LLOYD’S MARKET OVERSIGHT
SUPERVISORY PLAN
2015
01
APRIL
31
DECEMBER
INTRODUCTION

Oversight of the Lloyd’s market is one of the key roles undertaken by the Corporation. The purpose of this supervisory plan is to provide managing agents with a high level summary of Lloyd’s view of the key risks faced by the market in 2015, as defined by our market oversight objectives and a summary of how Lloyd’s plans to supervise the market, to ensure that we manage the risk to the Lloyd’s Central Fund, Lloyd’s licences, ratings, brand and reputation and seek to ensure good outcomes for policyholders.

We need to ensure that our supervision of the market is effective and we are accountable to both the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) in that regard. We do however, also need to ensure that our market oversight activities are properly coordinated and efficiently executed to ensure our work is proportionate and minimises, as much as possible, duplication with work undertaken by the PRA and the FCA.

This is the first time we have issued a market supervisory plan. By doing so, we hope to provide you with greater transparency over the Corporation’s work and help you anticipate deadlines and activities due to arise throughout the year. It is a framework and something we intend to build on in the future and so we would welcome your feedback.

Tom Bolt
Director, Performance Management

Sean McGovern
Chief Risk Officer & General Counsel

John Parry
Director, Finance

Please send any feedback or questions you may have on the 2015 Market Oversight Supervisory plan to risk.assurance@lloyds.com
The 2015 Market Oversight Supervisory plan and wall chart is also available online at www.lloyds.com/MinimumStandards
Strategic priorities related to supervision

Solvency II – A key focus of our oversight of the market will be the readiness of managing agents for Solvency II. In December 2014, a plan was published to the market outlining the process and approach that Lloyd’s will take with regard to syndicate Solvency II work in 2015. This plan can be accessed here: www.lloyds.com/SolvencyII/2015RiskAssurancePlanandGuidance

Conduct risk – Lloyd’s will be holding workshops for Executive and Non-Executive Directors, compliance officers and underwriters throughout the year. The assurance regime will consist of reviews of agents’ compliance with the minimum standards. In addition, reviews of managing agents’ complaints procedures will be introduced on a rolling basis. We will be communicating our progress throughout the year, both at managing agent level and in respect of the market’s overall readiness.

Approach to market oversight

Lloyd’s supervision of the market is risk-based and focused on four key areas:

• Clear minimum standards – The Corporation has set minimum standards for managing agents at Lloyd’s. These standards were revised in 2014 following market consultation to ensure they (i) are up to date (ii) are in-line with the emerging Solvency II tests and standards and (iii) incorporate new standards to ensure good customer outcomes. These standards are the foundation of our supervision of the market and compliance assurance is achieved through a range of measures from self-assessment to on-site reviews.

• Business planning and capital setting process – The Capital and Planning Group (CPG) reviews annual Syndicate Business Plans, including any Franchise Guideline dispensations and syndicate capital requirements. This process has been effective in coordinating the views of all of the key market oversight teams, to ensure all key issues are considered as part of the business plan and capital setting process.

Annual Syndicate Business Plan forecasts are reviewed from June to December in a consistent, fair manner with the intention of meeting Lloyd’s agreed prudential and business objectives. Analysis is based on a variety of management, benchmarking and qualitative information that is supported by regular interaction with managing agents. Market and syndicate level performance against approved Business Plans are monitored on a quarterly basis.

Lloyd’s also aims to provide guidance on underwriting matters, to develop good practice and to raise standards.
Reserving oversight and benchmarking – Reserve Risk oversight is based on a combination of the work undertaken centrally; benchmarking of syndicates relative reserve strength and reliance on verification of reserve adequacy through the Statement of Actuarial Opinion (SAO) process. Reliance is placed on the statutory SAO process which will continue as a specific PRA Handbook requirement under the Solvency II regime and is covered by formal actuarial standards.

The annual reserve benchmarking exercise is an effective way to measure relative reserving risk between syndicates and focus attention on syndicates with a higher risk. Syndicates also receive specific feedback packs to help them understand their reserving position compared with the market.

Lloyd’s annual review of the aggregate reserve requirements tests the level of surplus held in market reserves, identifies any classes of business of potential concern (that can result in thematic reviews) and verifies the level of reserve surplus claimed as capital is reasonable. The ongoing appropriateness of reserves is tested through the quarterly monitoring of actual versus expected claims development.

Reviews – In addition to specific managing agent reviews, the Corporation conducts thematic reviews on lines of business and other issues to ensure risks are properly understood and managed. It will provide feedback to the market on its findings from any such reviews. Lloyd’s proposes to complete the following thematic reviews during 2015:

- Reserve Adequacy – Professional Indemnity/Financial Institutions reserving
- Underwriting Performance reviews – UK Employer’s Liability
- Underwriting Performance reviews – International Professional Indemnity (Non-US)
- Governance, Risk & Operations – Board composition

MARKET CONDITIONS AND RELATED ISSUES

The global economy continues to remain fragile with growing concern around the potential impact of deflation in the Eurozone, a prolonged low interest rate environment leading to lower investment yields and political uncertainty, both in the UK as a general election approaches and beyond.

Whilst 2014 performance benefited from below average major loss activity, market conditions are expected to be weaker in 2015 with underwriting conditions remaining very competitive. The January renewal season was characterised by an extension...
of the downward rating pressure experienced in the property catastrophe market to other classes of business. Soft market behaviours will continue to present challenges.

As the internet and operational technology have developed over the last 20 years, the threat of systemic cyber-attacks is high on the list of potential concerns. Following consultation with the market, Lloyd's has revised its approach to the monitoring of cyber risks by ensuring effective controls exist to manage material aggregation of exposure in the market. This includes updated existing risk codes and the introduction of new codes to enhance the monitoring of aggregation by the Exposure Management team.

The continued influx of alternative capital (collateralised reinsurance, cat bonds etc.) has contributed to the over-supply of capital in the global market and is challenging existing (re) insurer business models. Ensuring syndicates reserving is adequate will remain a key area of focus at this stage of the cycle. Reserve releases have continued and have been supported by favourable underlying claims experience. Although no immediate concerns exist, the annual review cycle will aim to identify any cyclical related impact on reserves and regular monitoring will pay particular attention to any emerging reserving issues in casualty classes. The introduction of reserving minimum standards will further enhance the level of review and these will be tested through the completion of self-assessments and a programme of rolling effectiveness reviews, to commence in early 2016.

Careful management of catastrophe exposure is a business imperative at Lloyd's. The market must be able to withstand multiple catastrophe events in any given year. Potential threats are identified by the Emerging Risks team and Realistic Disaster Scenarios that stress-test both individual syndicates and the market as a whole. Additional activities planned for 2015 aim to improve the market’s understanding of non-modelled risk exposure, broaden the choice of catastrophe modelling and enhance market practices for monitoring of liability exposure management.

The Corporation will continue to monitor placement structures and remuneration arrangements in the Lloyd's market. Whilst the Corporation does not seek to interfere with the agreement of commercial arrangements in the market, it is important managing agents continue to properly consider the structure and terms of such arrangements to ensure their compatibility with relevant laws and regulations. Managing agents must also meet the very highest of standards in their dealings with brokers for the benefit of Lloyd’s policyholders. During 2015, the Corporation will be reviewing the quarterly returns on distribution costs to ensure they are adequately capturing both the type and quantum of these payments.

WE WELCOME FEEDBACK SO WE CAN DEVELOP THE PLAN ON AN ANNUAL BASIS

email: risk.assurance@lloyds.com
## Appendix 1: Market Oversight Objectives

<table>
<thead>
<tr>
<th>Oversight Objective</th>
<th>Minimum Standard</th>
<th>Core Processes</th>
<th>Reporting from/to Market</th>
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<tbody>
<tr>
<td><strong>1. Reserve Adequacy</strong></td>
<td>• To ensure adequate reserving processes and limit significant reserving deficits</td>
<td>• Reserving Standards</td>
<td>• Syndicate feedback meetings</td>
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<td></td>
<td>• Reserve Surplus Analysis</td>
<td>• Quarterly Monitoring Return reviews</td>
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<td>• Incurred But Not Reported (IBNR) Burn Analysis</td>
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<td>• Reserve Early Warning Exercise</td>
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<td>• Statement of Actuarial Opinion (SAO) Review – Valuation of Liabilities Rules</td>
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<td><strong>2. Underwriting</strong></td>
<td>• To ensure market performance is better than that of our peers, recognising that as a specialist P&amp;C market, we have appetite for volatile risk classes</td>
<td>• Underwriting Management Standards (Strategy, Pricing and Underwriting Controls)</td>
<td>• Quarterly Monitoring Return reviews</td>
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<td>• To ensure a reasonable expectation of making a gross underwriting profit on each Line Of Business every year</td>
<td>• Syndicate Business Forecast (SBF) Review as input to the Capital &amp; Planning Group (CPG) process</td>
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<td>• Review of new Syndicate and Agency proposals</td>
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<td><strong>3. Delegated Authority</strong></td>
<td>• To ensure that delegation of underwriting is properly managed and controlled</td>
<td>• Coverholder approval</td>
<td>• 6 monthly meeting reviews</td>
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<td>• Regional and Class of Business (CoB) extension approvals</td>
<td>• Compliance reports</td>
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<td>• Complaints reviews</td>
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<td><strong>4. Catastrophe Exposure</strong></td>
<td>• To ensure that syndicates do not take excessive catastrophe risk</td>
<td>• SBF/Lloyd’s Capital Return (LCR)</td>
<td>• Major Claims Return</td>
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<td>• To ensure the market in the aggregate is not taking excessive catastrophe risk</td>
<td>• Lloyd’s Catastrophe Model (LCM) Process</td>
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<td>• Validation reports</td>
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<td>• Realistic Disaster Scenarios framework and reporting</td>
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<td>• Emerging Risks</td>
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<td>• Rest of World Aggregates</td>
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<td>• Own Risk Solvency Assessment (ORSA)</td>
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<td><strong>5. Reinsurance</strong></td>
<td>• To ensure an appropriate degree and quality of diversification in reinsurance coverage</td>
<td>• Underwriting Management Standards (Reinsurance)</td>
<td>• General and Reinsurance specific quarterly returns</td>
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<td>• To avoid excessive use of reinsurance to limit exposure to reinsurance counterparties and encourage underwriting performance discipline</td>
<td>• LCR /SBF</td>
<td>• Annual and bi-annual general returns e.g. RDS, Related Party</td>
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<td>• Quarterly Reinsurance Review including Syndicate Reinsurance Programme (SRP) Return /Quarterly Monitoring Return (A&amp;B)</td>
<td>• Ad hoc general returns e.g. Minimum Capital Requirement</td>
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<td>• Reinsurance Asset</td>
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<td>• Related/Shared Reinsurance</td>
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<td>• RDS/RDL (latter refers to RDS “Light” and only involves the collection of basic information)</td>
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<td>• ORSA</td>
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<tr>
<td>OVERSIGHT OBJECTIVE</td>
<td>MINIMUM STANDARD</td>
<td>CORE PROCESSES</td>
<td>REPORTING FROM/TO MARKET</td>
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<td>6. CLAIMS</td>
<td>• Claims Management Standards</td>
<td>• Complaints Review</td>
<td>• Notification of Appointments/Departures - may result in exit interviews</td>
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<td></td>
<td>• To ensure that managing agents manage and adjust claims to meet or exceed Lloyd’s Claims Management Principles and Minimum Standards</td>
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<td>7. INVESTMENT</td>
<td>• Investment Management Standards</td>
<td>• Market Risk element of LCR</td>
<td>• Quarterly Market Risk Review</td>
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<td>• To ensure syndicates do not take excessive investment risk. To ensure members do not take excessive investment risk</td>
<td>• Investment Risk (Quarterly Asset Data (QAD)/Lloyd’s Asset Database (LAD))</td>
<td>• Quarterly asset holdings</td>
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<tr>
<td>8. GOVERNANCE, RISK &amp; OPERATIONS</td>
<td>• Governance, Risk Management, Operating at Lloyd’s Standards</td>
<td>• Board appointments and departures</td>
<td>• Notification of Appointments/Departures - may result in exit interviews</td>
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<tr>
<td>9. CAPITAL ADEQUACY/INTERNAL MODEL APPROVAL</td>
<td>• Modelling, Design and Implementation; Scope, Change and Use; Validation</td>
<td>• Capital Approval</td>
<td>• Validation Report</td>
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<td>• To ensure Central Fund exposures are managed within risk appetite</td>
<td>• Solvency II model sign off</td>
<td>• Actuarial Function Report</td>
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<td>• ORSA</td>
<td>• Model Change Report</td>
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<tr>
<td>10. REGULATION (INCLUDING CONDUCT AND TAX)</td>
<td>• Regulatory Standards</td>
<td>• Issue resolution and post event assurance</td>
<td>• Engagement with any targeted thematic financial crime and non-compliance reviews</td>
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<td>• Conduct Risk Standards</td>
<td>• Complaints Reporting</td>
<td>• High Product Risk data to be collected in future from agents as part of SBF process</td>
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<td>• Guidance &amp; advice to the market</td>
<td>• Information requests from agents subject to assurance reviews</td>
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<td>• Issue resolution/post-event assurance</td>
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