Standard Club

By your side

The Standard Club Ltd

Financial Condition Report (FCR) 2021

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INTRODUCTION

The Standard Club Ltd was incorporated in Bermuda on 5 February 1970, and is licensed as a Class 3A insurer by the Bermuda Monetary Authority. The Standard Club Ltd (the “club”) is a mutual association and provides marine Protection and Indemnity (“P&I”) and related covers to its members.

The club’s 100% subsidiary, Standard Reinsurance (Bermuda) Limited (“Standard Re”) reinsures 90% of the business of the club’s underwriting subsidiaries (The Standard Club UK Ltd, The Standard Club Asia Ltd and The Standard Club Ireland DAC). As Standard Re represents a substantial part of The Standard Club Ltd’s financial result this Financial Condition Report is applicate to Standard Re.

This report covers the Business and Performance of the Company, its System of Governance, Risk Profile, Valuation for Solvency Purposes and Capital Management.

The club’s financial year runs to 20 February each year and reports its results in US dollars.

DECLARATION STATEMENT

To the best of our knowledge and belief, the Financial Condition Report fairly represents the financial condition of The Standard Club Ltd and Standard Reinsurance (Bermuda) Limited in all material respects.

Nick Jelley

Chief Financial Officer

Date: 15 July 2021

I. BUSINESS AND PERFORMANCE

a. **Name**

The Standard Club Ltd

b. **Insurance and group supervisor**

Bermuda Monetary Authority
BMA House
43 Victoria Street
Hamilton
Bermuda

c. **Auditors**

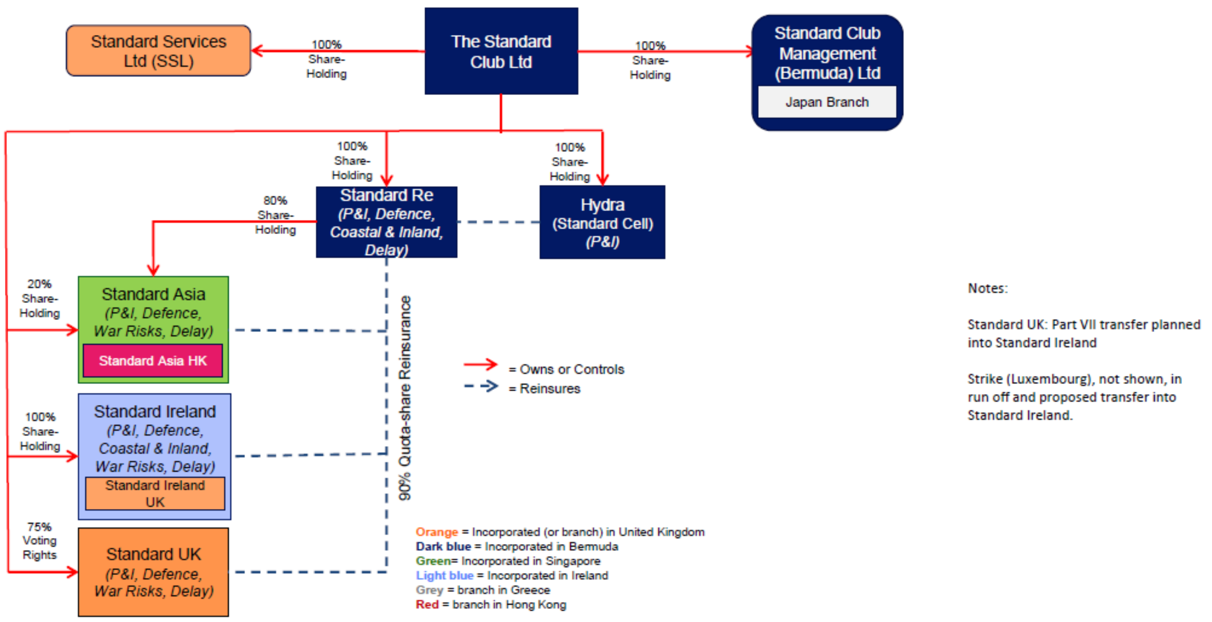
BDO LLP
150 Aldersgate Street
London
EC1A 4AB
United Kingdom

d. **Ownership details**

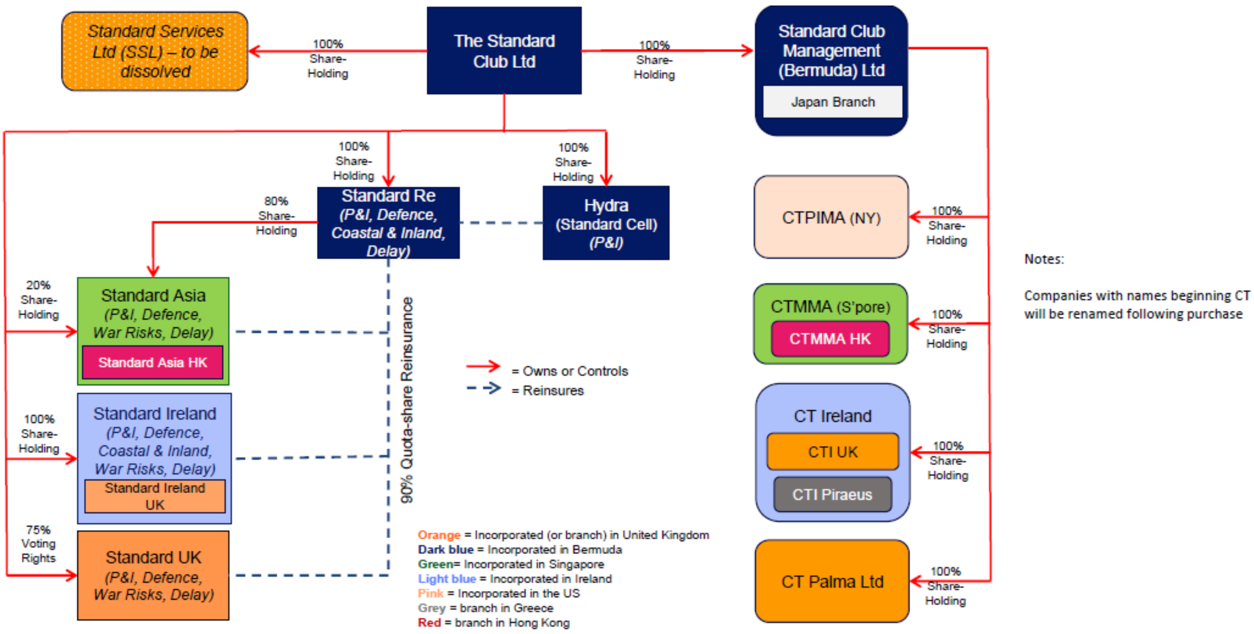
The club is a mutual association and is therefore owned and governed by its members. Members share risk and operate on a non-profit-making basis. The board of directors is primarily drawn from the membership.

e. **Group structure**

The Standard Club Group ("group") structure chart as at July 2021 is shown below.



The group structure chart that is currently proposed for August 2021 under the new operating model for the club is shown below.



f. **Insurance business written by business segment and by geographical region**

The principal activities of the group are the insurance and reinsurance of P&I and related risks, war risks, and defence risks, on behalf of its members.

Business Segments	**2021 Gross Premium Written (US$ '000)**	2020 Gross Premium Written (US$ '000)
P&I related	**292,900**	271,200
Syndicate	**-**	24,900
Total	**292,900**	296,100

The group insures ship owners located internationally; the material geographical areas where it insures risks are Europe and North America. The club's subsidiary, The Standard UK Ltd ("Standard UK"), is registered as an alien insurer in New York State, permitting it to write surplus lines insurance throughout the United States. Standard UK operates in countries outside of the European Union and Asia Pacific. The Standard Club Ireland DAC ("Standard Ireland") provides insurance on a freedom of services basis throughout the European Union and European Economic Area. The club operates in the Asia Pacific region through another subsidiary, The Standard Club Asia Ltd ("Standard Asia") and its Hong Kong licensed branch.

BMA Geographical Zones		**2021 Gross Premium Written (US$ '000)**	2020 Gross Premium Written (US$ '000)
Zone 1	Central & Western Asia	**21,591**	20,849
Zone 2	Eastern Asia	**27,600**	26,792
Zone 3	South and South-Eastern Asia	**29,140**	30,534
Zone 4	Oceania	**3,382**	3,456
Zone 5	Northern Africa	**2,174**	2,179
Zone 6	Southern Africa	**3,027**	3,058
Zone 7	Eastern Europe	**5,355**	5,302
Zone 8	Northern Europe	**19,255**	18,828
Zone 9	Southern Europe	**64,942**	65,849
Zone 10	Western Europe	**61,405**	63,619
Zone 11	Northern America (Excluding USA)	**11,064**	11,928
Zone 12	Caribbean & Centeral America	**2,383**	2,403
Zone 13	Eastern South America	**2,429**	1,925
Zone 14	Northern, Southern and Western South Americ	**3,765**	4,430
Zone 15	North-East United States	**14,952**	14,891
Zone 16	South-East United States	**12,168**	11,816
Zone 17	Mid-West United States	**301**	304
Zone 18	Western United States	**7,968**	7,938
Total		**292,900**	296,100

g. **Performance of investments and material income & expenses**

Performance of investments

In the year to 20 February 2021, the group's total investments returned 4.7% (2020: 9.7%).

Investments	**2021 Balance (US$ '000)**	**2021 Return (US$ '000)**	**2021 Return (%)**	2020 Balance (US$ '000)	2020 Return (US$ '000)	2020 Return (%)
Corporate bonds	**270,436**	**15,988**	**2.01%**	342,056	32,441	3.73%
Sovereign bonds including bills	**310,206**	**20,362**	**2.56%**	328,147	24,265	2.79%
Equities	**47,724**	**(1,670)**	**-0.21%**	108,264	4,523	0.52%
Alternatives	**127,264**	**3,023**	**0.38%**	98,444	14,698	1.69%
Gold	**-**	**-**	**-**	-	-	0.00%
Cash/FX forwards	**39,770**	**(398)**	**-0.05%**	10,279	(1,131)	-0.13%
Charles Taylor Shares	**-**	**-**	**-**	-	9,393	1.08%
Share of Syndicate 1884 investment	**-**	**-**	**-**	19,380	(289)	-0.03%
Total	**795,400**	**37,304**	**4.69%**	906,570	83,900	9.65%

Assets highlighted grey in the table above are those within the investment portfolio. In 2020 the club made returns on its holdings in CT plc shares and through its share of its Lloyds syndicate, which together contributed 1.05% to the group investment return (but fell outside the groups managed portfolio).

On 30 January 2020, the club sold its holding in Charles Taylor plc shares for $27.1m, with its participation in the Lloyds syndicate ending in March 2021.

Material income and expenses

The group's main revenue source is premium income. However, as a mutual insurance company, the club does not aim to make underwriting surpluses and instead its goal is break-even underwriting with investment returns used to strengthen the club's capital base.

For the 2020/21 financial year, the group achieved a financial year combined ratio of 121% (2019/20: 131%), the loss driven by exceptionally high claims on the Pool made by other members of the International Group. The group's free reserves stood at $360.3m at the year-end (2020: $393.7m).

The group's major expense arises from insurance claims, including a share of other International Group clubs claims on the Pool. While the Standard group's own claims were in line with budget, the group did record approximately $20m of Covid-19 related claims (not budgeted for), while there was an unprecedented level of International Group pool claims (the 2020/21 being the worst year on record, and the club's share of those claims being $30m higher than the historic average).

The overall year to year decrease in net claims incurred is due to the ending of the club's participation in Syndicate 1884.

The decrease in net operating expenses to $30.0m (2020: $58.1m) is again due to the ending of the club's participation in Syndicate 1884 (this contributed to $23.4m of the 2020 expenses, none in 2021).

Expense type	**2021 (US$ '000)**	2020 (US$ '000)
Claims incurred, net of reinsurance	**260,400**	309,100
Net operating expenses	**30,000**	58,100
Total	**290,400**	367,200

h. **Any other material information**

Management of the club

The day to day management of the club is currently outsourced to Charles Taylor and Co (Bermuda) ("the managers"), a Charles Taylor company. On 29 May 2020, Charles Taylor and the club announced their decision to work together to create a new operating model for the club. Following a review over the last year of club's strategy, scale and evolving governance requirements, the board decided to bring its core management operations 'in house'. A dedicated project team was established to ensure all aspects of the separation are managed effectively to ensure a smooth transition of the manager from Charles Taylor to the club for members, clients and stakeholders. The project is broken down by workstream: legal, compliance and controls, finance, IT, people, culture, property, operations, and communications. The new operating model and relationship with Charles Taylor should be fully in place by 20 August 2021.

This change will enable the club to insource and manage its day-to-day operations, while retaining the entrepreneurial and member-centric culture that, with the support of Charles Taylor, has led to its success over many decades. Under the new model, the same management team will remain in place, with the same individuals and teams continuing to service members' and brokers' needs and carrying out core management, underwriting, claims handling, loss prevention, finance and control activities, as part of the club's own organisation. Charles Taylor will provide a range of support services including the club's technology and services, investment management, internal audit and other support services under multi-year contracts. Charles Taylor Group companies will also be key providers to the club and its members for loss adjusting, medical assistance, marine technical and club correspondent services. The club will continue to be one of Charles Taylor's largest clients for the duration of the commercial negotiated service contracts.

International Group of P&I clubs

The club is part of the International Group of P&I clubs ("IG"), made up of 13 mutual P&I clubs who between them insure approximately 90% of the world's ocean going shipping. The IG pool (or share) large claims between them (currently claims excess of $10m are pooled), and collectively the IG purchase external reinsurance once these pooled claims exceed $100m.

UK exit from the European Union

The UK formally left the EU on 31 January 2020 and the transition period following withdrawal ended on 31 December 2020. The Standard Club Ireland DAC was established in 2019 to ensure that previous EU members of the club's UK operating subsidiary will be able to continue to be insured by the Standard Group. Options to ensure that EU risks previously insured by Standard UK prior to the February 2019 renewal are under consideration, including the option of a part VII transfer of its historic business (including EU liabilities) into Standard Ireland during 2022. The level of service and cover offered to members (both EU and non-EU) has not been affected by these changes, and has not impacted on the financial security of the wider group.

Principal risk carrying subsidiaries

Standard UK, Standard Ireland and Standard Asia, have in place a 90% quota share reinsurance arrangement with a fellow subsidiary, Standard Reinsurance (Bermuda) Limited ("Standard Re").

Standard Re holds 73% of the investments of the group (2020: 69%), has 68% of the net assets (2020: 70%), holds 72% of the net claims (2020: 71%), and has 78% of the net premium of the group (2020: 66%).

Sale of subsidiary and investment in associate

The sales of the club's subsidiary The Standard Club Corporate Name Limited ("SCCN") and the club's holding in Charles Taylor Managing Agency Limited were approved by the UK regulators, the Prudential Regulatory Authority, on 5 March 2020, with the sale completing on 16 March 2020. The sale was fully provided for in the February 2020 year end financial statements, and so had no financial impact on the February 2021 year end accounts.

COVID-19

The directors have been monitoring the development of the impact of COVID-19, both directly on the club's business, and indirectly through the development of government policy and advice. The main considerations are outlined below.

Operational

The club's managers have activated full business continuity contingency plans and have now proved that the club can continue to operate in the event of a serious prolonged incident, such as the present pandemic. Business records and documentation are stored electronically, are regularly backed up and are accessible remotely from anywhere in the world. Personnel in each of the managers' global offices have successfully transitioned to working from home and the club has been able to continue to provide the same level of service to its members.

Risks underwritten

The club insures only limited aspects of the effects of COVID-19. The marine protection and indemnity (P&I) policies, which form the majority of the club's book, provide cover for crew illness and death, crew repatriation and substitution, passenger illness and death, broader liabilities to passengers arising out of threats to life, health or safety on board, third-party illness and death, and additional quarantine expenses. The club also provides legal expenses cover for members (Defence) and cover for COVID-19 related delays. The net aggregate of COVID-19 claims notified up to 20 February 2021 across all classes of business amounted to approximately $20m (less than 13% of gross claims).

Policyholders

The economic downturn resulting from the pandemic has affected some of the club's members and business partners. However, due to the effectively compulsory nature of P&I insurance, the club has not seen any noticeable delays in collecting insurance premiums nor any upturn in bad debt. There has been an increase in the levels of laid-up ships, but any reduction in premium income arising has been offset by reduced claims on those vessels. The managers maintain very close links with members either directly or through brokers, and where members are struggling, the club is being as supportive as possible

II. GOVERNANCE STRUCTURE

a. **Board and senior executive**

i. Board and senior executive structure, role, responsibilities and segregation of responsibilities

1) Board

The board of the club comprises 28 directors, of which:

- 24 are drawn from leadership positions within shipping businesses which are insured by the club's subsidiaries;
- Three are non-executive directors with insurance industry experience;
- One is drawn from the managers, being the Chief Executive Officer ("CEO") of the club.

The role of the board is to focus on those tasks that are unique to it as the representative of the members and necessary for it to undertake for the effective promotion of the company's interests. The board will assure itself that the club is achieving the purpose by satisfying itself that the business plan developed by the managers and accepted by the board represents a satisfactory means of progressing the purpose.

2) Board committees

There is a schedule of matters reserved for consideration by the board and the board has established three committees: Audit and Risk Committee ("ARC"), Nomination and Governance Committee ("NGC") and Strategy Committee.

The board and its committees meet at least three times a year. One meeting is held at least every other year in Bermuda, the other meetings are held throughout the world as the majority of the board is comprised of members drawn from the global shipping community.

In addition, a 'Chairman's Group', comprising the chairmen and deputy chairmen of the Standard Club, Standard Asia, Standard Ireland and Standard UK, the chairmen of each committee, and a past chairman review the affairs of the club with the managers between board meetings.

A Remuneration Committee was established on 18 August 2020. The committee oversees remuneration matters for the club. Directors receive fees agreed by the club membership in general meeting, (other than the fees of non-member directors which are agreed by the board), and which are appropriate to their non-executive status. The fees paid to the directors are in line with those paid in other P&I clubs. Directors who are employed by the managers do not receive director's fees. However, the performance-related elements of their remuneration are reviewed by the Remuneration Committee to ensure that they are stretching and designed to promote the long-term success of the business. The Nomination and Governance Committee considered the remuneration policy of the managers and the objectives of the senior executive team to ensure that they are aligned with the interests of the club and risk appetite.

3) Delegation of responsibilities and allocation of functions.

a) Delegation of day-to-day management

The day-to-day management of the club and its subsidiary companies is delegated to the manager by contract under a management agreement.

b) Management Agreement

The management agreement sets out the terms upon which the managers and its affiliated group companies provide management services to the group.

c) Service Level Agreement and Key Performance Indicators

The services provided by the manager are subject to a Service Level Agreement ("SLA") which forms part of, and is subject to, the management agreement. The SLA sets out the key performance indicators ("KPI's") for the club's success and assist the board in its monitoring of the material outsourcing arrangement.

The NGC and the board review the manager's performance against KPIs set out in the SLA on an annual basis.

The manager oversees execution of the day to day management of the club through a number of committees, which include; manager's executive committee, manager's risk committee, manager's regulatory risk committee, and which are comprised of selected management and staff of the manager with appropriate professional qualifications, skills and experience. The manager's executive committee is led by the Chief Executive of the Management Services Division.

The club has appointed the following officer positions from employees of the manager:

Chief Risk Officer

Group Financial Controller

Group Compliance Officer

In addition the managers serve as the Company Secretary.

Each of these officers performs their group responsibilities from the head office in Bermuda and report directly to the club's board and committees as required.

4) Training - an annual program of training is provided to the board and its committees, key function holders and the manager's employees.

5) Internal audit and compliance reviews of management functions are carried out to assess performance against agreed systems and procedures and for effectiveness.

6) Annual appraisal process/board evaluation

As part of the club's governance processes, and in line with good corporate governance practices, the club conducts a periodic board and committee evaluation.

The NGC makes recommendations to the board in respect of enhancements that it considers desirable following its review of the evaluation results. Each January, it considers the progress against actions in respect of improvements identified in the results of the annual evaluation process.

ii. Remuneration policy and practices

Directors' fees (including committees) – The NGC's terms of reference include the review and recommendation of changes to directors' fees. A detailed benchmarking exercise was conducted during 2015 to ensure fees were brought into line with market rates, and a further review was conducted during 2016.

Management fee – Annually in October the manager submits a proposal in respect of the proposed fee to be paid by the club to the manager, for the services provided under the management agreement for the following year, to the NGC. The NGC reviews the fee proposals and makes a recommendation to the board. The NGC in reviewing the fee takes account of the fees paid by the other P&I clubs to their respective management companies and the resources required to execute the company's business strategy.

Remuneration policy - The NGC considers the remuneration policy of the manager to ensure that it aligns with the interests of the club and that it does not promote excessive risk taking. In doing so, it additionally reviews the objectives of the Chief Executive of the Management Services Division in respect of the previous year as well as the prospective objectives of the Chief Executive and selected members of the manager's executive committee. The chairman of the NGC reports to the board on its review of the policy.

iii. Pension or early retirement schemes

As part of the separation process with Charles Taylor, during the year 17 staff involved in the management of the club moved employment into a subsidiary of the club. This subsidiary does not operate any defined benefit or early retirement schemes for those employees.

iv. Material transactions with shareholder controllers, persons who exercise significant influence, the board or senior executives

No transactions occurred during the financial year.

b. **Fitness and proprietary requirements –**

i. Fit and proper process in assessing the board and senior executive

The club outsources management of the company and its subsidiaries to a manager, as is the most common operating structure for P&I Clubs across the world. The contract is with the managers who in turn engages other CT group entities. There are two basic groups of roles that can be considered key to the club:

- The Non-Executive Directors of the Club who act as Chair of the Board, Audit and Risk Committee or the Nomination and Governance Committee;
- The manager's executive committee which is comprised of management and staff of the manager with appropriate qualifications, skills and experience in all of the key roles and functions required to effectively operate the club's business and execute its strategy.

There is also a skills and knowledge matrix used by the club to ensure that the board has the right combination of skills, knowledge and experience to meet its regulatory obligations and the firm's strategic and operational objectives.

A Fit and Proper Policy is in place for the club and describes the objectives, roles and responsibilities and governance around the selection, due diligence and appointment of resource into the key roles. The policy is reviewed and approved at least annually.

ii. Board and senior executives' professional qualifications, skills and expertise

The board is drawn from a cross section of the club's membership, all of whom are senior managers (or owners) in those organisations, plus three non-executive directors with insurance industry expertise, and one executive of the managers. Members of the board are selected based on their professional experience and expertise. The table below outlines the board's areas of expertise.

SYSTEM OF GOVERNANCE	INSURANCE & FINANCIAL MARKETS	BUSINESS STRATEGY & BUSINESS MODEL	REGULATORY FRAMEWORK & REQUIREMENTS	FINANCIAL & ACTUARIAL ANALYSIS	LEGAL	SHIP OPERATIONS	SHIPPING
17	11	24	4	13	5	**3**	22

c. **Risk Management and Solvency Self-Assessment**

i. Risk management process & procedures to identify, measure, manage and report on risk exposures

1) Risk management system

The risk management system is owned and defined by the board. It is designed to ensure that the risk strategy is consistent with the overall business strategy and operates effectively within its documented risk appetite. The risk management system includes classification of risks in the risk register, assessment of risks in terms of likelihood and impact, and identification of key risk controls and indicators for each risk type. Oversight of the risk framework governance is delegated by the board to the ARC, and formal roles, responsibilities and governance of risk are set out in the scope of individual senior management role descriptions, terms of reference of internal oversight committees and the policies and procedures used within the business.

2) "Three lines of defence" principle

The risk management system follows 'three lines of defence' principles widely used within the insurance industry. Management of risk is performed by business functions on a day to day basis, supplemented by oversight and review of controls by the risk management function and independent assurance that controls are adequate through testing performed by the internal audit department.

3) Risk management function

The risk management function consists of the risk management department and other members of the executive management team involved in oversight of the risk management processes of the business, for example members of the manager's risk committee. The risk management department is responsible for co-ordinating the activities of the risk management function and maintaining a high level of risk management awareness across the business. The risk management department chairs a quarterly risk committee with cross function and division representatives from across the wider Standard Group. It is responsible for making recommendations and ensuring that executive management, as well as the Group and subsidiary boards and sub-committees are kept informed of key risk information and risk issues

4) Risk strategy and appetite

Risk management strategy is subject to a formal strategic risk appetite statement, which sets out the degree of risk considered prudent to accept in the overall long-term interests of the club's stakeholders. Risk appetite and strategy are explicitly linked with the capital management objectives of the club and the nature of its mutual ownership and ethos.

The strategic risk appetite statement requires the business to manage its affairs in a manner intended to:

- Reduce the likelihood that it is required to make an unbudgeted supplementary call on its members to an acceptable minimum;
- Target a breakeven underwriting result over the business planning horizon;
- Ensure it maintains delivery of excellent levels of service to members;
- Ensure the degree of risk to which mutual members subject to supplementary calls are exposed from activities other than core underwriting activities (for example, from investments or fixed premium business) is appropriate and commensurate with the expected benefits.

In addition, the business monitors the level of capital held to ensure it is at a level appropriate to allow for the orderly management of its affairs consistent with its mutual objectives, including maintaining its financial strength and external credit rating.

5) Risk governance

The ARC and board review the club's risk appetite and risk policies at least annually in respect of the major business risks facing the group, their potential impact, and the systems to manage and mitigate those risks.

Day to day management of risk is the responsibility of the manager's executives as part of the performance of their roles, as set out in individual job descriptions, defined processes and procedures identifying levels of authority within the management structure, and risk policies. The club operates an internal manager's risk committee led by the Chief Risk Officer and including key senior managers, which monitors and provides oversight of risk and capital issues across the business. The risk committee is responsible for making recommendations and ensuring that the manager's executive committee is kept informed of key risk information and issues, and escalating matters of concern to the ARC.

The club monitors its exposures against the risk appetite on an ongoing basis using a system of key risk indicators and tolerances that are regularly reported to the board through the risk overview presented in risk and board reports. The risk tolerance is the variance around the risk limit that the club may operate in before the development of a remediation plan is required to be prepared by the managers. Breaches of risk limits require immediate escalation to the board for their consideration of remediation actions.

6) Management information

Tools, models and systems have been developed in order to provide qualitative and quantitative management information for use in risk management decisions. In particular, the group makes use of its internal model in order to quantify the levels of aggregate risk carried at both group and entity level and to monitor whether levels of risk are within strategic risk appetite. Detailed measures of the group's appetite for risk have also been established, with key risk indicators reported at each board meeting against pre-set board and management tolerances, for example with respect to key financial ratios, maximum exposure to individual investment counterparties, maximum exposure to 3rd party counterparties and liquidity requirements.

7) Policies and procedures

Policies and procedures are in place in respect of the material risks of the club which, amongst other matters, set out the roles and responsibilities with respect to the management of risk. Specific processes and procedures are in place to manage risks arising from the business. These are designed to ensure that transactions and decisions are made by individuals with appropriate levels of experience and authority, with consideration of relevant risks.

ii. Risk management and solvency self-assessment systems implementation

1) Strategy and appetite

The risk management function provides significant input into the design and implementation of risk appetite which assists in setting the strategy of the club, for example with respect to the key underwriting and investment risks.

The risk management department co-ordinates the monitoring of whether the club is likely to, or has, exceeded risk appetite and assists in making decisions in those eventualities. The assessment is reviewed by the manager's risk committee on a quarterly basis.

2) Risk assessment and control effectiveness reviews

The risk management department has implemented a rolling program of reviews to assess business risks and the effectiveness of the mitigating controls in place. This program is designed to cover all areas of risk identified in the risk register at least once a year. These reviews, which are performed in conjunction with each business function, consider whether controls are effective and ensure that outstanding risk mitigation actions are occurring in a timely manner.

3) Incident reporting and embedding risk management

There is an emphasis upon continual education of management and staff in considering good risk management practice in the respective aspects of their roles. The risk management department maintains an incident reporting process which records control failures and "near miss" events and is designed to identify underlying root causes and whether any control improvements can be implemented. Incidents are reported to the executive management committee and to the board.

4) Use of internal model

The risk management system and processes are linked to the club's internal model. The internal model is used to create the financial projections which form the business plan. Key assumptions used in the model reflect expectations of future insured exposure and premium rate changes, claims frequency and severity trends and investment returns. Assumptions with respect to the degree of uncertainty and volatility arising from risk taking activities are based on a combination of analysis performed by the actuarial function and inputs provided by business functions. Internal model assumptions are reviewed by relevant business experts and the ARC. Internal model outputs are a key input into the ORSA process described below, and its uses include assessing levels of risk compared with risk appetite, assessing the adequacy of reinsurance arrangements, and informing pricing and capital management decisions.

iii. Relationship between solvency self-assessment, solvency needs & capital, and risk management

1) Key elements of the Solvency Self-Assessment process (known internally as the Own Risk and Solvency Assessment ("ORSA") process).

The ORSA process brings together the key elements of risk, capital and strategy. An annual ORSA report which summarizes the activity undertaken in the ORSA process is approved by the board which meets the Bermuda regulatory requirement to prepare a Commercial Insurers Solvency Self-Assessment report.

The ORSA process combines outputs from business strategy and planning processes with the results of risk profile monitoring, stress and scenario testing and outputs from the internal model on aggregate levels of risk. The annual ORSA report consolidates the results of these analyses in a single document in order to provide a coherent view of capital adequacy, risk profile, the effectiveness of the risk management system and key risk mitigating actions required to ensure the business remains within risk appetite.

In addition, each board meeting receives a summarised “Risk Overview” which sets out the status of key risks to achieving strategic objectives together with actions designed to mitigate these, The core strategic objective that most directly relates to the club’s overall solvency needs is “to provide first class financial security”. The current qualitative and quantitative risks to achieving this objective, any mitigating actions and the outlook over the next 12 months are assessed and incorporated into the ORSA process. The “Risk Overview” also includes an assessment of capital adequacy and an analysis of key risks for the current financial year.

2) Financial information and business plan

The prior year results used for financial reporting provide the basis for the first stage of the ORSA and strategic planning processes. The internal model is used to create a business plan over a three year time horizon including projected levels of free reserves and the potential distribution of outcomes around the central projection. These results are used to review the business plan against risk appetite and to amend plans if required.

3) Stress and scenario testing and emerging risk review

The ORSA process includes a pre-defined set of stress and scenario tests. There is a structured annual process to review potential emerging risks which is designed to identify whether any changing or new risk could have a significant impact on the business risk profile, and whether any consequent actions are required (for example, a new risk mitigating action or set of controls). The significance of new or emerging risks is typically assessed through development of appropriate stress tests.

<u>iv. Solvency self-assessment approval process</u>

1) ORSA report governance

The Chief Risk Officer is responsible for the preparation of the ORSA report, including ensuring that it articulates a coherent overall strategic plan that fits with the agreed risk appetite. The board reviews and approves the ORSA report. A key expectation is that the ORSA report and strategic and business plans are aligned and fit within strategic risk appetite.

2) ORSA process timing

The ORSA process is continuous, with various elements conducted through the year and integrated into the final ORSA report. For example, internal model outputs are used to inform decisions on potential changes in premium rates for renewals in the following policy year. A draft assessment of capital levels based on internal model outputs incorporating the results of February renewals is provided at the May board meeting.

The final ORSA report is approved annually at the October board meeting. Much of the information that forms part of the final ORSA report is reported to the ARC throughout the year via the regular risk reporting.

Internal Audit perform an independent review of the ORSA report to provide assurance that it has been prepared in line with the board’s ORSA policy and is consistent with underlying financial and other information.

d. **Internal controls**

i. Internal control system

The club has a robust system of internal controls which are used to manage the risks faced by the club to within its documented risk appetite. This system covers all functions and all activities undertaken by the managers on behalf of the club.

Business functions (such as underwriting, loss prevention or claims) own the functional controls for their areas of responsibility. These controls are set out in the risk register and described in procedure manuals, often accompanied by process flow diagrams. Formal procedures are in place covering a wide range of business activities, for example, pricing of new business, performance of member risk reviews by the loss prevention department, issuance of certificates of insurance, approval and payment of claims, and sanctions, anti-money laundering, anti-bribery and corruption due diligence on counterparties prior to transacting business.

The effectiveness of controls is assessed at least annually by the risk owners identified in the risk register in conjunction with the risk department, and subject to periodic Internal audit testing and review. Material controls are reviewed by Internal Audit on a three yearly rotating basis and those with a strong regulatory element are also subject to monitoring reviews by the compliance department. Any failure of a material control is recorded as an incident and reported through the executive management structure and to the board.

ii. Compliance function

The Compliance function, supported by Risk and Finance, covers four principal areas:

- Prudential (ensuring solvency and rating agency capital is maintained; regulatory capital is reported and pertinent waivers are maintained);
- Organisational (training and competence; fit and proper of key roles; general governance, including Conflicts of Interest and Data Protection issues)
- Transactional (regulatory reporting; conforming with licensing requirements; maintaining a complaints register; guarding against Financial Crime and screening against sanctioned entities, regions and cargo).
- Advisory (providing and issuing advice to the business on a range of regulatory issue)

e. **Internal Audit**

i. Implementation of the internal audit function

Internal audit (“IA”) prepares, in consultation with risk management, compliance senior management and other key users, an annual audit plan (‘the plan’), setting out the proposed timing and rationale for IA assignments. The plan is based on a risk assessment, identifying business objectives, all significant activities and key risks to the achievement of those objectives. The plan is reviewed and approved by the ARC and communicated to the club boards. The ARC satisfy themselves that the plan addresses all key business risks.

Any significant changes to the plan are discussed with the chairman of the ARC and are communicated to the ARC for approval.

ii. Independence and objectivity of the internal audit function

IA is independent of the activities that it audits, and its auditors are objective in performing their work. IA, while consultative in approach, is free from interference in determining the scope of internal auditing, performing work and communicating results. In summary, IA is impartial, unbiased and avoids conflicts of interest.

To ensure independence, IA is directly accountable to the chairman of the ARC, with a day-to-day administrative reporting line to the CEO of CT, and free and unrestricted access to the chairmen of the club boards.

The ARC approve the audit terms of reference and audit plan and material changes to them.

Members of the IA team do not generally perform day-to-day control procedures or take operational responsibility for any part of CT's operations outside IA. CT's management is responsible for the establishment and ongoing operation of the internal control system.

The ARC review the scope and nature of the work performed by IA to confirm its independence and objectivity.

f. **Actuarial function**

The Chief Actuary, a qualified actuary with more than 25 years of general insurance experience, has responsibility for the actuarial function, which:

- contributes to the effective implementation and embedding of the risk management system, in particular by designing, implementing, updating, testing, running and reporting on the internal model;
- calculates and validates the technical provisions;
- assists with the underwriting process by devising and maintaining pricing tools;
- expresses an opinion on the overall underwriting policy;
- uses the internal model to compare proposed reinsurance arrangements;
- expresses an opinion on the adequacy of current reinsurance arrangements;
- reports to the senior management and the board on the reliability and adequacy of actuarial calculations and technical provisions, including a comparison of actual developments with those previously expected;
- liaises with the external auditors to assist with their annual independent assessment of the technical provisions; and
- provides an opinion to regulators on the adequacy of the respective group regulated entities technical provisions.

The Chief Actuary reports to the board or its committees four times a year on subjects that as a minimum include the actuarial function reporting cycle, which comprises the setting of GAAP technical provisions, the conversion of GAAP technical provisions to an economic balance sheet ("EBS") basis, an opinion on the underwriting policy, an opinion on the reinsurance arrangements, and a description of how the actuarial function has contributed to the risk management system during the year (including use of the club's internal model).

g. **Outsourcing**

1) Outsourced management of the business

In common with a number of P&I Clubs (across the world), the day-to-day management of the club has from the outset been outsourced to a Club manager, Charles Taylor. On 29 May 2020 the club and Charles Taylor announced that the management of the club would be taken in-house. The two parties are working together to ensure a smooth transition for club members, clients and stakeholders, beginning in July 2020 and concluding in August 2021. In order to ensure a smooth transition an 'advance team' of senior staff were amongst the club's first official employees transferred to lead the technical build of the new operating model and to oversee day-to-day management. These individuals are directly employed by a subsidiary of the club and perform significant roles for the Standard group.

Until August 2021, Charles Taylor and Co (Bermuda) performs the outsourced management of the Standard Group from Bermuda or procures the performance of activities from other Charles Taylor entities. Reflecting the wide geographical scope of the club's business, it procures performance of some activities to other entities within the CT group, the most significant of which are:

- Charles Taylor Investment Management Company Limited – providing investment management services for the group and its subsidiaries.
- Charles Taylor & Co. Limited – providing insurance management services in London, including management of a substantial part of the affairs of Standard UK.
- Charles Taylor & Co (Ireland) - providing insurance management services in Ireland, including management of a substantial part of the affairs of Standard Ireland, and some claims management services on behalf of Standard UK.
- Charles Taylor Mutual Management (Asia) Pte. Limited – providing insurance management services in Singapore, including management of a substantial part of the affairs of Standard Asia, Standard Asia's Hong Kong branch and some claims management services on behalf of Standard UK.

A number of arrangements are in place between the managers and other affiliated CT entities, for example to support claims management activities performed on behalf of Standard UK in its regional offices or where specific ancillary services are performed such as acting as claims correspondent.

The performance of the managers is formally reviewed by the NGC at least annually against the Service Level Agreement detailed within the management agreement which governs the outsourced relationship. The board also exercises oversight of the performance of the managers through the regular reporting provided by the various function heads at each meeting of the board and its committees, through reports provided by the key functions (finance, underwriting, claims, actuarial, risk, finance, compliance and internal audit) and through regular discussion between key board members (for example, the chair of Standard UK and the chairs of the ARC and NGC) and executives.

2) Outsourcing policy

An Outsourcing Policy is in place which considers both:

- The primary outsourcing relationship with the managers and other CT group entities which have been delegated responsibility to provide management services to members of the group.
- The approach to be taken in the event that the managers themselves outsource activities that would otherwise be performed directly by them.

The outsourcing policy sets out a number of requirements with respect to outsourcing arrangements including:

- No activity or function reserved for the board may be outsourced. In addition, if the function or activity is considered critical or important (for example, insurance product design and pricing, performance of key functions such as actuarial), the board must authorise any further outsourcing arrangement proposed by the managers.
- Notification of material outsourcing arrangements to regulators where required.
- Criteria which must be considered in selecting a new outsourced provider or renewing an existing contract, including the ability of the provider to provide services in a manner that will not breach risk appetite and will meet business continuity standards and regulatory requirements.
- Prescribed elements to be included in written contractual arrangements.
- Contingency plans in the event the service provider is unable to deliver an adequate level of service or seeks to terminate the outsourced arrangement.

3) Future developments

As referred to above, the club is in the process of bringing it main management functions in-house. New contractual agreements will be in place from August 2021 with Charles Taylor for the provision of support services including the club's technology and services, investment management, internal audit and other support services. This change will enable the club to insource and manage its day-to-day operations, while retaining the entrepreneurial and member-centric culture that has led to its success over many decades. The outsourcing framework under which the new operating model will be governed are currently been reviewed as part of the transition phase to the new operating model.

h. **Other material information**

No other material information to report.

III. RISK PROFILE

The group's main risk categories are underwriting, market, credit, liquidity and operational risks. To maximise the efficient use of capital within the group Standard Re retains 90% of the underwriting, credit, liquidity and operational risk of the core P&I business and related covers, and holds the majority of the investment assets of the group. As a result, while the following risks are set out at group level, they also apply to the principal group risk carrier, Standard Re.

A. UNDERWRITING RISK

a. **Material underwriting risks**

1) The underwriting risk of the club arises from two main categories of insurance product which it provides to its members:

- "Poolable" P&I cover – being protection and indemnity insurance which covers members against third party liabilities arising from their shipping activities.

  "Poolable" P&I represents covers which qualify for inclusion within the International Group ("IG") pooling agreement. The IG is made up of 13 principal mutual P&I clubs which are owned and controlled by ship owners representing approximately 90% of the world's ocean going ship tonnage. Each club (including The Standard Club) pools losses in excess of a $10 million per claim retention, with losses in excess of this amount being shared between all clubs using a formula based on historic loss record of each club and the tonnage and type of ships entered into the pool. The IG has entered into a number of collective reinsurance arrangements with the commercial reinsurance market, which takes a progressively greater share of individual losses as claim size increases. Losses in excess $2.1 billion (termed "overspill claims") are re-pooled, however the IG reinsurance arrangement provides an additional $1 billion reinsurance for a single claim. In practice no claim has yet arisen which breached the limits of the IG reinsurance programme, with the largest individual poolable claim to date being $1.48 billion of third-party liability costs arising from the wreck of the Costa Concordia.

  Poolable P&I cover is a variable premium product, meaning that the club may make supplementary calls on members if required to meet unanticipated financial losses. All clubs which are members of the IG must be mutual associations capable of levying additional premiums on their members in the event that an overspill claim occurs. In practice, as set out in the club's risk appetite statement, the business seeks to minimise the possibility that such unbudgeted supplementary calls could occur.

  As a consequence of the pooling arrangement the club is subject to underwriting risk arising from both its own policyholders and through its share of other P&I club's poolable claims ("inwards pool" claims).

- "Non-pool" business – being either protection and indemnity insurance where the nature of the underlying activity does not qualify for inclusion in the IG pooling arrangement (primarily relating to offshore energy activities), liability cover for ship charterers, or ancillary covers such as legal expense costs relating to shipping disputes.

In addition to the benefit provided by the IG pooling agreement, the club benefits from specific per claim reinsurance for non-poolable risks and stop-loss reinsurances provided by commercial reinsurers.

2) Categorisation of types of underwriting risk

At a high level underwriting risk is categorised between premium risk, being the risk that premiums will not be sufficient to meet all claims covered and associated expenses, and reserve risk, being the risk that case or actuarial reserves will be inadequate in covering known or unreported losses. These risks are further considered in terms of:

- Inappropriate insurance strategy, including reinsurance strategy;
- Ineffective implementation of underwriting strategy;

- Ineffective implementation of reinsurance strategy;
- Ineffective claims management, leading to inappropriate case reserve and settlements;
- Inadequate actuarial reserving.

b. **Risk mitigation techniques**

A number of risk mitigation techniques are used to manage underwriting risk, including:

1) Premium risk

- Board and senior management review of underwriting results, drafting of strategy and business plans;
- Reinsurance strategy is reviewed and monitored by the board in line with risk appetite;
- Comprehensive and high quality reinsurance programme;
- Underwriting and reinsurance authorities, approvals, processes, reporting and review;
- Programme of peer reviews and other technical file reviews;
- Use of exposure based pricing tools for new business;
- Activities of the loss prevention department, including ship surveys, member risk reviews, and application of coverage warranties, exclusions or non-renewal of members where ship operating standards are considered deficient;
- Monitoring for undue concentrations of risk and acceptability of results consistent with risk appetite.

2) Reserve risk

- Claims case management: authorities, approvals, processes, reporting and review;
- Systems workflow in place to assist management of claims cases;
- Claims peer review, feedback and management information;
- Actuarial reserving: modelling processes, reporting and review;
- Board: review and approval of key reserving output.

c. **Material risk concentrations and changes in risk profile over the reporting period**

Gross underwriting risk decreased over the reporting period following the disposal of the Standard Club Corporate Name Ltd on 16 March 2020 (reducing reserve risk by 10%). Premium risk is largely unchanged from 2020 (as gross and net premium, which drives premium risk, is little changed).

More than 90% of net underwriting risk arises from poolable P&I cover, driven largely by the club's exposure to inwards pool claims. While the club monitors other types of underwriting risk concentration, including ship type and membership, these represent less significant sources of concentration risk. P&I cover provides liability cover for ships which are trading on a global basis, therefore the club is not significantly exposed to geographical risk concentrations, for example, compared with insurance of static property or similar asset based covers. As a consequence the primary drivers of underwriting risk relate to:

- The number and severity of large poolable P&I claims including inward pool claims.
- The potential for significant adverse reserve development arising from existing claims or new types of previously unreported liability.

The last two years has seen an upturn in large claims, both the clubs own and other IG clubs pool claims (with the 2020/21 policy year seeing the worst year on record for the pool). This has resulted in rate rises recorded across the International Group at the February 2021 renewal, with further increases expected in February 2022.

d. **Stress and scenario testing**

The key stress tests identified with respect to underwriting risk relate to:

- Premium risk – a significantly higher than historic average number of large pool claims occurring in the current policy year.
- Reserve risk – reserve deterioration across all years of account due to a systemic reserving issue.

- Reinsurance stresses include the impact of the removal of free reinstatements on GXL programme, removal of the whole account stop loss reinsurance.

The key scenario tests identified with respect to underwriting risk relate to:

- A large overspill claim
- Industry bankruptcies and consolidation
- Covid-19 worst case scenario.

The club is assessed as being within its risk appetite in relation to the above scenarios.

B. MARKET RISK

a. Material market risks

1) Market risk relates to the risk of losses on assets held to pay future claims and operating expenses, and losses on surplus assets held for solvency purposes.

The club's investment strategy has been developed with the following objectives:

- To preserve capital for the payment of the club's claims and other liabilities by limiting risk in the portfolio.
- Within the risk tolerance, to maximise the overall returns as measured over rolling three-year periods.

2) Categorisation of types of market risk

Market risk is considered in terms of three categories:

- Inappropriate investment strategy;
- Ineffective implementation of investment policy, strategy or investment rules;
- Ineffective management of investment counterparties.

b. Risk mitigation techniques

A number of risk mitigation techniques are used to manage market risk, including:

- The board reviews and approves investment strategy;
- Clear investment guidelines and rules are implemented and monitored, including counterparty limits;
- Investment guidelines require investing widely and in different asset classes to diversify the portfolio;
- Asset–liability matching processes are in place;
- Foreign-exchange matching processes are in place;
- Interest rate risk exposure is measured and controlled through regular review of the appropriate duration;
- Levels of investment risk are monitored using “Value at Risk” techniques which must remain within risk appetite.

c. Material risk concentrations and changes in risk profile over the reporting period

Following a review by the asset allocation working group, in February 2021 the benchmark, which reflects the long-term risk appetite of the club, was revised and saw a reduction in the equity and alternatives exposure (from 27% to 15%) with the allocation to corporate bonds increased (from 38% to 50%). Maximum exposures to asset classes are also prescribed however the given the level of uncertainty and volatility in global equity markets investments in equities are at the lower end of the permitted range.

Despite adopting a more conservative approach, market risk in the BSCR has increased since 2019 due to the changes in capital charges employed by the BMA in particular around equity risk (with the charge increasing from 14% to 35%) and concentration risk (the concentration risk charge applied to shares has also increased from 14% to 35%).

d. **Investment in assets in accordance with the Prudent Person Principles of the Code of Conduct**

The club invests in a range of assets and instruments whose risks it can sufficiently identify, measure, monitor, manage, control and report, and appropriately consider in the assessment of its overall solvency. All assets are invested to ensure the security, quality, liquidity and profitability of the portfolio as a whole. Sufficient assets are localised to ensure their availability. Assets are invested in the best interests of the club under the direction of the investment director and in accordance with the club's investment guidelines.

The asset allocation strategy in place reflects a more cautious investment risk appetite for Standard UK, Standard Ireland and Standard Asia than for Standard Re. This focusses on maintaining a portfolio which broadly reflects the liability profile in terms of currency and duration, and consists of a diversified range of investments primarily made up of high quality bonds or similar fixed income instruments. Although some more volatile investments including equities are held within Standard UK, the majority of the club's higher yield and more volatile assets are held within Standard Re, which also holds most of the group's capital assets.

These guidelines are reviewed on an annual basis and on an ad-hoc basis if any significant deviations have occurred that affect the financial markets.

e. **Stress and scenario testing**

Investment loss stress tests and scenarios, including consideration of historic scenarios and an inflation shock scenario, are regularly monitored. Standard stress tests include:

- Bond price falls
- Equity market falls
- Currency fluctuations
- Credit spread increases

The club is assessed as being within its risk appetite in relation to each of these scenarios.

C. CREDIT RISK

a. **Material credit risks**

Credit risk relates to the risk that another party fails to perform its financial obligations, or perform them in a timely manner. Counterparty risk arises in relation to members, guarantors, other IG clubs, reinsurers, investments and deposits. Under the risk management system investment counterparty risk is considered within the market risk category. Therefore the most significant credit risks arise from reinsurers, banking counterparties used to hold cash and the premium balances due from members of the club.

A diverse range of high quality reinsurers are used on the reinsurance programme.

Significant amounts of money are held with the custodian bank as money flows in respect of premiums, claims and management fees. The flow is carefully monitored and managed so as to not to exceed tolerance levels.

There are a number of credit controls over the possibility of members financial failure, allowing for the club to offset potential losses. The club continues to closely monitor the credit worthiness of members and collect premiums in good time.

b. **Risk mitigation techniques**

A number of risk mitigation techniques are used to manage reinsurer and IG pool reinsurance credit risk, including:

- Reinsurance is placed with many different reinsurers, reducing the potential impact of individual reinsurer default;
- The reinsurance programme is reviewed and approved by the board on an annual basis;
- All reinsurers are required to be hold a credit rating of A- (Standard & Poor's or equivalent) or better;
- The board receives regular reports on the amounts recoverable from reinsurers;
- The IG pooling agreement includes mechanisms to protect member clubs in the event of the default of one of its members, including securitisation of pool recoverables through Hydra Insurance

Company Limited, the IG members' captive insurer, and minimum solvency and rating requirements for P&I clubs to be included within the pooling agreement.
- No single reinsurer is able to participate more than 15% on any given layer or in total on the GXL programme.
- No single reinsurer is able to participate more than 15% on the non-pool programme.

Risk mitigation techniques used with respect to the club's banking relationships include:

- Maximum counterparty limits with any single banking entity, which may not exceed $50 million at any time and may not exceed $35 million for more than 5 working days;
- Frequent monitoring of bank credit rating.

Risk mitigation techniques used with respect to the club's exposure to outstanding member premium balances include:

- Under the terms of coverage, member claims may be offset against outstanding premiums.
- Overdue premium amounts are monitored and reported to the manager's executive committee on a monthly basis.
- Member cover can be cancelled for non-payment of premium.
- Guarantor security is monitored by the managers' finance committee.

c. **Material risk concentrations and changes in risk profile over the reporting period**

Reinsurance is placed with a range of highly rated reinsurers, with the highest single concentration being due from underwriters at Lloyd's. The potential overall concentration levels are considered when placing reinsurance and the top 10 exposures are reported to the board.

The club has a small number of key banking relationships for handling cash receipts and payments, which may result in material amounts of cash accumulating for short periods of time, for example when member premium payments are received on key due dates.

The club seeks to maintain a diversified member base, reducing the credit concentration risk to any one member. Given the significant risk mitigation in place, member credit risk is considered to be relatively low.

There has been no material change in risk profile over the period.

d. **Stress and scenario testing**

A regular stress test is performed which considers the impact of the failure of a major reinsurer. The club is assessed as being within its risk appetite in relation to this scenario.

D. LIQUIDITY RISK

a. **Material liquidity risks**

Liquidity risk is the risk of failure to maintain sufficient funds to meet obligations as they fall due, for example due to the lack of marketability of investments, inability to make reinsurance recoveries in a timely manner, and incorporating the risk that additional funding may only be secured at excessive cost.

Given the high level of liquid investments held and mechanisms in place to enable quick access to reinsurance recoveries, the risk is considered to be very low.

b. **Risk mitigation techniques**

A number of risk mitigation techniques are used to manage liquidity risk including:

- Asset-liability matching controls are in place, which assist in the club's ability to manage liquidity;
- The investment rules require a significant proportion of the portfolio to be held in easily realisable assets such as highly liquid sovereign debt;
- The club regularly reviews the time period required to liquidate the investment portfolio;
- Principal reinsurance arrangements allow for short period recovery of all significant claims payments due;
- A monitoring process is in place to identify short term potential cash needs in the business;
- The likely cash outflows in relation to specific large claims are projected and kept under review.

c. **Material risk concentrations and changes in risk profile over the reporting period**

Investment assets are administered by a single asset custodian. While investments are required to be held in segregated accounts, there is a risk that in the event of the failure of the custodian there may be delays in accessing funds in a timely manner.

There has been no material change in risk profile over the period.

E. OPERATIONAL RISK

a. **Material operational risks**

Operational risk is the risk of losses incurred as a result of inadequate or failed internal processes, people and systems, or from external events (including legal risks).

Operational risk is considered in terms of seven categories:

- Ineffective Management of Legal and Regulatory Requirements
- Ineffective Management of People Risk and Culture
- Ineffective Cyber Management
- Inadequate Risk Management
- Ineffective Management of Systems
- Poor Data Management or Application
- Ineffective Governance

b. **Risk mitigation techniques**

A number of risk mitigation techniques are in place including:

- Board oversight of service level agreement ("SLA");
- Maintaining professionally-staffed management functions;
- Investment to support recruitment, retention and development of good quality resources;
- Monitoring systems issues, accounting for the need to achieve service objectives and protect data;
- Business continuity planning, including both physical business continuity planning, disaster recovery processes and contingency plans in the event of failure of the outsourced manager;
- Requirement for the managers to maintain errors and omissions insurance;
- Regulatory compliance monitoring;
- Assessment procedures and reports are in place, which are used in the investment and underwriting strategic and business planning processes;
  - The ORSA (own risk and solvency assessment) is used in Europe, under solvency II regulations.
  - The CISSA (commercial insurers solvency self assessment) is used in Bermuda in respect of the Group (and therefore its subsidiaries - Re, Europe and Asia).
- A suite of detection, prevention and recovery controls to protect against malware have been implemented and combined with appropriate user awareness;
- A cyber risk dashboard reported on a quarterly basis to the managers Risk Committee, which shows a sophisticated suite of metrics designed to give comfort that cyber related controls are designed and operating effectively. This includes technical IT security controls (e.g. vulnerability scanning, penetration testing results, access).

A system of incident reporting is in place in order to quickly identify operational failings in order that they may be reported upon and improvement actions put in place in order to reduce the risk of reoccurrence.

c. **Material risk concentrations and changes in risk profile over the reporting period**

Operational risk has been heightened as a result of the global pandemic and the club undergoing a major change project in moving to insourced management - "Palma Project". A "Palma Project" risk and mitigants assessment has identified the following risks:

- Counterparty
- IT/Systems
- Client Relationships

- People/ Culture
- Regulatory/Legal
- Projects impact
- Reputational

Covid-19

The development of the impact of Covid-19 has been monitored closely since March 2020. Full business continuity contingency plans were activated and proved that the club can continue to operate in the event of a serious prolonged incident, such as the present pandemic. Business records and documentation are stored electronically, are regularly backed-up and are accessible remotely from anywhere in the world. Personnel in each of the managers' global offices successfully transitioned to working from home and the club has been able to continue to provide the same level of service to its members.

The impact of Covid-19 on the club's operational risk has been considered in the risk and control self assessment process and management are focussed on monitoring people and culture risk whilst the business operates under a work from home basis. Controls have been reviewed to assess the operational impact on the club. The following risks have been identified:

- Key Person Risk has been identified as an emerging risk. Several members of the senior management team could be potentially exposed to the coronavirus and experience severe symptoms. However, office social distancing measures, succession plans for direct reports to the CEO and identification of emergency deputies for the wider management team (and the CEO) mitigates this risk significantly.
- Culture Risk – risks associated with prolonged periods of working from home have been considered.

Cyber

The club continues to have a strong focus on mitigating the threat from cyber fraud and other cyber related risks. The sophistication of the threat has increased over the period and the club's controls have been strengthened in response. Work is ongoing to ensure the club is compliant with the requirements outlined in the BMA's "Insurance Sector Operational Cyber Risk Management Code of Conduct", in force from January 2021 with compliance to be evidenced by 31 December 2021.

A cyber risk policy was adopted by the board in the October 2019 meeting. This policy requires the establishment of a cyber risk appetite and tolerance under which the board can monitor cyber risk on an ongoing basis.

Data Management

A key project was initiated in 2019/2020 to strengthen the data management framework. Following the initiation of a detailed improvement plan, several new data quality controls have been rolled out in early 2021. The improvement plan has a multi-year timeframe with further data quality enhancements expected over 2021 and 2022.

d. **Stress and scenario testing**

A range of operational risk stress and scenario tests are performed in order to understand the potential impact of potential operational issues. The most significant scenarios identified include:

- Cyber attack – ransomware
- Rogue chief financial officer
- Covid-19 Worst Case
- Post Brexit Operational Model

The club is assessed as being within its risk appetite in relation to the above scenarios.

IV. SOLVENCY VALUATION

a. **Valuation bases, assumptions and methods to derive the value of each asset class**

The club has used the valuation principles outlined by Bermuda Monetary Authority's "Guidance Note for Statutory Reporting Regime" for the reporting period's statutory filing. The economic valuation principles outlined in this document are to measure assets and liabilities on a fair value basis (which is the value that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between open market participants at the measurement date). The fair value principles used for the assets are as follows:

- Cash and cash equivalents – these are valued at the amount held at period end date. Foreign currencies are translated at the US dollar rate of exchange at the balance sheet date.
- Investments – these are valued at market price at period end provided by the club's custodian, Northern Trust. The club uses Bloomberg to ascertain that investments are traded in active markets and hold no over the counter assets requiring modelling in the portfolio.
- Accounts and premium receivables – these are valued at cost less any provision for impairment in value. Premium receivable from members recognised as insurance receivables under UK GAAP, forms part of the best estimates technical provision in the EBS. See section b below on the valuation of technical provisions.
- Reinsurance balances receivable – these are valued at cost less any provision for impairment in value.
- Fixed assets - are stated at historic purchase cost less accumulated depreciation. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use.

b. **Valuation bases, assumptions and methods to derive the value of technical provisions**

The calculation of the technical provisions starts with the GAAP reserves and proceeds in a number of stages:

- Any prudence in the GAAP reserves is removed to arrive at a 'best estimate'.
- An explicit additional allowance is made for events not in data ("ENIDs"): large events that have not happened in the past (so are not in the basic reserves) but might happen in the future.
- An allowance is made for the expenses, both external and internal, of settling the claims. A claims handling expense ("CHE") allowance is already included in the GAAP reserves, however the methodology for calculating this allowance differs under EBS, because it allows for activities of administration, training, management etc. in addition to pure claims settlement activity.
- An allowance is made for reinsurance bad debt. The managers use the credit ratings of the club's reinsurers and default rates published by S&P to estimate the cost of reinsurer defaults over the future lifetime of the claims.
- Reclassification of insurance receivables. Premium debt that is due after the balance sheet date (being the third instalment of poolable premium that is due 9 months after the year-end) is included as a debtor balance in the GAAP balance sheet but forms part of the claims provision on the EBS balance sheet.
- Time value of money. While the GAAP reserves take credit for the time value of money on the asbestos reserves, under EBS discounting is applied to all cash flows for all classes of business.
- 'Premium provisions' are added, on the same basis, for premiums, claims and expenses in respect of future exposures that the club has already agreed to underwrite.
- Risk margin. A risk margin is included to allow for the cost of funding the solvency capital required to support the reserves until they fully run off.

At 20 February 2021, the total Technical Provisions amounted to $576m (2020: $625m) net of reinsurance comprising the following (reported in thousand units):

Technical Provision	2021 Net (US$ '000)	2020 Net (US$ '000)
Best Estimate Loss and Loss Expense Provision	**534,733**	585,029
Best Estimate Premium Provision	**(3,986)**	(12,073)
Risk Margin	**45,489**	52,447
Total	**576,236**	625,403

The reduction from February 2020 is largely due to the removal of the club's exposure to its Lloyds syndicate from the balance sheet.

c. **Description of recoverable balances from reinsurance contracts**

The main elements of the reinsurance recoverable balance are in respect of (a) recoveries on pooled business from the International Group pooling arrangement, which includes recoveries from pool members and from external excess-of-loss reinsurers; and (b) recoveries on non-pooled business from external excess-of-loss reinsurers.

There are no material changes in the relevant assumptions made in the calculation of technical provisions compared to the previous reporting period.

d. **Valuation bases, assumptions and methods to derive the value of other liabilities**

Similar to the valuation principles for assets, the club's liabilities follow the valuations principles outlined by Bermuda Monetary Authority's "Guidance Note for Statutory Reporting Regime".

- Insurance and reinsurance balances payables – these are valued at cost less any provision for impairment in value.
- Accounts payables and accrued liabilities – these are valued at cost less any provision for impairment in value.
- Derivative instruments – these are valued at quoted market prices. In the absence of an active market, prices are based on observable market inputs.
- Any other liabilities – these are valued at cost less any provision for impairment in value. Accrued expenses are included on an accrual basis.

e. **Any other material information**

No additional material information to report.

V. CAPITAL MANAGEMENT

a. **Eligible capital**

i. Capital management policy and process for capital needs, how capital is managed and material changes during the reporting period

The club and board's tolerance for risk is limited by the desire to minimise the chance of making unbudgeted calls on the club's membership, and so the club seeks to maintain sufficient capital such that the chance of a supplementary call or other similar material mitigating action is less than 10% over a 12 month time horizon. Own funds are well in excess of regulatory capital requirements.

In addition one of the club's goals is to provide first class financial security to its membership, including maintaining a 'AAA' capital strength rating with Standard and Poor's, and so any decisions around premium returns or underwriting rate rises are made in the context of ensuring UK GAAP net assets remain above the capital level.

Another goal of the club (which supports maintaining capital strength) is to aim for breakeven underwriting, so ensuring the maintenance of the level of own funds.

There were no material changes during the reporting period.

ii. Eligible capital categorised by tiers in accordance to the eligible capital rules used to meet ECR and MSM requirements of the Insurance Act

At the end of the reporting period, the group's Eligible Capital for its Minimum Margin of Solvency (MSM) and Enhanced Capital Requirement (ECR) was categorised as follows:

Eligible Capital	**2021 MSM (US$ '000)**	**2021 ECR (US$ '000)**	2020 MSM (US$ '000)	2020 ECR (US$ '000)
Tier 1	**303,307**	**303,307**	345,557	345,557
Tier 2	**45,496**	**45,496**	52,138	52,138
Tier 3	**-**	**-**	-	-
Total	**348,803**	**348,803**	397,695	397,695

The majority of capital is Tier 1, the highest quality capital, consisting of contributed surplus, and statutory surplus. Tier 2 capital consists of ancillary own funds of $45.5m (2020: 52.1). Further information on the ancillary own funds is in section v. Identification of ancillary capital instruments approved by the Authority. The group does not have any Tier 3 capital.

iii. Confirmation of eligible capital that is subject to transitional arrangements

There is no eligible capital subject to transitional arrangements.

iv. Identification of any factors affecting encumbrances on the availability and transferability of capital to meet the ECR

None identified.

v. Identification of ancillary capital instruments approved by the Authority

The club's Tier Two ancillary own funds are $45.5m, recognising the ability of the club to make unbudgeted supplementary calls (capped at 15% of Tier 1 capital). The club obtained approval from the BMA for the use of the ancillary own funds on 16 October 2019 for the period from 1 March 2019 to 20 February 2022. The ancillary own funds are calculated as below:

[ETP*M*R], subject to the calculated amount not exceeding 15% of Available Economic Capital and Surplus;

Where:

ETP (estimated total premium) is defined as the amount of mutual premium agreed with the members at inception of each open policy year gross of reinsurance less mutual premium for which release calls have been paid. There are always three open policy years so the calculation applies to all three years;

M is defined as a factor of 0.3 during the current year (first year), 0.25 during the following year (second year) and 0.20 during the year thereafter (third year). These factors reflect the loss absorbing capacity of the ancillary capital;

R is defined as a factor of 0.65. This represents a 0.1 factor deduction for default risk and a 0.25 factor deduction for liquidity risk;

vi. Identification of differences in shareholder's equity as stated in the financial statements versus the available capital and surplus

Differences relate to the impact of employing statutory-based technical provision valuation techniques as summarised below:

Reconciliation - UK GAAP to EBS	2021 Capital and Surplus (US$ '000)	2020 Capital and Surplus (US$ '000)
UK GAAP capital and surplus	**360,300**	393,700
Tier 2 ancillary funds	**45,496**	51,873
Technical provision adjustments (excluding risk margin	**(11,504)**	4,568
Risk Margin	**(45,489)**	(52,447)
BMA EBS capital and surplus	**348,803**	397,695

b. **Regulatory capital requirements**

i. ECR and MSM requirements at the end of the reporting period

The group's regulatory capital requirements at 20 February 2021 were assessed as follows:

Requirement	2021 (US$ '000)	2020 (US$ '000)
Minimum Margin of Solvency	**81,010**	82,369
Enhanced Capital Requirement	**228,046**	229,081

ii. Identification of any non-compliance with the MSM and the ECR

The group was compliant with the MSM and ECR requirement at the end of the reporting period.

iii. A description of the amount and circumstances surrounding the non-compliance, the remedial measures and their effectiveness

Not applicable.

iv. Where the non-compliance is not resolved, a description of the amount of the non-compliance

Not applicable.

c. **Approved internal capital model**

i. Description of the purpose and scope of the business and risk areas where the internal model is used

Not applicable - the club has not applied to have its internal capital model approved to determine regulatory capital requirements.

ii. Where a partial internal model is used, description of the integration with the BSCR model

Not applicable.

iii. Description of methods used in the internal model to calculate the ECR

Not applicable.

iv. Description of aggregation methodologies and diversification effects

Not applicable.

v. Description of the main differences in the methods and assumptions used for the risk areas in the internal model versus the BSCR model

Not applicable.

vi. Description of the nature & suitability of the data used in the internal model

Not applicable.

vii. Any other material information

Not applicable.

viii. Significant and subsequent events

Not applicable.