition Costs

Acquisition costs comprise costs arising from the conclusion of insurance contracts. They include both direct costs, such as intermediary commissions or the cost of drawing up the insurance document or including the insurance contract in the portfolio, and indirect costs, such as the advertising costs or the administrative expenses connected with the processing of proposals and the issuing of policies.

Deferred acquisition costs are costs arising from conclusion of insurance contracts that are incurred during the reporting period, but which relate to a subsequent reporting period and which are carried forward to subsequent reporting periods.

Deferred acquisition costs are amortised over the period in which the related premiums are earned.

Reinsurance Assets

The Syndicate cedes insurance risk in the normal course of business for all of its lines of business. Reinsurance assets represent balances due from reinsurance companies and other Lloyd’s syndicates. Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision or settled claims associated with the reinsurer’s policies and in accordance with the related reinsurance contract.

Reinsurance assets are reviewed for impairment at each reporting date, or more frequently should an indication of impairment arise during the reporting year. Impairment occurs when there is objective evidence as a result of an event that occurred after initial recognition of the reinsurance asset that the Syndicate may not receive all outstanding amounts due under the terms of the contract and the event has a reliably measurable impact on the amounts that the Syndicate will receive from the reinsurer. The impairment loss is recorded in the Income Statement.

Ceded reinsurance arrangements do not relieve the Syndicate from its insurance obligations to its policyholders.

Insurance Receivables

Insurance receivables are recognised when due and measured on initial recognition at the fair value of the consideration received or receivable. Subsequent to initial recognition, they are measured at amortised cost, using the effective interest rate method. The carrying value of insurance receivables is reviewed for impairment should events or circumstances indicate that the carrying amount may not be recoverable, with the impairment loss recorded in the Income Statement.

Insurance receivables are de-recognised when the de-recognition criteria for financial assets have been met.

Insurance Payables

Insurance payables are recognised when due and measured on initial recognition at the fair value of the consideration received less directly attributable transaction costs. Subsequent to initial recognition, they are measured at amortised cost using the effective interest rate method. Insurance payables are derecognised when the obligation under the liability is settled, cancelled or expired.

g. Provisions

Provisions are recognised when the Syndicate has a present obligation as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

h. Foreign Currencies

The Syndicate's functional currency and presentational currency is Sterling.

Transactions in US dollars, Canadian dollars, Euros, Australian dollars and Japanese Yen are initially recorded in the functional currency at the average rates of exchange for the period where for practical purposes it is not possible to use the actual rate at the date of transaction. Transactions denominated in other foreign currencies are included at the rate of exchange ruling at the date the transaction is processed.

Monetary assets and liabilities (which include unearned premiums and deferred acquisition costs) denominated in foreign currencies are translated at the rate of exchange at the statement of financial position date. Non-monetary items denominated in a foreign currency, measured at fair value are translated into the functional currency using the exchange rate ruling at the date when the fair value was determined.

Exchange differences arising on the re-translation of opening statement of financial position items at the closing statement of financial position rate and the retranslation of the Income Statement for the year from the average rate to the closing statement of financial position rate are recorded in the non-technical account.

i. Taxation

Under Schedule 19 of the Finance Act 1993 managing agents at Lloyd's are not required to deduct basic-rate income tax from trading income. In addition, all UK basic-rate income tax deducted from syndicate investment income is recoverable by the Agency and consequently the distribution made to members or their members' agents is gross of tax. Capital appreciation falls within trading income and is also distributed gross of tax.

No provision has been made for any United States Federal Income Tax payable on underwriting results or investment earnings. Any payments on account made by the Syndicate are included in the statement of financial position under the heading "other debtors".

No provision has been made for any overseas tax payable by members of the Syndicate on underwriting results.

j. Pension Costs

The Arch Group of companies, of which the Agency is a member, operates a defined contribution pension scheme. Pension contributions relating to agency staff are charged to the Syndicate and included within net operating expenses.

k. Profit Commission

Profit commission is payable to the Agency at a rate of 17.5% on the Whole Account 1955 quota share and 10% on the Syndicate's other five classes of business. With the exception of the 1955 quota share business, profit commission is only calculated when the Syndicate's profit is 4% or more of capital. This is charged to the Syndicate as incurred but does not become payable until after the appropriate Year of Account closes, normally at 36 months.

2. Segmental Analysis

Analysis by Class of Business

An analysis of the underwriting result before investment is set out below:

2020	Gross premiums written £'000	Gross premiums earned £'000	Gross claims incurred £'000	Gross operating expenses £'000	Reinsurance balance £'000	Total £'000	Net technical provisions £'000
Direct insurance:							
Aviation	13,116	10,161	(9,532)	(2,575)	(2,339)	(4,285)	(6,418)
Energy-Marine	438	1,443	(1,072)	(309)	(331)	(269)	(909)
Energy Non-Marine	498	4,402	(3,521)	(999)	(1,093)	(1,211)	(2,998)
Fire and Other damage to Property	35,346	28,347	(26,391)	(7,168)	(6,576)	(11,788)	(18,041)
Third party liability	18,136	15,607	(14,349)	(3,897)	(3,613)	(6,252)	(9,911)
Total Direct	67,534	59,960	(54,865)	(14,948)	(13,952)	(23,805)	(38,277)
Reinsurance	11,424	16,257	7,008	(16,572)	(34,834)	(28,141)	(95,564)
	78,958	76,217	(47,857)	(31,520)	(48,786)	(51,946)	(133,841)

2019	Gross premiums written £'000	Gross premiums earned £'000	Gross claims incurred £'000	Gross operating expenses £'000	Reinsurance balance £'000	Total £'000	Net technical provisions £'000
Direct insurance:							
Aviation	7,279	5,753	(5,339)	(1,394)	667	(313)	(12,326)
Energy-Marine	2,341	1,390	(1,315)	(367)	169	(123)	(3,126)
Energy Non-Marine	7,709	6,573	(6,074)	(1,561)	754	(308)	(13,928)
Fire and Other damage to Property	14,444	11,795	(11,063)	(2,851)	1,475	(644)	(27,255)
Third party liability	7,631	6,361	(5,886)	(1,519)	732	(312)	(13,523)
Total Direct	39,404	31,872	(29,677)	(7,692)	3,797	(1,700)	(70,158)
Reinsurance	67,126	72,427	(60,876)	(17,465)	3,773	(2,141)	(69,712)
	106,530	104,299	(90,553)	(25,157)	7,570	(3,841)	(139,870)

The reinsurance balance is the aggregate total of reinsurance outwards balances included in the technical account.

All premium were written in the UK.

Analysis by Geographical Location

The geographical analysis of premiums by destination (or location of risk) is as follows:

	2020	2019
	£000	£000
UK	657	1,215
EU member states	1,894	6,035
US	65,207	42,982
Other	11,200	56,298
Gross premiums written	78,958	106,530

Part VII Transfer

On 30 December 2020, the Members of the Syndicate, as comprised for each of the relevant years of account between April 2016 and April 2019, transferred all EEA non-life insurance policies written between 2016 and 2020 (and related liabilities) underwritten by them for those years of account to Lloyd's Insurance Company S.A. ('Lloyd's Brussels'), in accordance with Part VII of the Financial Services and Markets Act 2000. On the same date, the Members of the Syndicate entered into a 100% Quota Share Reinsurance Agreement whereby Lloyd's Brussels reinsured all risks on the same policies back to the relevant open years of account of the Syndicate which wrote the transferring policies and/or inherited liabilities on transferring policies through Reinsurance to Close of earlier years of account.

Following the sanction of the scheme by the High Court on 18 November 2020, the scheme took effect on 30 December 2020 and the Members of the Syndicate transferred the impacted EEA policies and related liabilities to Lloyd's Brussels, together with cash of £0.15m. On the same date, under the Reinsurance Agreement, Lloyd's Brussels reinsured the same risks back, together with an equal amount of cash of £0.15m and non-cash assets relating to the transferred liabilities. The combined effect of the two transactions had no economic impact for the Syndicate, and accordingly there is no impact on the Syndicate's profit and loss account and no net impact on the balance sheet.

Current year underwriting results for the transferred policies have been reported in the same classes of business as in prior years, as the effective date of the transfer was 30 December 2020, and in line with Society of Lloyd's guidance no movements were processed on these policies on 31 December 2020. In future years, results relating to these risks will be reported under the Inwards Reinsurance class of business, reflecting the new contractual arrangement with Lloyd's Brussels.

3. Investment Return

All of the Syndicate's investments are recognised at fair value through the profit and loss.

	2020	2019
Investment income	£000	£000
Income from investments, cash, and other deposits	846	1,324
Gains on realisation of investments	123	128
Total Investment Income	969	1,452
Unrealised gains on investments at fair value through profit or loss	49	206
Investment management expenses, including interest	(34)	(20)
Net investment income	984	1,638

4. Net Operating Expenses

	2020	2019
	£000	£000
Acquisition costs	26,898	19,245
Change in deferred acquisition costs (Note 13)	(1,768)	287
Administrative expenses	6,390	5,625
	31,520	25,157

Administrative expenses include:

	2020	2019
	£000	£000
Members' standard personal expenses (Lloyd's subscriptions, New Central Fund contributions, Managing Agent's fees and profit commission)	3,425	2,549

The gain on the translation of monetary assets and liabilities at the reporting date of 31 December 2020 was £1.08m (2019: £0.4m loss). Included in administrative expenses are staff costs of £3.5m (2019: £3.4m), which is analysed in note 6.

5. Auditor's Remuneration

	2020	2019
	£000	£000
Audit of the Syndicate Annual Accounts	101	72
Audit related services	48	42
	149	114

The above represents the Syndicate's share of the total audit fee.

Auditors' remuneration is included as part of the administrative expenses in note 4 to the annual accounts.

6. Staff Costs and Directors' Remuneration

a. Staff Costs

All staff in the Barbican Group are employed by Arch Europe Insurance Services Limited ("AEIS"), an Arch group Company. The following amounts were recharged to the Syndicate in respect of salary costs:

	2020	2019
	£000	£000
Wages and salaries	3,061	2,989
Social security costs	291	334
Other pension costs	147	115
	3,499	3,438

The average number of employees employed by Arch, but working for the Syndicate during the year was as follows:

	2020	2019
	No.	No.
Administration and Finance	10	13
Underwriting	8	7
	18	20

b. Directors' Remuneration

The eight executive Directors of the Agency, three of whom served throughout the year, received no remuneration in the year charged to the Syndicate.

The Active Underwriter received the following remuneration:

	2020	2019
	£000	£000
Aggregate remuneration in respect of qualifying services	645	645

No advances or credits granted by the Agency to any of its directors subsisted during the year. This includes non-cash benefits.

7. Calendar Year Investment Yield

The average amount of Syndicate funds available for investment during 2019 and the investment return and yield for that calendar year were as follows:

	2020	2019
	£000	£000
Average Syndicate funds available		
Sterling	7,997	13,599
Euro	4,462	8,265
United States dollars	44,297	42,841
Canadian dollars	4,578	2,384
Australian dollars	2,432	4,737
Japanese Yen	3,231	5,885
	66,997	77,711

	2020	2019
Investment return for the year	£000	£000
Sterling	109	116
Euro	(34)	(2)
United States dollars	850	(20)
Canadian dollars	33	1,434
Australian dollars	26	40
Japanese Yen	-	70
	984	1,638

	2020	2019
Analysis of calendar year investment yield by fund	%	%
Sterling	1.37	0.85
Euro	(0.76)	-
United States dollars	1.92	-
Canadian dollars	0.73	3.35
Australian dollars	1.06	1.68
Japanese Yen	-	1.48

The Syndicate's funds are held in trust fund and short-term deposit accounts and at the 2020-year end were £51.9m (2019: £79.4m), a decrease of 34.6%.

Investment yield decreased overall in 2020 to 1.47% (2019: 2.11%). The 2020 investment return of £1.0m is above prior year (2019: £1.6m) due to decrease of funds and short-term deposits.

8. Financial Investments

	Carrying Value 2020 £000	Carrying Value 2019 £000	Purchase Price 2020 £000	Purchase price 2019 £000
Shares and other variable yield securities	16,395	14,331	16,395	14,331
Debt Securities and other fixed income securities	29,835	48,435	27,615	47,155
	46,230	62,766	44,010	61,486

All "Shares and other variable yield securities" are designated at fair value through profit or loss. These comprise 35.4% (2019: 23%) of the total market value of the Syndicate's financial investments.

The following table shows financial instruments recorded at fair value analysed between the three levels in the fair value hierarchy.

31 December 2020	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Shares and other variable yield securities	14,829	-	1,566	16,395
Debt Securities and other fixed income securities	8,652	21,183	-	29,835
Other deposits	-	2,512	-	2,512
	23,481	23,695	1,566	48,742

31 December 2019	Level 1	Level 2	Level 3	Total
	£000	£000	£000	£000
Shares and other variable yield securities	13,986	-	345	14,331
Debt Securities and other fixed income securities	14,046	34,389		48,435
Other deposits	-	1,413	-	1,413
	28,032	35,802	345	64,179

Included in the level 1 category are financial assets that are measured by reference to published quotes in an active market. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Included in the level 2 category are other deposits which consist of overseas deposits presented separately in other assets in the statement of financial position. These are financial assets measured using valuation technique based on assumptions that are supported from observable current market transactions.

Included in the Level 3 category are the financial assets for which market data is unavailable. These relate to loans made to Lloyd's Central Fund which have been valued at cost since the assessed fair value is not materially different.

9. Financial Instruments

A breakdown of how the Syndicate's financial instruments are measured is given below:

	2020	2019
	£000	£000
Financial assets at fair value through profit and loss		
Shares and other variable yield securities	16,395	14,331
Debt securities and other fixed income securities	29,835	48,435
Other Deposits	2,512	1,413
Financial assets that are debt instruments measured at amortised cost		
Debtors arising out of direct insurance operations	20,840	16,445
Debtors arising out of reinsurance operations	23,225	37,111
Cash at bank and in hand	5,700	16,638
Financial liabilities measured at amortised cost		
Creditors arising out of reinsurance operations	24,318	20,524

10. Provisions for Unearned Premiums

2020	Gross	Reinsurer's share	Net
	£000	£000	£000
At 1 January 2020	46,268	(15,778)	30,490
Premiums written in the year	78,958	(38,332)	40,626
Premiums earned in the year	(76,217)	42,102	(34,115)

Foreign Exchange	(3,507)	323	(3,184)
At 31 December 2020	45,502	(11,685)	33,817

2019	Gross	Reinsurer's share	Net
	£000	£000	£000
At 1 January 2019	45,667	(13,221)	32,446
Premiums written in the year	106,530	(37,399)	69,131
Premiums earned in the year	(104,299)	34,246	(70,053)
Foreign Exchange	(1,630)	596	(1,034)
At 31 December 2019	46,268	(15,778)	30,490

11. Claims Outstanding

2020	Gross	Reinsurer's share	Net
	£000	£000	£000
At 1 January 2020	184,673	(75,293)	109,380
Claims incurred in current accident year	47,857	6,684	54,541
Claims paid during the year	(86,655)	24,054	(62,601)
Unexpired risk provision	(2,000)	-	(2,000)
Foreign Exchange	350	354	704
At 31 December 2020	144,225	(44,201)	100,024

2019	Gross	Reinsurer's share	Net
	£000	£000	£000
At 1 January 2019	185,769	(74,386)	111,383
Claims incurred in current accident year	90,553	(41,816)	48,737
Claims paid during the year	(85,042)	38,085	(46,957)
Foreign Exchange	(6,607)	2,824	(3,783)
At 31 December 2019	184,673	(75,293)	109,380

An unexpired risk reserve has been included for Property Insurance and Space classes of business amounting to £2m due to insufficient unearned premiums available to cover the future losses from these classes.

12. Cash at bank and in hand

This balance comprises the cash and cash equivalents presented in the Statement of Cash Flows.

	2020	2019
	£000	£000

Cash at bank and in hand	5,700	16,638
	5,700	16,638

13. Deferred Acquisition Costs

	2020	2019
	£000	£000
At 1 January	9,098	9,846
Change in deferred acquisition costs	1,768	(287)
Foreign Exchange	171	(461)
At 31 December	11,037	9,098

14. Debtors arising out of reinsurance operations

	2020	2019
	£000	£000
1955 Quota share reinsurance debtor	2,134	8,929
Due from intermediaries	21,091	28,182
	23,225	37,111

15. Other Creditors

Within 1 year	Note	2020	2019
		£000	£000
Amounts due to Arch Group Companies	20	1,793	1,482
		1,793	1,482

16. Debtors arising out of direct insurance operations – Intermediaries

	2020	2019
	£000	£000
Gross premium due	20,840	16,445
	20,840	16,445

17. Creditors arising out of reinsurance operations

	2020	2019
	£000	£000
Reinsurance Premium Due	24,318	16,445
	24,318	16,445

18. Other Debtors

	Note	2020	2019
		£000	£000
VAT Control Account		21	36
Refund due from Lloyd's		82	475
Inter Company with Arcus 1856 Limited	20	177	115
		280	626

19. Risk Management

a. Governance Framework

The primary objective of the Agency's risk and financial management framework is to protect the members from events that hinder the sustainable achievement of financial performance objectives, including failing to exploit opportunities. Management recognises the critical importance of having efficient and effective risk management systems in place.

The Agency has established a risk management framework and has adopted the terms of reference of the Arch Group's Risk Management function and approves the annual plans of that function to support its risk management framework. The risk management framework is supplemented with a clear organisational structure with documented delegated authorities and responsibilities from the Agency Board to the Managing Director and executive management committees. Lastly, a policy framework which sets out the risk profiles for the Syndicate, risk management, control and business conduct standards for the Syndicate's operations has been put in place.

The Agency Board approves risk management policies and meets regularly to approve any commercial, regulatory and organisational requirements of such policies relevant to the Syndicate and their implementation. These policies define the identification of risk and its interpretation to ensure the appropriate quality and diversification of assets, align underwriting and reinsurance strategy to the corporate goals, and specify reporting requirements. Significant emphasis is placed on the assessment and documentation of risks and controls, including the articulation of risk appetite.

b. Capital Management Objectives, Policies and Approach

In line with the Lloyd's capital framework, Lloyd's capital setting process and provision of capital by members, the Agency has established the following capital management objectives, policies and approach to managing the risks that affect the Syndicate's capital position:

- To maintain the required level of stability of the Syndicate thereby providing a degree of security to insureds;
- To allocate capital efficiently and support the development of business by ensuring that returns on capital employed meet the requirements of its capital providers and of its members;
- To retain financial flexibility by maintaining strong liquidity and access to a range of capital markets;
- To align the profile of assets and liabilities taking account of risks inherent in the business, and
- To maintain financial strength to support new business growth and to satisfy the requirements of the insureds, regulators and stakeholders.

The operations of the Agency, which manages the underwriting of the Syndicate, are subject to regulatory requirements within the jurisdictions in which it operates, in particular compliance with Financial Conduct Authority ("FCA") rules, Prudential Regulation Authority ("PRA") rules, the Society of Lloyd's standards and by-laws, and relevant EU regulations and European Insurance and Occupational Pensions Authority ("EIOPA") guidelines. Such regulations not only prescribe approval and monitoring of activities, but also impose certain restrictive provisions (e.g., capital adequacy) to minimise the risk of default and insolvency on the part of insurers to meet unforeseen liabilities as they arise.

The Syndicate has met all of these requirements throughout the financial year.

In reporting financial strength, capital and solvency are principally measured using the rules prescribed by the PRA as applicable to the Society of Lloyd's and Lloyd's managing agents. These regulatory capital tests are based upon required levels of solvency, capital and a series of prudent assumptions in respect of the type of business written.

The Agency's capital management policy is to hold sufficient capital to cover the statutory requirements based on the requirements of the PRA and Lloyd's, including any additional amounts required by the regulators.

c. Approach to Capital Management

The Agency seeks to optimise the structure and sources of capital to ensure that it consistently maximises capital resources.

The Agency's approach to managing Syndicate capital involves managing assets, liabilities and risks in a coordinated way, assessing shortfalls between reported and required capital levels on a regular basis and taking appropriate actions to manage the capital position of the Syndicate in the light of changes in economic conditions and risk characteristics. An important aspect of the Syndicate's overall capital management process is the setting of target risk adjusted rates of return, which are aligned to performance objectives and ensure that the Syndicate is focused on the creation of value for members.

The primary sources of capital used by the Syndicate are members' balances and bank letters of credit.

The capital requirements are routinely forecast on a periodic basis and assessed against both the forecast available capital and the expected internal rate of return, including risk and sensitivity analyses. The process is ultimately subject to approval by the Agency Board.

The Agency has developed a Lloyd's Internal Model ("LIM") framework on behalf of the Syndicate to identify risks and quantify their impact on economic capital. The LIM estimates how much capital is required to reduce the risk of insolvency to a remote degree of probability under Solvency II requirements. The LIM has also been considered in assessing the capital requirement.

The Syndicate has had no significant changes in its policies and processes to its capital structure during the past year.

d. Capital Resources Requirement

The Syndicate is subject to capital requirements imposed by Lloyd's. Throughout the year the Syndicate has complied with the Lloyd's risk-based LIM methodology under Solvency II, which is used to calculate the Syndicate's capital requirement. Lloyd's capital setting use a capital requirement set at syndicate level as a starting point. The requirement to meet Solvency II & Lloyd's capital requirements apply at overall member level respectively, not at syndicate level. Accordingly, the capital requirement of Syndicate 1856 is not disclosed in these annual accounts.

e. Solvency II Capital Requirements

Under the Solvency II regime, there are two prescribed methods for assessing an insurer's regulatory capital requirements – using either a standard formula set by the regulator or an Internal Model specific to that insurer which is subject to regulatory approval.

The Syndicate operates within the Lloyd's market. The PRA has determined that the Society of Lloyd's is the relevant insurer for the Lloyd's market. The Society of Lloyd's has chosen to operate an Internal Model, and this was approved by the PRA in December 2015. The Society of Lloyd's require all managing agents to operate an internal model for each managed syndicate that is structured on Solvency II lines and which (when aggregated) ensures the integrity and effectiveness of the Society of Lloyd's Internal Model. The Solvency II regime became effective on 1 January 2016.

The Society of Lloyd's not only oversees the approval and monitoring of each syndicate's internal model, but also imposes certain restrictive provisions to minimise the risk of non-compliance with regulatory capital requirements.

The effective management of risk and capital is a key strategic priority. The Agency's risk management framework enhances the definition of the risk standards and risk tolerances which guide the day-to-day business decision making and processes and aim to ensure that the risk appetite is not exceeded.

Economic capital is calculated for the Syndicate considering the complete spectrum of risks identified by the risk framework, ensuring that the capital requirement reflects the risk profile and enabling capital to be allocated and returns measured on a risk adjusted basis.

The Solvency II Directive has been transposed into UK legislation through PRA rules and guidance. In addition, Solvency II firms are obligated to comply with relevant EU regulations and EIOPA guidelines. The PRA authorises and regulates both the Society of Lloyd's and Lloyd's managing agents, including the Agency. In addition, the Society of Lloyd's supervises certain activities performed by Lloyd's managing agents.

The Syndicate submitted its Quarterly Solvency Return (QSR) for 31 December 2020 to Lloyd's on 21 January 2021 and will submit its Annual Solvency Return (ASR) for 31 December 2020 to Lloyd's on 11 March 2021.

f. Insurance Risk

Insurance risk refers to fluctuations in the timing, frequency and severity of insured events, relative to the expectations of the Syndicate at the time of underwriting.

Some specific examples of insurance risk include variations in the severity or frequency of claims or the unexpected occurrence of multiple claims arising from a single cause. More generally, insurance risk includes the potential for claims overruns relative to pricing or reserving assumptions.

Insurance risk is a concern in a prudential context because inadequate systems and controls for its management can create a threat to the PRA's regulatory objectives of maintaining market confidence and consumer protection. Inadequately managed insurance risk may result in:

1. The inability of a syndicate to meet its contractual insurance liabilities as they fall due; and
2. The inability of a syndicate to treat its insureds fairly and consistently with the Syndicate's obligations.

The Syndicate's underwriting strategy is to write a book of business with a focus on building a composite portfolio with a high level of diversification, thus creating a business with low volatility and a good opportunity for consistent profit across the underwriting cycle. The Syndicate's appetite is governed by market conditions and management undertakes a continuous assessment of its portfolio against this background.

Tolerance - Risk Appetite

The Syndicate's tolerance by class of business is covered within the business plan. The Syndicate operated within defined exception criteria as follows:

1. Stamp capacity was £109.2m for the 2020 year of account (2019 year of account: £104.9m):
2. Maximum realistic disaster scenario net exposure for the 2020 year of account of 38% (2019 year of account: 69%) of stamp capacity; and
3. Maximum gross line size for 2020 of £39.0m (2019: £15.0m).

Claims

Open market claims are settled by the claim's management team. The claims department operates to approved claims handling guidelines which reflect Lloyd's minimum standards.

Claims development tables shown on an underwriting year basis and are set out below and the key assumptions underlying liability estimates are set out in the Key Assumptions section.

Gross insurance ultimate contract outstanding claims provisions as at 31 December 2020:

Gross Ultimate Claims Development Year	1	2	3	4	5	6	Total
	£000	£000	£000	£000	£000	£000	£000
Year of Account							
2016	57,083	59,022	95,617	95,099	45,248		45,248
2017	88,598	91,992	92,909	77,603			77,603
2018	93,703	99,934	102,578				102,578
2019	86,095	88,776					88,776
2020	100,281						100,281
Current estimate of ultimate claims							414,486
Cumulative payments							(241,071)
Gross unearned claims reserve							(31,190)
Gross claims reserve							142,225

Net insurance ultimate contract outstanding claims provisions as at 31 December 2020:

Net Ultimate Claims Development Year	1	2	3	4	5	6	Total
	£000	£000	£000	£000	£000	£000	£000
Year of Account							
2016	39,711	41,687	67,546	68,533	34,271		34,271
2017	55,797	55,827	56,470	43,238			43,238
2018	48,119	48,943	52,067				52,067
2019	48,059	55,973					55,973
2020	89,049						89,049
Current estimate of ultimate claims							274,599
Cumulative payments							(151,149)

Gross unearned claims reserve	(25,425)
Gross net claims reserve	98,024

The claim liabilities are sensitive to the key assumptions that follow. It has not been possible to quantify the sensitivity of certain assumptions such as legislative changes or uncertainty in the estimation process.

The following analysis is performed for reasonably possible movements in key assumptions with all other assumptions held constant, showing the impact on gross and net liabilities, profit before tax and members' balances.

31 December 2020	**Change in assumptions**	**Impact on gross liabilities £000**	**Impact on net liabilities £000**	**Impact on profit and members' balances £000**
Average claim cost	+10%	13,778	8,182	(8,182)
Average number of claims	+10%	14,070	9,576	(9,576)

31 December 2019	**Change in assumptions**	**Impact on gross liabilities** £000	**Impact on net liabilities** £000	**Impact on profit and members' balances** £000
Average claim cost	+10%	17,952	6,583	(6,583)
Average number of claims	+10%	18,275	9,065	(9,065)

The syndicate has material exposure to Hurricanes Laura and Sally and the Derecho Windstorm in Iowa on the 2020 year of account. In addition, there is some exposure to Hurricanes Hanna, Isaias, Zeta and Delta, wildfires in California, Washington and Oregon and the Alberta hailstorms. This increases the uncertainty of the Syndicate's total reserves, but not beyond the normal range of uncertainty for insurance liabilities at this stage of development. By performing a sensitivity analysis to the 2020 Catastrophe losses, the Syndicate determined that a 10% increase on the gross reserves amount of £20.8m will have a smaller impact on the net reserves due to the Property Aggregate reinsurance programme covering the affected classes of business.

The syndicate also has material exposure to Covid losses on 2019 and 2020 representing £10.8m of gross reserves on the Property Treaty account. Given the unprecedented nature of the pandemic, there is significant uncertainty around this estimate. A 10% increase in this gross reserve would lead to a £1.0m net reserve increase.

The Agency uses both its own and commercially available proprietary risk management software to assess Syndicate catastrophe exposure. However, there is always a risk that the assumptions and techniques used in these models are unreliable or that claims arising from an un-modelled event are greater than those arising from a modelled event.

The following table shows hypothetical claims arising for the largest realistic disaster scenarios based on the Syndicate's average risk exposures during 2020.

	Estimated gross loss $m	Estimated net loss $m
US earthquake	143	32
US windstorm	234	57
Japan earthquake	65	30
Japan windstorm	37	30
Europe windstorm	39	30
	518	179

The following table shows hypothetical claims arising for the largest realistic disaster scenarios based on the Syndicate's average risk exposures during 2019.

	Estimated gross loss $m	Estimated net loss $m
US earthquake	135	32
US windstorm	220	95
Japan earthquake	73	8
Japan windstorm	30	18
Europe windstorm	44	20
	502	173

There are agreed documented outwards reinsurance procedures in place covering the purchase of reinsurance and the recovery process. There is also a policy for the approval of reinsurers to minimise credit risk.

The Agency assesses the Syndicate's need for reinsurance on a continuous basis. The structure of the reinsurance programme is part of the annual planning process and broad estimates of reinsurance spend are made. The programme is subject to extension or modification as the year progresses. Procedures for purchasing approval and transactions processing are set out in a procedure's manual.

The table below sets out the concentration of outstanding claim liabilities by business segment:

31 December 2020	Gross liabilities	Reinsurance assets	Net liabilities
	£000	£000	£000
Aviation	(23,958)	7,342	(16,615)
Energy marine	(800)	245	(555)
Energy non-marine	(909)	279	(631)
Fire and other damage to property	(64,564)	19,787	(44,777)
Third party liability	(33,128)	10,153	(22,975)
Reinsurance	(20,866)	6,395	(14,471)
Total	**(144,225)**	**44,201**	**(100,024)**

31 December 2019	Gross liabilities	Reinsurance assets	Net liabilities
	£000	£000	£000
Aviation	(16,274)	6,635	(9,639)
Energy marine	(4,127)	1,683	(2,444)

Energy non-marine	(18,390)	7,498	(10,892)
Fire and other damage to property	(35,985)	14,672	(21,313)
Third party liability	(17,855)	7,279	(10,576)
Reinsurance	(92,042)	37,526	(54,516)
Total	**(184,673)**	**75,293**	**(109,380)**

The geographical concentration of the outstanding claim liabilities is noted below. The disclosure is based on the countries where the risk is located. The analysis would not be materially different if based on the countries in which the counterparties are situated.

31 December 2020	Gross liabilities £000	Reinsurance assets £000	Net liabilities £000
United Kingdom	(1,199)	368	(831)
EEA	(3,460)	1,061	(2,399)
USA	(119,108)	36,502	(82,606)
International	(20,458)	6,270	(14,188)
Total	**(144,225)**	**44,201**	**(100,024)**

31 December 2019	Gross liabilities £000	Reinsurance assets £000	Net liabilities £000
United Kingdom	(2,107)	859	(1,248)
EEA	(10,462)	4,265	(6,197)
USA	(74,511)	30,379	(44,132)
International	(97,593)	39,790	(57,803)
Total	**(184,673)**	**75,293**	**(109,380)**

Key Assumptions

The principal assumption underlying the liability estimates is that the future claims development will follow a similar pattern to past claims development experience. This includes assumptions in respect of average claim costs, claim handling costs, claim inflation factors and claim numbers for each accident year. Additional qualitative judgements are used to assess the extent to which past trends may not apply in the future, for example: one–off occurrence; changes in market factors such as public attitude to claiming; economic conditions and internal factors such as portfolio mix, policy conditions and claims handling procedures. Judgement is further used to assess the extent to which external factors such as judicial decisions and government legislation affect the estimates.

Other key circumstances affecting the reliability of assumptions include variation in interest rates, delays in settlement and changes in foreign currency rates.

g. Credit Risk

Credit risk arises where one party is exposed to a loss through another party failing to perform its financial obligations to the other party, including failure to perform in a timely manner. Examples of credit risk arising in insurance are from premium debtors, where cover under contracts of insurance may either commence before premiums become due or continue after their non-payment. It can also arise if a reinsurer fails to fulfil its obligation to pay where a valid claim has been made.

Credit risk is not limited to those risks arising in insurance but also in financial investments where the Syndicate is exposed to potential failure by investment counterparties.

Credit risk is a concern in a prudential context because of the risk of erosion of capital due to persistent credit losses so threatening its viability as a going concern and hampering the Syndicate's ability to meet its own obligations to its insureds.

The key aspect of credit risk is the risk of default by one or more of the Syndicate's reinsurers. The Agency's policy is that the Syndicate generally reinsures with businesses rated A- or higher by one or more rating agencies. The Syndicate only uses reinsurers with lower ratings or that are completely unrated where collateral or a claim paying guarantee from a parent undertaking is provided. As at 31 December 2020, the Syndicate had £83.4m of collateral (2019: £63.8m).

The Agency has adopted a prudent investment policy. Exposure to investment counterparty risk has been minimised by appointing experienced third-party investment managers and operating to agreed investment guidelines which determine the investments to which the Syndicate is exposed. Investments performance is overseen by the Investment Committee.

The overall responsibility for the oversight of intermediaries and reinsurers has been delegated to the Risk and Capital Committee. The Risk and Capital Committee reviews the credit ratings of reinsurers on a quarterly basis and reports to the Agency Board, which approves the use of intermediaries and reinsurers and reviews any late settlement or reputational issues of the counterparties. The Agency finance and compliance functions support the formation and renewal of intermediary relationships to help ensure that inappropriate parties are not used by the Syndicate.

The policy for approving reinsurers includes limits on counterparty exposure in order to limit the total credit risk the Syndicate may be exposed to in respect of any one reinsurer.

Credit risk from exposure to investment counterparties is controlled by operating to very prudent investment guidelines. Investments are managed by a third-party investment manager, appointed under the terms of an Investment Management Agreement. The Syndicate's maximum exposure to credit risk to the assets below at 31 December 2020 is the carrying amount as presented in the note.

A ratings table for the Syndicate's financial assets that are neither due nor impaired is given below.

At 31 December 2020	**AAA**	**AA**	**A and Below**	**Unrated**	**Total**
	£000	**£000**	**£000**	**£000**	**£000**
Financial Investments	9,893	19,094	8,130	9,113	46,230
Cash at bank and in hand	-	-	5,700	-	5,700
Overseas deposits	997	208	1,142	165	2,512
Reinsurer' share of claims outstanding	-	25,784	4,911	13,506	44,201
Debtors arising out of reinsurance operations	-	3,226	12,903	7,096	23,225
Total	10,890	48,312	32,786	29,880	121,868

At 31 December 2019	AAA	AA	A and Below	Unrated	Total
	£000	£000	£000	£000	£000
Financial Investments	17,675	30,998	14,093	-	62,766
Cash at bank and in hand	-	-	16,638	-	16,638
Overseas deposits	713	125	534	41	1,413
Reinsurer' share of claims outstanding	-	10,458	41,829	23,006	75,293
Debtors arising out of reinsurance operations	-	5,155	20,617	11,339	37,111
Total	18,388	46,736	93,711	34,386	193,221

The source for ratings is Standard and Poor's. The Syndicate does not consider that there is a significant concentration of risk with respect to its insurance receivables accounts. Of the total assets, none have been impaired.

The ageing of the Syndicate's assets is disclosed below:

At 31 December 2020	Neither due nor impaired	Up to three months	Three to six months	Six months to one year	Greater than one year	Total
	£000	£000	£000	£000	£000	£000
Financial investments	46,230		-	-	-	46,230
Overseas Deposits	2,512	-	-	-	-	2,512
Cash at bank and in hand	5,700	-	-	-	-	5,700
Reinsurer' share of claims outstanding	44,201	-	-	-	-	44,201
Insurance Debtors	19,080	-	1,760	-	-	20,840
Debtors arising out of reinsurance operations	12,371	2,052	992	7,810	-	23,225
Other Assets	23,002	-	-	-	-	23,002
	153,096	2,052	2,752	7,810	-	165,710

At 31 December 2019	Neither due nor impaired	Up to three months	Three to six months	Six months to one year	Greater than one year	Total
	£000	£000	£000	£000	£000	£000
Financial investments	62,766		-	-	-	62,766
Overseas Deposits	1,413	-	-	-	-	1,413
Cash at bank and in hand	16,638	-	-	-	-	16,638
Reinsurer' share of claims outstanding	75,293	-	-	-	-	75,293
Insurance Debtors	16,445	-	-	-	-	16,445
Debtors arising out of reinsurance operations	35,650	378	1,083	-	-	37,111
Other Assets	25,502	-	-	-	-	25,502
	233,707	378	1,083	-	-	235,168

h. Market Risk

Market risk is defined as the risk or uncertainty arising from possible market price movements and their impact on the future performance of a business. This includes the possibility that changes in market factors, foreign currency exchange rates or interest rates will adversely affect the value of the Syndicate's financial assets, liabilities or expected future cash flows.

The intention of the Agency is for the Syndicate to invest surplus funds in low risk securities in line with the agreed investment guidelines.

i. Foreign Currency Risk

In order to minimise market risk arising from foreign exchange the Syndicate matches the currency of anticipated liabilities to its assets. Shortfalls of sterling to settle expenses are managed by the sale of surplus currencies as required.

Cash flow reports form part of monthly accounting. Cash flow forecasts are performed regularly to ensure currencies are matched and to minimise any foreign exchange risk.

The Syndicate maintains ledger balances in six main currencies: Sterling, Euros, US Dollars, Japanese Yen, Australian Dollars and Canadian Dollars.

The most important non-sterling currency exposure relates to the US dollar. As well as the US Situs business, exposures arise from a number of classes of business transacted outside of the USA, mainly Property. Maintenance of currency ledgers enables the Agency to monitor foreign exchange risk.

The carrying value of total assets and liabilities by currency is as follows:

At 31 December 2020	GBP	US $	Euro €	CAD $	Other	Total
	£000	£000	£000	£000	£000	£000
Reinsurers' share of technical provisions	-	53,555	2,335	(4)	-	55,886
Insurance and reinsurance receivables	9,864	39,347	(4,224)	(1,543)	621	44,065
Financial investments	1,566	38,893	-	5,771	-	46,230
Cash at bank and in hand	1,061	-	2,362	0	2,277	5,700
Other deposits	621	382	-	674	836	2,512
Other assets	(15,283)	(4,126)	9,273	(2,657)	24,110	11,317
Total assets	(2,171)	128,051	9,746	2,241	27,843	165,710
Technical Provisions	(13,548)	(138,539)	(4,782)	(6,144)	(26,715)	(189,727)
Insurance and Reinsurance Payables	478	(21,807)	(3,333)	(0)	343	(24,318)
Other creditors	(2,675)	(2)	(14)	-	-	(2,692)
Total Liabilities	(15,744)	(160,348)	(8,129)	(6,144)	(26,371)	(216,737)
Currency Adjustments	(17,644)	(12,863)	9,166	(2,665)	24,005	-
Members' balances	(35,559)	(45,159)	10,783	(6,568)	25,477	(51,027)

At 31 December 2019	GBP £000	US $ £000	Euro € £000	CAD $ £000	Other £000	Total £000
Reinsurers' share of technical provisions	3,477	80,366	7,020	60	148	91,071
Insurance and reinsurance receivables	6,715	46,618	(178)	27	374	53,556
Financial investments	9,784	50,519	-	2,463	-	62,766
Cash at bank and in hand	2,625	329	6,228	-	7,456	16,638
Other deposits	336	341	-	280	456	1,413
Other assets	(17,068)	26,118	13,573	199	(13,098)	9,724
Total assets	5,869	204,291	26,643	3,029	(4,664)	235,168
Technical Provisions	(23,729)	(143,054)	(16,698)	(2,092)	(45,368)	(230,941)
Insurance and Reinsurance Payables	186	(14,939)	(5,503)	(132)	(136)	(20,524)
Other creditors	(1,473)	-	(9)	-	-	(1,482)
Total Liabilities	(25,016)	(157,993)	(22,210)	(2,224)	(45,504)	(252,947)
Currency Adjustments	19,282	(19,032)	(13,307)	(136)	13,193	-
Members' balances	135	27,266	(8,874)	669	(36,975)	(17,779)

The Syndicate has sufficient free funds available in other currencies, which can be translated at any point to cover expenses payable and any other liabilities incurred.

j. Sensitivity Analysis

Sensitivity analysis is carried out on the underwriting/investment portfolio in relation to key parameters such as: exchange rates, market rating cycles, coverage cycles and catastrophe model output. At 31 December 2020, the Syndicate used closing rates of exchange of £1: $1.37 and £1: €1.12 (31 December 2018: £1: $1.32 and £1: €1.18).

The Agency performs sensitivity analysis based on a 10% strengthening or weakening of Pound Sterling against the Euro and US Dollar. This analysis assumes that all other variables, in particular interest rates, remain constant and that the underlying valuation of assets and liabilities in their base currency is unchanged. The process of deriving the undernoted estimates takes account of the linear retranslation movements of foreign currency monetary assets and liabilities.

Increase/(decrease) on members' balances	2020 £000	2019 £000
Strengthening of US dollar	684	1,073
Weakening of US dollar	(736)	(995)
Strengthening of Euro	323	(393)
Weakening of Euro	(353)	361

k. Interest Rate Risk

The Syndicate holds financial assets that are exposed to interest rate risk. Changes in interest yields, with all other variables constant, would result in changes in the capital value of financial investments and cash. This would affect reported profits and members' balances as indicated in the stress test below. This is applied to the position as at 31 December 2018 and considers the full effect of mark to market movements, but without recognising any running yield benefit.

	Impact on loss for the year		Impact on members' balances	
	2020	2019	2020	2019
	£000	£000	£000	£000
Shift in yield (basis points)				
50 basis points decrease	58	264	58	264
50 basis points increase	(142)	(262)	(142)	(262)

l. Liquidity Risk

Liquidity risk is the risk that a Syndicate, although solvent, either does not have available sufficient financial resources to enable it to meet its obligations as they fall due, or can secure such resources only at excessive cost. The Agency's liquidity risk policy covers only those aspects of liquidity risk which do not fall under the heading of insurance risks. Broadly, it is the management of risk arising from short-term cash-flows, rather than the risk arising from longer term matching of assets and liabilities. Nevertheless, it covers the risk of shock loss events and the risk of having insufficient liquid funds to settle liabilities.

Liquidity risk arises if assets prove to be worth substantially less than anticipated when they have to be realised i.e. there is a mismatch between planning to realise assets and actual events. Liquidity risk is closely related to market and credit risks though these are covered by separate risk policies. Market risk arises where the value of the fund/investments proves to be significantly less than anticipated due to deterioration/flux in the general economy or from currency exchange rate movement. The credit risk policy seeks to ensure that the Syndicate is in a position to meet all payments as they fall due by ensuring that inwards funds are paid promptly.

Additionally, the Syndicate aims to maintain minimum and maximum amounts of its investments in liquid funds and/or cash and cash equivalents.

The credit risk policy covers key reinsurance contracts into which the Syndicate enters, with details given below of complex reinsurance arrangements:

Future Cash Flows

The table below presents the undiscounted value of monetary liabilities of the Syndicate into their relevant maturing groups based on the remaining period at the end of the year to their contractual maturities or expected repayment dates for insurance contract liabilities.

31 December 2020	No stated maturity	< 1 year	1-3 years	3-5 years	> 5 years	Total
	£000	£000	£000	£000	£000	£000
Claims outstanding	-	93,750	41,681	8,123	671	144,225
Creditors arising out of reinsurance operations	1,471	22,847	-	-	-	24,318
Other Creditors	-	1,793	-	-	-	1,793
Total Liabilities	**1,471**	**108,108**	**51,963**	**8,123**	**671**	**170,336**

31 December 2019	< 1 year	1-3 years	3-5 years	> 5 years	Total

	£000	£000	£000	£000	£000
Claims outstanding	69,546	95,158	15,577	4,392	184,673
Creditors arising out of reinsurance operations	20,467	57	-	-	20,524
Other Creditors	1,482	-	-	-	1,482
Total Liabilities	**91,495**	**95,215**	**15,577**	**4,392**	**206,679**

m. Operational Risk

Operational risk is the risk of loss, resulting from inadequate or failed internal processes, people and systems, or from external events. Operational risk is inclusive of all internal processes, manual and computerised, and all systems; internal and external fraud; and employee competence. Employee relations and culture are included in people risks.

An assessment of operational risk is important as it can affect a Syndicate's solvency or lead to unfair treatment of consumers or lead to financial crime. The Syndicate should consider all operational risk events that may affect these matters in establishing and maintaining its systems and controls.

The Agency's strategy is to implement and maintain a high level of operational processes and procedures. These are subject to ongoing review and update. This will help reduce and control operational risk more effectively and make any subsequent loss more manageable. The operational controls are designed to meet the requirements of relevant regulatory bodies and agreed best practice. All operational controls are monitored on a regular basis to ensure that they remain fit for purpose.

n. Dependencies between Risk Categories

Under certain conditions, the outcome with respect to one risk category could influence the outcome of another. There are two such specific dependencies which the Agency has identified:

1. A major loss event could lead to widespread failures within the reinsurance market. The loss would need to be very large since the reinsurance market, particularly that part of the market to which the Syndicate is exposed, has in the past shown itself to be robust enough to withstand losses such as World Trade Center and major hurricane losses.
2. There are a number of operational risks that have the potential to correlate with major natural catastrophe losses. For example, the consequences of inadequately monitoring liquidity are only likely to be suffered should there be a significant call on liquidity (likely to happen after a major loss event).

Major loss events may have an effect on investment markets; however, the effect tends to be felt principally in equity markets to which the Syndicate has no current direct exposure.

In terms of other loss types, an aggregation of casualty claims might coincide with a weak economy. Historically, although more commonly a weak economy has coincided with a period of lower interest rates, this relationship varies depending upon the cause of the weak economy and in some instances can be accompanied by higher interest rates. The timing of the claims experience is also far from clear; in some instances, recessionary claims emerge with clarity only with a sufficient time lag (even under claims-made cover) such that the economy is improving again, and interest rates might be rising. Therefore, although there is an argument for some degree of positive correlation, it is not clear how significant this might be.

o. Risk Arising out of the COVID-19 Pandemic

Throughout 2020 the COVID-19 pandemic has continued to develop leading to increased uncertainty in the market. The level of CAT exposure in respect of COVID-19 for the Syndicate is considered material and continues to be monitored closely. Following the Supreme Court's final judgement on the FCA's business interruption test case, which substantially allowed the FCA's appeal on behalf of policy holders, the COVID-19 reserves held by the Syndicate were reviewed in light of the updated court ruling and found be appropriate. As the claims experience continues to develop, the reserves continue to be subject to ongoing review.

In addition to the reserve risk arising out of the COVID-19 pandemic, there is also an increased probability of further risks arising out of the COVID-19 pandemic. These risks include second order impacts on the economy, the insurance industry and individual classes of business, such as interest rate and currency volatility, increased risk of security defaults and an increased risk of inability to bind business. As the Syndicate continues to be closely currency matched, the exposure to currency volatility is significantly reduced, whilst the interest rate risk continues to be monitored in conjunction with the investment manager. To date, no increase in security defaults have been observed or notified by the investment manager but the investment committee continues to monitor the performance of the Syndicate's investment portfolio. Lastly, the transition to working fully digitally has been successful with the ability to successfully bind business not being impacted by the COVID-19 pandemic.

The operational risks to the Syndicate arising out of the COVID-19 pandemic broadly fall within two categories:

a) Maintaining the operating effectiveness of risk and control procedures;
b) Ensuring efficiency and effectiveness of staff working 100% remotely.

To ensure the operating effectiveness of the Syndicate's risk and control procedures, the risk function performed an in-depth review of the risk and control procedures in conjunction with the business. The review focused on whether, and to what extent, business risks had changed as a result of the pandemic and whether the effectiveness of any controls would be compromised due to staff working 100% remotely. The review concluded that on the whole operational risk had not materially increased due to the pandemic and that the business was able to function broadly as prior to the COVID-19 outbreak. The impact on risk and controls continues to be monitored.

During the early stages of the COVID-19 pandemic, a working from home policy was implemented across all UK staff and offices closed ahead of the government mandated action. The policy continuities to be revised to align with the latest government advice.

To enable a successful remote working environment, new IT initiatives were rolled out to facilitate better communication, positively impacting team collaboration whilst additional IT equipment was sourced to provide conducive home working environments.

Whilst there have not been no reports of significant infection rates amongst Arch staff, with limited impact on workforce productivity, infection rates continue to be monitored on an ongoing basis.

20. Related parties

a. Whole Account 1955 Quota Share

Syndicate 1955 ceded £0.1m (2019 £4.8m) of premium to Syndicate 1856 in 2020 on its whole account quota share, for the 2018 year of account. Further, the Syndicate refunded £49.1m as a result of commuting 2017 and prior years of account back to Syndicate 1955. This transaction was settled during the year.

b. Key Management Personnel Compensation

The key management personnel are deemed to be the Directors of the Agency or the Active Underwriter.

The Directors' remuneration has been disclosed separately in note 6 to the annual accounts.

c. Arch Companies

The Syndicate is managed by the Agency, At 31st December 2020 the Syndicate had an outstanding creditor balance with Arch of £1.8m (2019: £1.5m).

d. Arcus 1856 Limited

Arcus 1856 Limited provides services to the Syndicate paying and recharging expenses to the Syndicate, the Syndicate provides a monthly float of £0.07m to Arcus 1856 Limited, as at 31st December 2020 the Syndicate had a debtor balance of £0.2m (2019: £0.1m).

e. Working Capital Loans

The loans were repaid in 2019.

	2020	2019
	£000	£000
Balance as at 1 January	-	6,022
Repaid during the year	-	(6,050)
Interest accrued in year	-	27
FX movement in year	-	1
Balance as at 31 December	-	-

21. Funds at Lloyd's

Every member of Lloyd's is required to hold capital at Lloyd's which is held in trust and known as Funds at Lloyd's (FAL). These funds are intended primarily to cover circumstances where Syndicate assets prove insufficient to meet participating members' underwriting liabilities.

The level of FAL that Lloyd's requires a member to maintain is determined by Lloyd's based on PRA requirements and resource criteria. FAL has regard to a number of factors including the nature and amount of risk to be underwritten by the member and the assessment of the reserving risk in respect of business that has been underwritten. Since FAL is not under the management of the Agency or the Syndicate, no amount has been shown in these Annual Accounts by way of such capital resources.

However, the Agency is able to make a call on the members' FAL to meet liquidity requirements or to settle losses.

22. Off-statement of financial position items

As at 31 December 2020, the Syndicate had received £83.4m of collateral (2019: £63.8m) from reinsurers with ratings lower than A-.

The Syndicate has not been party to any other arrangement, not reflected in its annual accounts, where material risks or benefits accrue to the Syndicate.

23. Derivatives

The Syndicate has not purchased any forward foreign currency contracts to hedge currency exposure or entered into any other derivative contracts within the period.

24. Post Reporting Date Events

For the 2021 year of account, capital to support the syndicate's underwriting changed from funds managed by Credit Suisse ILS to ERS' corporate member. Support is for the currently approved business plan. But it is likely that early in the year a resubmission to Lloyd's will be made that increases the capacity and introduces new classes of business. This is in line with ERS' ambition to build a diverse, scaled Lloyd's operation as part of their overall strategy for the business. It is also the intention that later in 2021 management of the syndicate will novate from Arch to ERS. At that stage the syndicate, managing agency and corporate member will be fully aligned.

On the 4th January 2021, the Syndicate transferred across £0.2m to Lloyd's Brussels as advance claims settlement funds as part of the Part VII arrangements. This transaction will be reflected as a deposit with ceding undertakings on the syndicate balance sheet going forward.