

Guidance on the 2% Innovation ICX class

Background

Lloyd's introduced a non-transferrable class of Business "Innovation ICX" on 1 June 2020. It is designed to help the market to undertake innovation experiments without having to compete internally for capacity or impacting their performance based oversight.

We know that the market undertakes a great deal of innovation within their standard business plans. The Innovation ICX class is not designed to replace that, but to provide additional capacity where that is not possible.

While some syndicates have made use of the class during the business planning process, the majority did not. There is no downside to including ICX within your business plan, and making use of it or not depending on whether the opportunity arises.

This note aims to clarify Lloyd's views on certain regularly asked questions.

1. What is Innovation ICX?

Innovation ICX is a syndicate class of business that syndicates can use to write up to an additional 2% of Syndicate Business Forecast GWP of innovative business.

2. What is innovation?

Innovation takes many forms, and will often form parts of standard business plans that do not require the use of the Innovation ICX class. We do not define innovation and have adopted a principles-based approach. Innovation experiments often contain one or more of the following:

- Incorporates major new risks that are not materially serviced by the Lloyd's market;
- Uses new technologies to trigger and/or pay claims;
- Uses new technologies to price or quantify risks;
- Explores new methods of distribution;
- Delivers a major simplification in some regard – e.g. fast claims payments; clarity of coverage;
- Explores new ways to create capacity or consortia for innovation

We do not believe the following constitutes innovation:

- Writing a risk that is new to you but common within the Lloyd's market
- A product that you have already written for a number of years without material changes. Once a product is established and stable, we would expect it to move out of the Innovation ICX class
- Small changes to wordings of current business or the addition of minor new risks as customer needs evolve

Examples of new risks would include: coverage of human capital assets – such as team knowledge (e.g. a key team insurance to build on existing key-person insurance); coverage of the reputation asset triggered by an external service providers model or a liability policy to cover certain risks associated with a new prototype technology. In practice at a high level many risks will already be covered somewhere in the Lloyd's market (e.g. reputation insurance is already sold) – but innovation may seek to extend this to a wider definition or clarify or simplify the product.

Ultimately what constitutes innovation is the responsibility of the person responsible for innovation within the syndicate e.g. Head of Innovation or Chief Underwriting Officer. The Corporation will rely upon their assessment against the examples defined above. Every few years Markets will assess what has been written through the Innovation ICX class and if any of it is against the spirit of the guidance, permission for that syndicate to use ICX for the following year will be reconsidered.

3. Do I need to ask about individual ICX experiments?

No.

Lloyd's does not require advance discussion of your ICX experiments. We need to see the total premium allocated to ICX in your Quarterly Monitoring reporting. We also request that you include an estimate of the Innovation ICX class in the following year's plan but this does not need to link to specific innovation experiments if you don't know them yet.

If you are the lead we do expect you to have the necessary expertise and knowledge in the product line to write the ICX Experiment appropriately. For truly new risks we do not expect a track record but expect Managing Agents to have carried out a proportionate degree of analysis to estimate key parameters of any pricing models which should then be monitored. We understand that small experiments may be needed to establish data when none exists and, in this case, initial assumptions must be chosen through general reasoning.

Classes where there are existing constraints (such as financial guarantee business) remain restricted and would require approval, as usual. Refer to the Supplementary Guidance for restrictions in relation to risk codes CF, CR, FG, FM and SB.

4. Can I have the Innovation ICX class if I am RIO unacceptable?

No.

5. Can I have the Innovation ICX class if I am RIO underperforming?

If you are RIO Underperforming you will need to speak to your Syndicate Performance Manager and your proposal will be considered on a case by case basis.

6. Can I have the Innovation ICX class for the current year of account even if it wasn't in my agreed plan?

Yes.

It is ok to introduce the new Innovation ICX class mid-year; it is also ok to add additional innovation experiments beyond that indicated in your plan. If you forecast that the GWP will exceed the 2% you will need prior agreement from your SP Manager and, in this case, we would need to see details of what will be included in your plan for this class.

7. Do I need to re-submit my plan if I introduce the Innovation ICX class for the current YoA

No.

However, if you do not do so we will not be able to strip out the results from our analysis of your performance longer term.

Syndicates will need to ensure that QMB and PMDR returns also capture the Innovation ICX class of business.

8. Do I need to include the Innovation class in the capital and capacity calculations?

Yes, you will need to include the Innovation class in the LCR and when setting the Capacity number.

9. Will there be additional capital requirements if I introduce the Innovation ICX class for the current YoA?

This will depend on the type of business envisaged.

Overall it is likely that the new products will have largely independent loss experience and the additional capital can be considered de-minimis.

Only if there is a strong correlation between the new ICX experiments and your existing capital driving classes, could the impact on capital required be material.

As such a proportionate approach can be taken to the parameterisation of the class in most cases.

10. If the leader wants to include an experiment within their BAU plan but followers want to use the Innovation ICX class, can they?

Yes

11. If the follower wants to include the experiment within their BAU plan but leaders want to use the Innovation ICX class, can they?

Yes.

We understand that some syndicates will have included the Innovation ICX class in their business plan and others will be writing into their BAU classes.

12. How do we ensure consistency of performance measurement within groups of Managing agents participating on the same experiment?

Leaders should be encouraged to share performance measurement data with followers so that all parties have the same information to judge the ongoing success of experiments. Managing agents should seek advice if they are concerned about anti-competition; or ask to see the Lloyd's Product Launchpad anti-competition guidance note.

13. I want to lead but don't have the risk code – can I do it?

If you wish to lead a new product it is important to have the relevant and appropriate skills and knowledge. You would need approval from Lloyd's to add the risk code to your plan.

For truly new risks we do not expect a track record but expect Managing Agents to have carried out a proportionate degree of analysis to estimate key parameters of any pricing models which should then be monitored. We understand that small experiments may be needed to establish data when none exists and in this case initial assumptions must be chosen through general reasoning.

14. I want to follow but don't have the risk code – can I do it?

Yes.

You do not need the risk code to follow – and will be automatically granted it for following purposes only. This does not imply that you have authority to lead other experiments with that new risk code. Follow syndicates should however include risk codes in their ICX plans at the point of resubmission.

You must satisfy yourself that you have the necessary portfolio management skills to follow classes that you do not have strong underwriting skills for. This is so that you can track the performance of the innovation experiment and know when to exit if performance is poor. You should think through any reinsurance implications – including the possibility that the experiments are not covered by your programme and in this case that you are happy to write the business net of reinsurance.

15. Will Lloyd's opinion of syndicate performance be damaged if an experiment performs badly?

The combined ratio of the Innovation ICX class will not be included in Lloyd's oversight of BAU lines. Acquisition expenses are often high and results initially poor and that innovation experiments are more likely to fail. This will not be considered as evidence of poor management.

However, on a normalised expense base, business should be expected and planned to be profitable.

If the Innovation product is written into an existing class and not reported into the Innovation ICX class, Lloyd's will not be able to remove the performance of the Innovation products from the existing classes.

16. Can an ICX experiment involve a new coverholder automatically?

No.

If the innovation is to be delivered through a coverholder then Syndicate Performance Manager approval will be required.

17. Can I carry out innovation activities in excess of 2% of GWP?

Yes – but you need to speak to your Syndicate Performance Manager first. Examples of this include Syndicate in Box where their entire plan can be innovative.

18. If an experiment is included in Year of Account N and then carried forward into YoA N+1 does this count towards the 2% total in the second year?

There are two choices, either the innovation experiment is taken into the BAU plan or kept in the ICX class.

If the former, then the results will contribute to the loss ratio for the YOA N+1 against the relevant risk code as for other business. If you keep the experiment within ICX then the results will not be included in the risk code loss calculations but will count towards the YOA N+1 total.

In the SBF guidance we say: Experiments that were carried out in the current YoA may have run their course. If these are being transferred to BAU then the full 2% is available. If, however, Managing Agents are continuing with an existing experiment then this should be allocated to the prospective Innovation ICX class and the remainder will be available for new experiments.

19. Can the Innovation ICX class have an absolute maximum gross linesize that is greater than the absolute maximum gross linesize in the agreed SBF for the corresponding class?

For example, the Property SBF class has an absolute maximum gross linesize agreed at USD 50m but the Innovation ICX class for a property related experiment would need a USD 75m absolute maximum gross line size.

You will need approval from Lloyd's if you want to exceed the agreed SBF limit for the class. In this case the absolute maximum gross linesize in the Innovation ICX class would be considered on its individual merits and taking Absolute Maximum Gross Franchise Guideline Dispensations into consideration. You must also satisfy yourself that you have matching RI in place in order to cover the business written in the Innovation ICX class. The Absolute Maximum Net Retained Line should be considered taking franchise guideline dispensations into consideration. Again, you will need approval from Lloyd's in this case.