Powers exercised

A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):  

1. section 138 (General rule-making power);  
2. section 141 (Insurance business rules);  
3. section 150(2) (Actions for damages);  
4. section 156 (General supplementary powers);  
5. section 157(1) (Guidance);  
6. section 316 (Direction by Authority); and  
7. section 340 (Appointment).

B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

C. This instrument comes into force as follows:  

1. the amendments in Annex G, Part 2 come into force on 1 January 2006;  
2. LLD 18.2.1R(1) as it applies PRU 1.2.22R to managing agents in Annex M comes into force on 1 January 2006;  
3. the amendment to the Glossary definition of "IPRU(INS)" in Annex V comes into force on 31 December 2004;  
4. the remainder of this instrument comes into force on 1 January 2005.

Amendments to the Lloyd's sourcebook

D. The Lloyd's sourcebook is amended as follows:  

1. the chapters of the Lloyd's sourcebook listed in column (1) of the following table are amended in accordance with the Annexes in column (2):

<table>
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(2) by inserting as new chapters and sections as listed in column (1) of the following table the provisions in the Annex listed in column (2):

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Amendments to the Supervision manual

E. The Supervision manual is amended in accordance with Annex U to this instrument.

Amendments to the Glossary

F. The Glossary is amended in accordance with Annex V to this instrument.

Citation

G. This instrument may be cited as the Lloyd's Sourcebook (Integrated Prudential and Auditing and Actuarial Requirements) Instrument 2004.

By order of the Board
16 December 2004
Annex A

Amendments to the Lloyd's sourcebook, Table of Contents

In this Annex, underlining indicates new text and striking through indicates deleted text.

LLD Contents

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Annex B

Amendments to the Lloyd's sourcebook, Chapter 1

In this Annex, underlining indicates new text and striking through indicates deleted text.

1 Society's regulatory functions

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1.2 Carrying out the Society's regulatory functions

Delegation

…

Disciplinary arrangements

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Dealing with the FSA

1.2.7 G [deleted]
[Delete LLD 1.2.7G in its entirety; the deleted text is not shown struck through.]

1.2.8 G [deleted]
[Delete LLD 1.2.8G in its entirety; the deleted text is not shown struck through.]

1.2.9 G [deleted]
[Delete LLD 1.2.9G in its entirety; the deleted text is not shown struck through.]

1.3 Conflicts of interest [deleted]
[Delete LLD 1.3 in its entirety; the deleted text is not shown struck through.]

1.4 Confidential regulatory information

1.4.1 G [deleted]
[Delete LLD 1.4.1G in its entirety; the deleted text is not shown struck through.]
Annex C

Amendments to the Lloyd's sourcebook, Chapter 2

In this Annex, underlining indicates new text and striking through indicates deleted text.

2 Provision of information

…

2.6 Information about the Society's byelaws [deleted]

[Delete LLD 2.6 in its entirety; the deleted text is not shown struck through.]
Annex D

Amendments to the Lloyd's sourcebook, Chapter 9

In this Annex, underlining indicates new text and striking through indicates deleted text.

9 Prudential requirements for the Society [deleted]

[Delete LLD 9 in its entirety; the deleted text is not shown struck through.]
Annex E

Amendments to the Lloyd's sourcebook, Chapter 10

In this Annex, underlining indicates new text and striking through indicates deleted text.

10 Insurance operational risk [deleted]

[Delete LLD 10 in its entirety; the deleted text is not shown struck through.]
Annex F

Amendments to the Lloyd's sourcebook, Chapter 11

In this Annex, underlining indicates new text and striking through indicates deleted text.

11 Required margins of solvency  [deleted]

[Delete LLD 11 in its entirety; the deleted text is not shown struck through.]
Annex G

Part 1

Amendments to the Lloyd's sourcebook, Chapter 12

In this Part, underlining indicates new text and striking through indicates deleted text.¹

12 Determination of liabilities

12.1 Application and purpose

…

12.2 Requirement to determine liabilities [deleted]

[Delete LLD 12.2 in its entirety; the deleted text is not shown struck through.]

…

12.3 Members' liabilities

12.3.1 R For open syndicate years, a member's liabilities are the aggregate of:

(1) his proportionate share of the liabilities of each open syndicate year in which he participates, including:

(a) liabilities associated with earlier syndicate years that have been closed into that year; and

(b) any equalisation reserve allocated to him for the syndicate year by the Society under LLD 12.2.5G; and

(2)

At stage (e) of PRU 2.2.14R the Society must deduct from a member’s capital resources a negative valuation difference being, for each member, (for open syndicate years through which the member carries on general insurance business taken together), if A+B exceeds C, A+B-C, where:

(1)(a) A is the total of the member's proportionate shares for each syndicate year of the accumulated excess of income over outgoings;

(2)(b) B is the amount of any unpaid additional contributions the

¹ The amendments to LLD 12 set out in this Part 1 take effect on 1 January 2005 until 31 December 2005. Further amendments taking effect on 1 January 2006 are set out in Part 2.
member is required to make to the funds maintained for the syndicate years by the managing agents; and

(3)(e) C is the total of his member's proportionate shares of the liabilities net of reinsurance recoveries.

12.3.2 R For the purpose of LLD 14.3 PRU 4.2.52G to 4.2.56G (Currency matching of assets and liabilities) and PRU 7.2.30R (Localisation (UK firms only)), the amounts in-

(1) LLD 12.3.1R(2) LLD 12.3.1R, which are intended to prevent the premature release of profits, and

(2) LLD 12.2.4R (the equalisation reserve);

may be left out of account.

12.3.3 R [deleted]
[Delete LLD 12.3.3R in its entirety; the deleted text is not shown struck through.]

12.3.4 R [deleted]
[Delete LLD 12.3.4R in its entirety; the deleted text is not shown struck through.]

12.4 General insurance business technical provisions [deleted]
[Delete LLD 12.4 in its entirety; the deleted text is not shown struck through.]

12.5 Long-term liabilities [deleted]
[Delete LLD 12.5 in its entirety; the deleted text is not shown struck through.]
Annex G

Part 2

Amendments to the Lloyd's sourcebook, Table of Contents and Chapter 12

In this Part, underlining indicates new text and striking through indicates deleted text.\(^2\)

The Lloyd's sourcebook, Table of Contents is amended as follows:

LLD Contents

Lloyd’s

...\[
\begin{array}{ll}
\text{LLD12} & \text{Determination of liabilities [deleted]} \\
12.1 & \text{Application and purpose} \\
12.2 & \text{[deleted]} \\
12.3 & \text{Members’ liabilities} \\
12.4 & \text{[deleted]} \\
12.5 & \text{[deleted]} \\
\end{array}
\]

...

The Lloyd's sourcebook, Chapter 12 is amended as follows:

12  

\text{Determination of liabilities [deleted]} \\
[Delete \text{LLD 12} in its entirety; the deleted text is not shown struck through.]

\(^2\) The amendments to LLD 12 set out in this Part 2 take effect on 1 January 2006.
In this Annex, underlining indicates new text and striking through indicates deleted text.

13 Assets: valuation and realisability risk [deleted]

[Delete LLD 13 in its entirety; the deleted text is not shown struck through.]
Annex I

Amendments to the Lloyd's sourcebook, Chapter 14

In this Annex, underlining indicates new text and striking through indicates deleted text.

14 Assets: market and credit risk [deleted]

[Delete *LLD* 14 in its entirety; the deleted text is not shown struck through.]
In this Annex, underlining indicates new text and striking through indicates deleted text.

LLD 15: Reporting by the Society

[Change to title of the chapter]

LLD 15: Reporting by the Society

15.1 Application and purpose

Application

15.1.1 R This chapter applies to the Society and to managing agents.

15.1.4 G This chapter requires the Society to report on the insurance business carried on by members and on the assets and liabilities of members and the Society. It also requires managing agents to report on the insurance business carried on through each syndicate they manage. Reporting at syndicate level is required to enable the Society to prepare the Lloyd's Return.

15.1.5 G The Lloyd's Return is made annually and contains the statement required from the Society that it has maintained the margin of solvency required under LLD 11 (Required margin of solvency) capital resources equivalent to its capital resources requirement under PRU. This does not absolve the Society from the obligation to maintain the required margin of solvency—capital resources equivalent to its capital resources requirement at all times.

15.2 Requirement to report to the FSA

15.2.2 R The report in LLD 15.2.1R must be prepared in accordance with LLD 9.4.1R PRU 1.3.5R and this chapter.

15.3 Content and form of the Lloyd's Return

15.3.1 R In preparing the Lloyd's Return, the Society must:

(1) complete the forms in LLD 15 Ann 1R, subject to LLD 9 to LLD 15 to LLD 25.

(a) following the requirement of and making the disclosures required under Appendices 9.1, 9.2, 9.3 and 9.4 of
(b) having regard to Guidance Note 9.1 of \textit{IPRU(INS)};

as if in the documents referred to in (a) and (b) those Appendices references to an \textit{insurer} were references to the \textit{Society} and \textit{members}, and adapting the requirements in (a) and the guidance in (b) those Appendices where necessary;

(2) …

15.4.7 G Further guidance on risk groups and country classification is in \textit{IPRU(INS)}, Guidance Note 9.1, paragraph 9.4. [deleted]

15.8 Additional information …

15.8.1 R …

(8) the circumstances surrounding the use of any \textit{derivative} contract held at any time during the \textit{financial year} which did not fall within \textit{LLD 13.6.1R}; fulfil the criteria outlined in PRU 4.3.5R; and

15.8.5 R …

(2) for each of the realistic disaster scenarios set by the \textit{Society} under \textit{LLD 10.6} when fulfilling its obligation under PRU to monitor aggregation of risk within the Lloyd's market of the contribution it is assumed each such reinsurer would provide in the event of that disaster occurring.

15.9 Certificates and audit report …

15.9.1 R (4) an abstract from the \textit{syndicate actuary} of each \textit{syndicate} which carries on \textit{long-term insurance business} of the actuary's report made under \textit{LLD 10.9.4R}(2)(b) SUP 4.6.14R(2).

New text to be inserted into LLD Chapter 15 after LLD 15.12

15.13 Syndicate-level reporting

15.13.1 R Each \textit{managing agent} must:

(1) prepare a return for each \textit{financial year} in respect of the \textit{insurance business} carried on through each \textit{syndicate} managed by it; and
(2) __________ provide the return in (1) to the Society as soon as practicable after the end of the financial year but in any event in time to enable the Society to report to the FSA in accordance with LLD 15.2.1R.

15.13.2 R The Society must:

(1) issue instructions to managing agents setting out the form and content of the return under LLD 15.13.1R; and

(2) issue the instructions in (1) as soon as practicable but in any event in time to enable managing agents to comply with LLD 15.13.1R.

15.13.3 R A managing agent must annex to each return which it prepares under LLD 15.13.1R, a certificate signed by the persons referred to in LLD 15.13.4R, including the statements required by LLD 15.13.5R.

15.13.4 R The certificate in LLD 15.13.3R must be signed by:

(1) where there are more than two directors of the managing agent, at least two of those directors and, where there are not more than two directors, all the directors; and

(2) a chief executive, if any, of the managing agent or (if there is no chief executive) the secretary.

15.13.5 R Table

<table>
<thead>
<tr>
<th></th>
<th>The certificate in LLD 15.13.3R must state that:</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>(1) the return has been properly prepared in accordance with the instructions referred to in LLD 15.13.2R;</td>
</tr>
<tr>
<td></td>
<td>(2) proper accounting records have been maintained and adequate information has been obtained by the managing agent;</td>
</tr>
<tr>
<td></td>
<td>(3) an appropriate system of control has been established and maintained by the managing agent over the syndicate’s transactions and records;</td>
</tr>
<tr>
<td></td>
<td>(4) in relation to the statement by the syndicate actuary of a syndicate carrying on long-term insurance business required by LLD 15.9.1R(3):</td>
</tr>
<tr>
<td></td>
<td>(a) proper accounts and records have been maintained for the purpose of preparing the statement, and</td>
</tr>
<tr>
<td></td>
<td>(b) the information given has been ascertained in</td>
</tr>
</tbody>
</table>
conformity with *LLD* 15 Annex 4R.

15.13.6 R  A *managing agent* must ensure for each *syndicate* managed by it that the return required under *LLD* 15.13.1R is examined and reported on by the *syndicate* auditor.

15.13.7 R  A *managing agent* must annex to each return required under *LLD* 15.13.1R an audit certificate provided by the *syndicate* auditor including the statements required by *LLD* 15.13.8R.

15.13.8 R  Table

<table>
<thead>
<tr>
<th>1</th>
<th>The certificate in <em>LLD</em> 15.13.7R must state:</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>that in the auditors’ opinion, the return has been properly prepared in accordance with the instructions referred to in <em>LLD</em> 15.13.2R;</td>
</tr>
<tr>
<td>(2)</td>
<td>that according to the information and explanations that the auditors have received:</td>
</tr>
<tr>
<td>(a)</td>
<td>in their opinion, the certificate required to be signed in accordance with <em>LLD</em> 15.13.3R (other than statements to which paragraph 1(3) relates) has been properly prepared in accordance with the instructions; and</td>
</tr>
<tr>
<td>(b)</td>
<td>it was or was not unreasonable for the <em>persons</em> giving the certificate to have made the statements in it (other than statements to which paragraph 1(3) relates);</td>
</tr>
<tr>
<td>(3)</td>
<td>the extent to which, in giving their opinion, the auditors have relied, in respect of <em>long-term insurance business</em>, on the work of the <em>syndicate actuary</em>.</td>
</tr>
</tbody>
</table>

2  The audit opinion required by paragraph 1 does not extend to cover information on major treaty reinsurers or major facultative reinsurers.

3  To the extent that the information and explanations they have received do not allow the auditors to express an opinion as to whether it was or was not unreasonable for the persons giving the certificate required to be signed in accordance with *LLD* 15.13.3R to have made the statements therein, the auditors must add to their report such qualification, amplification or explanation as may be appropriate.
Annex K

Amendments to the Lloyd's sourcebook, Chapter 16

In this Annex, all the text is new and is not underlined.

16  General provisions applying PRU to Lloyd's

16.1  Section 150 of the Act (Actions for damages)

16.1.1  R  A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

16.2  Application

16.2.1  R  This chapter applies to:

(1)  the Society; and

(2)  managing agents.

Purpose

16.2.2  G  The purpose of this chapter is to:

(1)  set out specific requirements for the prudential management of the insurance business of Lloyd's members, including management of the assets supporting that business; and

(2)  clarify how PRU rules and guidance are to apply to the insurance business of Lloyd's members.

16.2.3  G  Members bear the risk in respect of their insurance business and so it is their responsibility to hold financial resources to support that business. A member participates on a several basis, for its own account. In practice managing agents manage the business and the Society manages the market. Should a member hold insufficient financial resources, the Society's own assets may be used to support that member's business.

16.3  Application of PRU to the Society and managing agents

16.3.1  R  If a provision in PRU applies to the Society "in accordance with" this rule, the Society must:

(1)  manage each member's funds at Lloyd's;
(2) manage its central assets; and

(3) supervise the insurance business carried on by each member at Lloyd's;

so as to achieve in relation to those assets and that insurance business the same effect as the relevant PRU provision would have (that is, conforming with the requirements of any rule and taking appropriate account of any applicable guidance,) when applied to a firm or to the insurance business of a firm.

16.3.2 G The Society is subject to PRU rules in respect of the insurance business of each Lloyd's member. These include rules in respect of:

(1) the calculation of the capital resources requirements for each member;

(2) the financial resources it manages on behalf of members; and

(3) the Society's own financial resources.

16.3.3 R If a provision in PRU applies to a managing agent "in accordance with" this rule, the managing agent must, in relation to each syndicate managed by it and for each syndicate year, manage:

(1) the syndicate assets; and

(2) the insurance business carried on by the members of the syndicate through that syndicate;

so as to achieve in relation to those assets and that insurance business the same effect as the relevant PRU provision would have (that is, conforming with the requirements of any rule and taking appropriate account of any applicable guidance,) when applied to a firm or to the insurance business of a firm.

16.3.4 G Syndicate membership may change from year to year or it may remain constant. Managing agents are required to apply PRU to the insurance business carried on through each syndicate for each syndicate year. This should ensure that PRU is applied to Lloyd's in a way that is consistent with the provision of capital to support the insurance business underwritten.

16.3.5 G Where common systems and controls or processes are appropriate for all the insurance business carried on through more than one syndicate year, a single response may be adequate for all syndicate years. However, in some cases it will be important to consider the business of each open syndicate year separately, particularly for quantitative rules. For example, it is important that managing agents separately assess the financial resources (including capital) that are required and are available to support the insurance business carried on through each syndicate year, where the syndicate membership changes from year to year. This is because each member's assets are only available to support its own business, so the assets
supporting one year of account may not be available to support another. For example, if a managing agent were to assess the financial requirements of two or more syndicate years together where the capital structure had changed, there would be a risk that the managing agent might take account of diversification effects that were not reflected in the capital supporting the insurance business.

16.3.6 G There is no requirement on managing agents to carry out separate individual capital assessments for syndicates for each syndicate year. Managing agents are required to carry out individual capital assessments for each syndicate as if that syndicate were a firm; this would normally be on the basis of a going concern but, just as in a firm, account needs to be taken of any restrictions on the availability of assets (e.g. deposits with cedants), and some account needs to be taken of changes in the capital participation in the syndicate. The Society is responsible for the individual capital assessment for each member, which must take into account the assessments made by managing agents of any syndicates on which the member participates. PRU 2.3 contains rules and guidance on the assessment of capital adequacy for firms and LLD 19.4.1R to LLD 19.4.24R provide for the application of PRU 2.3 to the Society and managing agents.

16.4 Summary of application of PRU to Lloyd's

16.4.1 G Table: Key PRU requirements for Lloyd's

<table>
<thead>
<tr>
<th>Key PRU requirements</th>
<th>PRU</th>
<th>LLD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk management, systems and controls</td>
<td></td>
<td></td>
</tr>
<tr>
<td>The Society to establish and maintain systems and controls</td>
<td></td>
<td>17.4</td>
</tr>
<tr>
<td>to address risks affecting the Lloyd's market</td>
<td></td>
<td></td>
</tr>
<tr>
<td>The Society to establish and maintain systems and controls</td>
<td>1.4, 3.1, 4.1, 5.1 &amp; 6.1</td>
<td>17.4, 18.4, 20.2, 21.2, 22.2 &amp; 23.2</td>
</tr>
<tr>
<td>for the management of prudential, credit, market, liquidity and operational risks affecting funds at Lloyd's and central assets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Managing agents to establish and maintain systems and controls for the management of prudential, credit, market, liquidity, operational, and insurance risks affecting each syndicate</td>
<td>1.4, 3.1, 4.1, 5.1, 6.1 &amp; 7.1</td>
<td>17.4, 18.4, 20.2, 21.2, 22.2, 23.2 &amp; 24.2</td>
</tr>
<tr>
<td>Adequacy of financial resources</td>
<td></td>
<td></td>
</tr>
<tr>
<td>The Society to ensure that members' financial resources are adequate</td>
<td>1.2</td>
<td>18.2</td>
</tr>
<tr>
<td><strong>Members</strong> taken together to maintain adequate financial resources in respect of the <em>insurance business</em> conducted at Lloyd's</td>
<td>18.2</td>
<td></td>
</tr>
<tr>
<td>---</td>
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<td></td>
</tr>
<tr>
<td><strong>Managing agents</strong> to ensure that financial resources are adequate for each <em>syndicate</em></td>
<td>1.2</td>
<td>18.2</td>
</tr>
<tr>
<td><strong>Valuation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The <em>Society</em> and <em>managing agents</em> to apply generally accepted accounting principles to valuing assets, liabilities, equity and income statement items for the purposes of the <em>rules</em> and <em>guidance</em> in <em>LLD</em> and <em>PRU</em> unless the contrary is expressly stated</td>
<td>1.3 &amp; 4.3</td>
<td>18.3 &amp; 21.4</td>
</tr>
<tr>
<td><strong>Capital resources requirements</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The <em>Society</em> to calculate the <em>MCR</em> in respect of the <em>general insurance business</em> of each <em>member</em></td>
<td>2.1</td>
<td>19.2</td>
</tr>
<tr>
<td>The <em>Society</em> to calculate the <em>CRR</em> (higher of <em>MCR</em> and <em>ECR</em>) in respect of the <em>long-term insurance business</em> of each <em>member</em></td>
<td>2.1</td>
<td>19.2</td>
</tr>
<tr>
<td><strong>Capital resources</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The <em>Society</em> and <em>managing agents</em> to calculate <em>capital resources</em> in accordance with the <em>rules</em> and <em>guidance</em> in <em>LLD</em> and <em>PRU</em></td>
<td>2.2</td>
<td>19.3</td>
</tr>
<tr>
<td><strong>Adequacy of capital resources</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>Managing agents</em> to assess the adequacy of <em>capital resources</em> held at <em>syndicate</em> level in respect of <em>insurance business</em> carried on through each <em>syndicate</em> (annual ICA for each <em>syndicate</em>)</td>
<td>2.3</td>
<td>19.4</td>
</tr>
<tr>
<td>The <em>Society</em> to assess the adequacy of <em>capital resources</em> available to support each <em>member's insurance business</em> (ICA for each <em>member</em>), both at <em>syndicate</em> level (taking account of <em>syndicate ICAs</em>), and as <em>funds at Lloyd's</em></td>
<td>2.3</td>
<td>19.4</td>
</tr>
</tbody>
</table>
Annex L
Amendments to the Lloyd's sourcebook, Chapter 17

In this Annex, all the text is new and is not underlined.

17 Special provisions for Lloyd's
17.1 Section 150 of the Act (Actions for damages)
17.1.1 R A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

17.2 Management of insurance business
17.2.1 R Neither the Society nor managing agents may permit a member to carry on any insurance business except as a participant on one or more syndicates.

17.2.2 G LLD 17.2.1R ensures that any insurance business carried on by members is subject to appropriate FSA requirements.

17.3 Obligations under PRU
17.3.1 R The Society must ensure that all participants in the Lloyd's market are made aware of their obligations under PRU.

17.3.2 G The application of PRU to Lloyd's is effected in LLD 16 to LLD 24. SUP Appendix 2 is applied to Lloyd's in LLD 25. Further requirements relevant to the Society's general responsibilities with regard to the market are contained in LLD 1 to LLD 8A and LLD 17. Requirements relevant to managing agents and other participants and advisers in relation to the Lloyd's market are contained elsewhere in the Handbook.

17.4 Management of risk
17.4.1 R The Society must establish and maintain systems and controls to enable it appropriately to address the risks to which the Lloyd's market is exposed.

17.4.2 G As well as the risks that are common to other firms, there are significant risks in the Lloyd's market arising out of its structure and the inter-relationships between the entities involved. The risks include aggregations of risk in the market. The Society should ensure that the systems and controls required by LLD 17.4.1R enable it to identify, monitor and manage those risks.

17.4.3 R The systems and controls in LLD 17.4.1R must include systems and controls to enable the Society to ensure that any assumptions made in calculating a
member's capital resources or in determining the individual capital assessment for each member are regularly reviewed and that appropriate action is taken if any assumption is no longer valid.

17.4.4 R The Society must take all reasonable steps, including establishing and maintaining adequate systems and controls to enable it:

(1) to manage the risks to which funds at Lloyd's and central assets are exposed; and

(2) to ensure that funds at Lloyd's and central assets are adequate to support all balancing amounts.

17.4.5 G In complying with LLD 17.4.4R the Society should take appropriate account of effects such as diversification and concentrations.

17.4.6 R A managing agent must establish and maintain adequate systems and controls to manage the risks to which the insurance business carried on through each syndicate it manages is exposed.

17.4.7 R In complying with LLD 17.4.6R a managing agent need not take account of risks associated with assets that are not syndicate assets.

17.4.8 R The Society must take reasonable steps to ensure that systems and controls established and maintained by managing agents are adequate to ensure that risks to which the insurance business carried on through each syndicate is exposed do not have a detrimental effect on funds at Lloyd's or central assets.

17.4.9 G Managing agents and the Society each hold and manage some of the financial resources held to support the insurance business carried on through syndicates. In particular:

(1) the Society holds and manages funds at Lloyd's and central assets which must be held to support balancing amounts. The Society is required to manage the risks that affect funds at Lloyd's and central assets directly, once the effects of any aggregation and diversification have been taken into account;

(2) managing agents hold and manage some of the financial resources in respect of the insurance business carried on through each syndicate that they manage. Managing agents are required to manage all risks affecting a syndicate except for the risk that funds at Lloyd's and central assets are not available to support the balancing amount.

17.4.10 G Should the Society intend to exercise any power it may have to prescribe a course of action for a managing agent which the managing agent might reasonably consider to be inconsistent with the interests of any member whose insurance business it manages, the Society should:

(1) consult any affected member, where practical in advance; and
(2) in accordance with PRIN 11 (Relations with regulators), LLD 2 and, to enable the FSA to comply with section 314 of the Act (Authority's general duty), consider whether it should notify the FSA.

Group risk and conflicts of interest

17.4.11  Many entities operating within the Lloyd's market are part of a corporate group, including the Society, certain managing agents and members. Those entities are subject to group risk arising from their own corporate group and, depending on the relationships within their own group, may be subject to FSA systems and controls requirements or group risk requirements. The rules and guidance in this section are intended to ensure that sufficient systems and controls are in place to protect policyholders and potential policyholders from such risks. The Society is also subject to the risk of wider conflicts of interest or the appearance of conflicts of interest in carrying out the Society's regulatory functions. LLD 17.4.13R(1) requires the Society to monitor and manage those risks.

17.4.12  In complying with LLD 17.4.6R, managing agents should have particular regard to:

(1) transactions which may give rise to a conflict of interest, such as those to which the counterparties are:

(a) other members of the managing agent's own group;

(b) any members of any syndicates managed by the managing agent; or

(c) any entity that is part of a group to which one or more members of any syndicates managed by the managing agent belong; and

(2) transactions involving:

(a) the provision of capital;

(b) the provision of reinsurance; or

(c) the provision of other services.

17.4.13  The Society must establish and maintain effective arrangements to monitor and manage risk arising from:

(1) conflicts of interest (including in relation to (2) to (4));

(2) inter-syndicate transactions, including reinsurance to close and approved reinsurance to close;

(3) related party transactions; and
transactions between members and itself.

17.4.14 R The arrangements in LLD 17.4.13R must enable the Society to identify any significant overstatement of financial resources resulting from any transaction falling within LLD 17.4.13R (2) to (4), including as a result of:

(1) any differences in the amounts recorded as due or payable by each party to any such transaction; or

(2) any actual or likely disputes between the parties to any such transaction.

17.4.15 R If the Society identifies a significant overstatement of the kind referred to in LLD 17.4.14R, it must ensure that an appropriate adjustment is made, including if appropriate by a deduction from or reduction in the value attributed to:

(1) the capital resources of any member concerned; or

(2) the Society's capital resources.

17.4.16 G In complying with LLD 17.4.14R and LLD 17.4.15R, the Society should consider the significance of any overstatement with regard to the value of the Society's capital resources that are not required to cover shortfalls in a member's capital resources.

17.5 Approved reinsurance to close

17.5.1 G As defined in the Glossary, "approved reinsurance to close" excludes:

(1) reinsurance between parties other than members; and

(2) balance transfers between syndicate years of syndicates having only one member, which have no effect on the overall liabilities of that member.

17.5.2 G The "approved" status of an approved reinsurance to close does not alter the legal status or effect of the original contract of insurance, or the liability of a reinsured member to the policyholder under or in respect of the original contract of insurance.

17.5.3 R Notwithstanding that the liability of a reinsured member to a policyholder is unaffected by an approved reinsurance to close as described in LLD 17.5.2G, for the purposes of PRU only:

(1) a contract of insurance reinsured under an approved reinsurance to close must be treated as if the reinsuring member and not the reinsured member had effected the original contract of insurance; and

(2) any payment received by a member as consideration for or in connection with an approved reinsurance to close must be treated as
a Lloyd's member's contribution and not as premium or as a reinsurance recovery.

17.6 Provision of information by managing agents

17.6.1 R A managing agent must, as soon as possible, give the Society any information the managing agent has concerning material risks to funds at Lloyd's or central assets.

17.6.2 R A managing agent need not comply with LLD 17.6.1R if the managing agent knows that the Society already has the relevant information.

17.7 Insurance receivables to be carried to trust funds

17.7.1 R The Society must take all reasonable steps to ensure that each member:

(1) executes the appropriate Lloyd's trust deeds; and

(2) carries to the appropriate Lloyd's trust fund all amounts received or receivable by the member, or on its behalf, in respect of any insurance business carried on by it.

17.7.2 R The Society must carry all amounts it receives on behalf of any member in respect of that member's insurance business to the appropriate Lloyd's trust fund.

17.7.3 R A managing agent must carry all amounts it receives on behalf of any member in respect of that member's insurance business to the appropriate Lloyd's trust fund.

17.7.4 R In complying with LLD 17.7.1R to LLD 17.7.3R, the Society and managing agents must take all reasonable steps to ensure that amounts received or receivable by a member in respect of general insurance business and long-term insurance business are carried to separate Lloyd's trust funds.

17.7.5 G The requirement in LLD 17.7.4R should be read in conjunction with the requirements of PRU 7.6 as applied to the Society and managing agents in LLD 24.6.1R to LLD 24.6.5G.

17.8 Amendments to byelaws, trust deeds and standard form letters of credit and guarantees

17.8.1 R The Society must, as soon as it is practical to do so, notify the FSA of its intention to approve the form of any new Lloyd's trust deed.

17.8.2 R The Society must, as soon as it is practical to do so, notify the FSA of its intention to make any amendment which may alter the meaning or effect of any byelaw, including:

(1) any Lloyd's trust deed;

(2) any standard form letter of credit prescribed by the Society from time
to time; or

(3) any standard form guarantee agreement prescribed by the Society from time to time.

17.8.3 R The Society must provide the FSA with full details of:

(1) the form of any new Lloyd's trust deed it intends to approve, as described in LLD 17.8.1R; and

(2) any amendments falling within LLD 17.8.2R.

17.8.4 R The Society must consult interested parties in relation to any new Lloyd's trust deed and in relation to any amendment falling within LLD 17.8.2R.

17.8.5 G Except in urgent cases, the Society should consult in relation to any new Lloyd's trust deed or amendments before the new deed or amendments take effect.

17.8.6 R The information provided to the FSA by the Society under LLD 17.8.3R must include:

(1) a statement of the purpose of any proposed amendment or new Lloyd's trust deed and the expected impact, if any, on policyholders, managing agents, members, and potential members; and

(2) a description of the consultation undertaken under LLD 17.8.4R including a summary of any significant responses to that consultation.

17.8.7 G The FSA would normally expect to receive the information required under LLD 17.8.3R and LLD 17.8.6R not less than three months in advance of the proposed change.
Annex M

Amendments to the Lloyd's sourcebook, Chapter 18

In this Annex, all the text is new and is not underlined.

18 Application of PRU 1 to Lloyd's

18.1 Section 150 of the Act (Actions for damages)

18.1.1 R A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

18.2 Adequacy of financial resources

Application of PRU 1.2

18.2.1 R PRU 1.2 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.

18.2.2 R LLD 18.2.7R applies to members, pursuant to the insurance market direction in LLD 18.2.5D.

Insurance market direction

18.2.3 G The insurance market direction in LLD 18.2.5D is given under section 316(1) of the Act (Direction by Authority) and applies to members.

18.2.4 G The purpose of the insurance market direction in LLD 18.2.5D is to enable the FSA to make the rule in LLD 18.2.7R applying to members, in order to:

(1) protect policyholders against the risk that members may not have adequate financial resources to meet liabilities under or in respect of contracts of insurance as they fall due;

(2) promote confidence in the market at Lloyd's by requiring members to maintain financial resources which are adequate to meet their liabilities.

18.2.5 D With effect from 1 January 2005, Part X of the Act (Rules and Guidance) applies to the members of the Society taken together in relation to the insurance market activities of effecting and carrying out contracts of insurance written at Lloyd's, for the purpose of applying the rules and guidance in LLD 18.2.7R to LLD 18.2.9G.

18.2.6 G Part X of the Act is a core provision specified in section 317(1) of the Act
(The core provisions). Section 317(2) provides that references in an applied core provision to an authorised person are to be read as references to a person in the class to which the insurance market direction applies. From 1 January 2005, references in Part X of the Act are to be read as references to members for the purposes of LLD 18.2.7R to LLD 18.2.9G.

Members' obligation to maintain adequate financial resources

18.2.7 R The members taken together must at all times maintain overall financial resources, including capital and liquidity resources, that are adequate, both as to amount and quality, to ensure that there is no significant risk that liabilities under or in respect of contracts of insurance written at Lloyd's will not be met as they fall due.

18.2.8 G Under PRU:

1. Managing agents must ensure that adequate financial resources are available to support the insurance business carried on through each syndicate that they manage; and

2. The Society must, having regard to the availability and value of the central assets, ensure that the financial resources supporting the insurance business of each member are adequate at all times.

18.2.9 G In practice compliance with the requirements described in LLD 18.2.8G are likely to have the effect that members comply with LLD 18.2.7R.

18.3 Valuation and recognition

Application of PRU 1.3

18.3.1 R PRU 1.3 applies to managing agents and to the Society in accordance with:

1. For managing agents, LLD 16.3.3R; and

2. For the Society, LLD 16.3.1R.

Amounts receivable but not yet received

18.3.2 R When recognising and valuing assets that are available to meet liabilities arising from a member's insurance business, neither the Society nor managing agents may attribute any value to any amounts receivable but not yet received from that member or another member, except for:

1. Timing differences provided that a corresponding amount has been deducted from syndicate assets or funds at Lloyd's;

2. The Society's callable contributions, which are valued according to LLD 18.3.10G to LLD 18.3.12R; and
(3) debts owed by a member to another member of the Society where the debt is a liability arising out of the insurance business he carries on at Lloyd's.

Letters of credit, guarantees and life assurance policies

18.3.3 G Letters of credit, guarantees and life assurance policies are admissible assets in respect of insurance business at Lloyd's and qualify as capital resources under PRU 2.2, subject to LLD 18.3.4R to LLD 18.3.9G.

18.3.4 R When recognising and valuing assets held as members' funds at Lloyd's the Society may, if the conditions in LLD 18.3.5R are satisfied, attribute a value to letters of credit and guarantees that it holds in respect of a member's insurance business.

18.3.5 R The conditions referred to in LLD 18.3.4R are that letters of credit and guarantees must be:

1. in the form prescribed by the Society from time to time and notified to the FSA; and

2. issued by a credit institution or an insurance undertaking.

18.3.6 R When recognising and valuing assets held as members' funds at Lloyd's the Society may attribute a value to verifiable sums arising out of life assurance policies.

18.3.7 R The Society must value any letter of credit, guarantee or life assurance policy at its net realisable value. The Society must make all appropriate deductions, including those in respect of:

1. the expenses of realisation; and

2. any reduction in value that would be likely to occur if the asset needed to be realised at short notice to meet liabilities falling due earlier than expected.

18.3.8 R If a member relies on a value attributed to a letter of credit or guarantee to meet any applicable capital resources requirement and that letter of credit or guarantee will expire in less than one month, the Society must take appropriate steps to ensure that the applicable capital resources requirement will continue to be met, including taking steps to ensure that sums due under the letter of credit or guarantee are drawn down when due and carried to the appropriate Lloyd's trust fund.

18.3.9 G In LLD 18.3.8R, the expiry date includes the date on which the instrument will terminate if not renewed, and the date on which any notice to terminate will or would take effect.

The Society's callable contributions

18.3.10 G Under LLD 19.3.7R(2) and LLD 19.3.9R, the Society may recognise and
value \emph{callable contributions} in its calculation of its own \emph{capital resources}. \emph{LLD} 18.3.11R specifies the maximum value that may be attributed to \emph{callable contributions}.

18.3.11 R For the purposes of \emph{LLD} 19.3.7R(2) and \emph{LLD} 19.3.9R, the amount assumed to be callable from a \emph{member} must not exceed the lower of:

1. the maximum \emph{callable contribution} that \emph{member} is or may be liable to make in that \emph{financial year}; and
2. the amount by which the \emph{member's own capital resources} exceed the \emph{member's own capital resources requirement}.

18.3.12 R The \emph{Society} must value \emph{callable contributions} taking appropriate account of any legal, constructive or other limits on its ability to call for contributions from \emph{members} or to realise the amount called.

18.3.13 R The \emph{Society} must give the \emph{FSA} adequate advance notice if it proposes to change the maximum amount of the \emph{callable contribution} that \emph{members} may be liable to make in any \emph{financial year}.

18.3.14 G The \emph{FSA} would normally expect not less than six months' notice under \emph{LLD} 18.3.13R.

\textbf{Liabilities}

18.3.15 R Subject to \emph{LLD} 18.3.16R, the \emph{Society} must recognise and value all of a \emph{member's liabilities in respect of its insurance business}.

18.3.16 R The \emph{Society} need not recognise or value a \emph{member's liabilities} that are recognised and valued at \emph{syndicate} level by \emph{managing agents} in accordance with \emph{PRU} 1.3.

18.3.17 R For the purposes of calculating a \emph{member's capital resources}, when valuing a \emph{member's funds at Lloyd's} the \emph{Society} must deduct the value of a \emph{member's liabilities} determined under \emph{LLD} 18.3.15R.

18.3.18 G The liabilities to be valued under \emph{LLD} 18.3.15R and deducted under \emph{LLD} 18.3.17R include:

1. amounts owing to \emph{members' agents};
2. amounts owing to the \emph{Society};
3. an appropriate accrual for tax payable on any profits;
4. (where required under any applicable accounting principle in accordance with \emph{PRU} 1.3.5R), any contingent liability relating to liabilities reinsured into Equitas Reinsurance Ltd; and
5. amounts apportioned to \emph{members} in respect of the credit equalisation
reserve under PRU 7.5.

18.3.19 R  In recognising and valuing a member's liabilities, the Society and managing agents may, to the extent permitted by applicable accounting principles, leave out of account the liabilities in respect of 1992 and prior general insurance business reinsured by Equitas Reinsurance Limited.

18.3.20 G  There may be contingent liabilities associated with the reinsurance into Equitas. PRU 1.3 requires managing agents and the Society to treat those contingent liabilities in accordance with applicable accounting principles: see PRU 1.3.5R. Depending on the circumstances, managing agents or the Society may need to disclose or account for such a liability.

18.4 Prudential risk management and associated systems and controls

Application of PRU 1.4

18.4.1 R  Subject to LLD 18.4.2R, PRU 1.4 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.

18.4.2 R  The requirement in PRU 1.4.18R to take reasonable steps to ensure the establishment and maintenance of a business plan does not apply to the Society.
Annex N

Amendments to the Lloyd's sourcebook, Chapter 19

In this Annex, all the text is new and is not underlined.

19 Application of PRU 2 to Lloyd's

19.1 Section 150 of the Act (Actions for damages)

19.1.1 R A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

19.2 Calculation of capital resources requirements

Application of PRU 2.1

19.2.1 R PRU 2.1 applies to the Society in accordance with LLD 16.3.1R.

19.2.2 R PRU 2.1.34R to PRU 2.1.35G apply to managing agents in accordance with LLD 16.3.3R.

19.2.3 G PRU 2.1.9R requires the Society to ensure, in relation to each member's insurance business, that capital resources equal to or in excess of the member's capital resources requirement (CRR) are maintained. PRU 2.1 sets out the overall framework of the CRR. PRU 7.2 sets out the calculation of the components of the general insurance capital requirement and the long-term insurance capital requirement.

19.2.4 G Managing agents are required to calculate the ECR for the purposes of carrying out syndicate ICAs under PRU 2.3. As with-profits insurance business is not carried on through any syndicate, the calculation of the with-profits insurance capital component will not be applicable. PRU 7.4 is not applied to Lloyd's.

Calculation of the MCR

19.2.5 R For the purposes of PRU 2.1.21R, the Society must calculate the MCR in respect of the general insurance business of each member as the higher of:

(1) the member's share of the base capital resources requirement in respect of general insurance business for the members in aggregate; and

(2) the general insurance capital requirement for the member, calculated according to LLD 19.2.11R.

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19.2.6  R  For the purposes of LLD 19.2.5R(1), the Society must determine the member's share by apportioning the base capital resources requirement in respect of general insurance business for the members in aggregate between members in proportion to the result for each member of LLD 19.2.11R.

19.2.7  R  For the purposes of PRU 2.1.22R, the Society must calculate the MCR in respect of the long-term insurance business of each member as the higher of:

1. the member's share of the base capital resources requirement in respect of long-term insurance business for the members in aggregate; and
2. the sum of, for each member:
   a. the long-term insurance capital requirement; and
   b. the resilience capital requirement.

19.2.8  R  For the purposes of LLD 19.2.7R(1), the Society must determine the member's share by applying to the aggregate long-term business base capital resources requirement the ratio of the result for the member of LLD 19.2.7R(2) to the aggregate of the results of LLD 19.2.7R(2) for all members.

Calculation of the base capital resources requirement

19.2.9  R  Subject to PRU 2.1.27R, the amount of the base capital resources requirement for the members in aggregate is:

1. for general insurance business, €3 million; and
2. for long-term insurance business, €3 million.

Calculation of the general insurance capital requirement

19.2.10  R  For the purposes of PRU 2.1.30R, the Society must calculate the general insurance capital requirement for the members in aggregate as the higher of:

1. the aggregate for all members of the higher of, for each member, the result of the premiums amount and the claims amount; and
2. the brought forward amount.

19.2.11  R  The Society must determine the general insurance capital requirement for each member by apportioning the result of LLD 19.2.10R between members on a fair and reasonable basis, provided that the general insurance capital requirement for a member must not be less than the higher of the result of the premiums amount and the claims amount for that member.

19.2.12  G  The Society should calculate the premiums amount and the claims amount for each member on the basis of the member's own general insurance business, including insurance business that attaches to the reinsuring
member for the purposes of PRU following an approved reinsurance to close (see LLD 17.5.3R).

19.2.13 R The Society must calculate the general insurance capital requirement it would have to determine under PRU 2.1.30R if it were an insurer carrying on all the general insurance business carried on by its members, but eliminating inter-syndicate reinsurance (the Society GICR).

19.2.14 G For the purpose of LLD 19.2.13R the Society may make appropriate approximations, taking reasonable care to avoid underestimating the Society GICR.

19.2.15 R The Society must determine each member's share of the Society GICR by allocating the Society GICR between the members in proportion to the result for each member of LLD 19.2.11R.

19.3 Capital resources

Application of PRU 2.2

19.3.1 R Subject to LLD 19.3.3R, LLD 19.3.4R and LLD 19.3.6R, PRU 2.2 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.

19.3.2 G PRU 2.1 sets out minimum capital resources requirements for a firm and for Lloyd's members. PRU 2.2 sets out how, for the purpose of these requirements, capital resources are defined and measured. PRU 2.2 applies:

(1) to managing agents for their calculation of the capital resources managed by them in respect of each syndicate they manage (by reference, where there is a change in the underlying capital provision, to each open syndicate year); and

(2) to the Society for its calculation of:

(a) each member's capital resources; and

(b) its own capital resources.

19.3.3 R PRU 2.2.15G to PRU 2.2.26R (Limits on the use of different forms of capital) do not apply to managing agents.

19.3.4 R PRU 2.2.15G to PRU 2.2.26R (Limits on the use of different forms of capital) apply to the Society with respect to:

(1) the capital resources requirements for the members in aggregate;
and

(2) the aggregate capital resources supporting the insurance business of all the members.

19.3.5 R PRU 2.2.72R does not apply to the Society or to managing agents.

19.3.6 R In this Chapter LLD 19, “the aggregate capital resources supporting the insurance business of all the members” are:

(1) the aggregate of all the members' capital resources calculated under LLD 19.3.10R; and

(2) the Society's capital resources excluding callable contributions.

Calculation of capital resources

19.3.7 R Table PRU 2.2.14R applies with the modifications that:

(1) (A) CORE TIER ONE CAPITAL includes Lloyd's members' contributions in accordance with LLD 19.3.19R, subject, in the case of letters of credit, guarantees and verifiable sums arising out of life assurance policies, to compliance with LLD 18.3.3G to LLD 18.3.9G; and

(2) the Society may also recognise and value callable contributions, pursuant to LLD 19.3.9R.

19.3.8 G Lloyd's member's contributions are admissible assets under LLD 19.3.19R and include letters of credit, guarantees and verifiable sums arising out of life assurance policies held as funds at Lloyd's. Assets that may be valued as part of capital resources under PRU are not necessarily, however, permitted investments for members under the terms of any Lloyd's trust deed.

19.3.9 R In calculating its capital resources, the Society may, subject to LLD 18.3.10G to LLD 18.3.12R, recognise and value callable contributions.

19.3.10 R The Society must calculate each member's capital resources as the sum of:

(1) a member's proportionate share of the capital resources held at syndicate level for each syndicate in which the member participates; and

(2) the value of a member's funds at Lloyd's after deducting liabilities in compliance with LLD 18.3.17R.

19.3.11 R In order to comply with PRU 2.1.9R the Society must ensure at all times that:

(1) each member's capital resources requirement is covered by:

(a) that member's capital resources, calculated according to LLD
19.3.10R; and

(b) to the extent that (a) is insufficient, by the Society's own capital resources; and

(2) the Society GICR is covered by the aggregate capital resources supporting the insurance business of all the members.

19.3.12 R For the purposes of LLD 19.3.11R(1)(b), the Society must maintain at all times capital resources sufficient to meet the aggregate of, for each member, the amount, if any, by which the member's capital resources fall short of the member's capital resources requirement.

19.3.13 R The Society must calculate each member's share of the amount of capital resources required to comply with PRU 2.2.17R as the higher of:

(1) 1/3 of the long-term insurance capital requirement for the members in aggregate; and

(2) the base capital resources requirement;

allocated between the members in proportion to the result for each member of LLD 19.2.7R(2).

19.3.14 R For the purposes of PRU 2.2.18R, the Society must ensure that the aggregate capital resources supporting the insurance business of all the members meet the higher of:

(1) 1/3 of the general insurance capital requirement for the members in aggregate; and

(2) 1/3 of the Society GICR; and

(3) the base capital resources requirement;

with the sum of the items listed in PRU 2.2.18R.

19.3.15 R The Society must calculate each member's share of the amount of capital resources required to comply with PRU 2.2.18R as the higher of:

(1) 1/3 of the general insurance capital requirement for the members in aggregate; and

(2) 1/3 of the Society GICR; and

(3) the base capital resources requirement;

allocated between the members in proportion to the result for each member of LLD 19.2.11R.

Characteristics of tier one capital

19.3.16 R A Lloyd's member's contribution may be included in tier one capital
resources to the extent that:

(1) the proceeds are immediately and fully available in respect of the member's insurance business at Lloyd's;

(2) (except in relation to letters of credit), it complies with PRU 2.2.29R(3) or cannot be repaid to a member until all of the member's liabilities in respect of its insurance business at Lloyd's have been extinguished, covered or reinsured by an approved reinsurance to close;

(3) it otherwise complies with PRU 2.2.29R(5) to (8).

Adjustments for related undertakings

19.3.17 R PRU 2.2.90R applies to the Society with the modification that the Society must also value its insurance undertakings in accordance with PRU 2.2.90R.

19.3.18 R If a related undertaking is an insurance undertaking which has a deficit in the capital resources available to cover its capital resources requirement, the Society must make provision for:

(1) its proportionate share of that deficit; or

(2) in the case of a subsidiary undertaking, the whole of that deficit.

Modification of Annex 1R for Lloyd's

19.3.19 R In the case of members, Lloyd's members' contributions are included in PRU 2 Annex 1R and include:

(1) letters of credit;

(2) guarantees; and

(3) verifiable sums arising out of life assurance policies;

held as funds at Lloyd's.

19.3.20 G The effect of LLD 19.3.19R is that Lloyd's members' contributions, including letters of credit, guarantees and life assurance policies, are admissible assets.

19.4 Individual capital assessment

Application of PRU 2.3

19.4.1 R Subject to LLD 19.4.2R, PRU 2.3 applies to managing agents and to the Society in accordance with:
(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.

19.4.2 R Managing agents must carry out assessments of capital adequacy for each syndicate they manage by reference to all open syndicate years taken together.

Assessment of adequacy of capital resources for syndicates and members

19.4.3 G PRU 1.2 requires firms to carry out assessments of the adequacy of their financial resources. Financial resources include capital resources and liquidity resources. PRU 5 contains guidance on liquidity stress tests. Managing agents should manage liquidity risk affecting each syndicate they manage and the Society should manage liquidity risk affecting funds at Lloyd's and central assets, including the risk that it cannot make liquid assets available to support syndicates on a timely basis.

19.4.4 G PRU 2 sets out provisions that deal specifically with the adequacy of that part of a firm's financial resources that consists of capital resources. PRU 2.3 sets out guidance on how firms should assess the adequacy of their capital resources. The relevant requirements for Lloyd's are that:

(1) the Society should carry out regular assessments of the adequacy of the capital resources available to support each member’s insurance business; and

(2) managing agents should carry out regular assessments of the adequacy of capital resources held at syndicate level in respect of the insurance business carried on through each syndicate.

19.4.5 G Responsibility for:

(1) managing the risks associated with the insurance business; and

(2) holding the capital resources that support those risks;

is divided between managing agents and the Society. To clarify the respective responsibilities of managing agents and the Society for ensuring the adequacy of financial resources, the FSA distinguishes between the managing agents’ responsibility to carry out capital adequacy assessments for each syndicate that they manage, and the Society's responsibility to carry out an assessment for each member.

19.4.6 R In carrying out capital adequacy assessments in respect of the insurance business carried on through each syndicate (the syndicate ICA), managing agents must consider the risks, controls and the financial resources relevant to each syndicate.

19.4.7 R When carrying out the syndicate ICA, managing agents must not take into account risks to which a member may be exposed or controls from which a
member may benefit:

(1) because that member carries on insurance business through another syndicate or more than one syndicate year (whether or not managed by the same managing agent); or

(2) because that member’s financial resources include funds at Lloyd’s or central assets.

19.4.8 R The Society must have regard to syndicate ICAs in arriving at its own capital assessment for each member.

19.4.9 G In assessing the adequacy of the capital resources supporting the insurance business of each member, the Society should consider the risks, controls and financial resources relevant to the totality of the member’s insurance business, including:

(1) the adequacy of syndicate ICAs;

(2) the member’s share of syndicate ICAs;

(3) adjustments in respect of risks and controls relating to funds at Lloyd’s, central assets and the interaction of risks underwritten by the member through different syndicates and in respect of different syndicate years; and

(4) the ongoing validity of any relevant assumptions it makes.

19.4.10 G The Society should be able to justify any reliance it places on a syndicate ICA, for example by being able to demonstrate that it has carried out appropriate checks.

19.4.11 G In taking account of a syndicate ICA under LLD 19.4.8R:

(1) if the Society considers a syndicate ICA to be adequate, it should use the managing agent’s risk and capital assessments in carrying out its individual capital assessment in relation to any member of that syndicate, or it should be able to justify why it will not; and

(2) if the Society considers a syndicate ICA to be less than adequate, the Society should increase the syndicate ICA so that it is adequate for the purpose of carrying out its individual capital assessment in relation to the members of that syndicate.

19.4.12 G The assessment of capital adequacy for a member will rarely equal the proportionate share of a syndicate ICA (or sum of those shares, where the member participates on more than one syndicate) as attributed to that member, because, in determining the capital assessments for each member, the Society may make adjustments to take account of:

(1) risks and controls associated with funds at Lloyd’s and central assets,
which can increase the member's individual capital assessment;

(2) diversification effects, including as a result of members' participations on more than one syndicate year, which can reduce the member's individual capital assessment; and

(3) its own assessment of syndicate risks, which can be higher than the managing agent's and so increase the member's individual capital assessment.

The balancing amount

19.4.13 G Capital resources to meet each syndicate ICA could be:

(1) held within a syndicate and managed by the managing agent; or

(2) held and managed by the Society; or

(3) not needed in full, because of effects such as diversification that the Society takes into account.

19.4.14 G The balancing amount is a function of the relationship between the syndicate ICA and the amount of assets held within the syndicate. As illustrations:

(1) if the syndicate holds no capital resources (but its liabilities are fully covered by relevant assets), the balancing amount equals the syndicate ICA (as there are no capital resources at syndicate level, all the capital resources must be held as funds at Lloyd's or central assets);

(2) if capital resources held at syndicate level are negative (i.e. if relevant assets do not fully cover liabilities for the syndicate), the balancing amount should be higher than the syndicate ICA by an amount corresponding to the negative capital resources held by managing agents on behalf of the syndicate; and

(3) conversely, if a syndicate holds positive capital resources for the syndicate, the balancing amount should be lower than the syndicate ICA by a corresponding amount.

19.4.15 R Managing agents must periodically notify the Society of the syndicate ICA and the balancing amount in respect of each syndicate.

19.4.16 R For the purpose of assessing the adequacy of capital resources held as funds at Lloyd's and central assets, the Society must have regard to balancing amounts notified to it by managing agents.

19.4.17 R After notification of a balancing amount by a managing agent, the Society must:

(1) confirm to the managing agent that capital resources held as funds
at Lloyd's and central assets are adequate to support the balancing amount; or

(2) notify the managing agent that it cannot give that confirmation.

19.4.18 G Managing agents should submit syndicate ICAs and notify balancing amounts to the Society as part of the annual capital-setting process at Lloyd's. The submission of the syndicate ICA and notification of the balancing amount should be made in good time for the Society to review them and place appropriate reliance on them when it determines the capital assessments for each member.

19.4.19 G When communicating the syndicate ICA and balancing amount for each syndicate to the Society, managing agents should agree with the Society an allocation of the syndicate ICA between syndicate years. The purpose of the allocation is to ensure that there is an appropriate matching of assets to risk and liabilities and an equitable treatment between the members reflecting the provision of capital in each syndicate year.

19.4.20 G Under LLD 19.4.23R, a managing agent has a continuing obligation to communicate to the Society a revised syndicate ICA and, where appropriate, a revised balancing amount, if it considers that the syndicate ICA and balancing amount communicated in the capital-setting process are no longer adequate in the light of the risks to which the syndicate business is exposed.

Monitoring of capital resources

19.4.21 G For the purposes of complying with their obligations under PRU, managing agents may assume that any balancing amount confirmed by the Society under LLD 19.4.17R is supported by capital resources held as funds at Lloyd's and central assets.

19.4.22 G Following initial confirmation of a balancing amount by the Society, assumptions made about risks and controls may change or risks may crystallise, affecting:

(1) the syndicate ICA (and hence, possibly, the balancing amount); or

(2) the relationship between a syndicate ICA and a member's individual capital assessment; or

(3) the amount of capital resources available.

19.4.23 R If a managing agent has, at any time, a significant doubt about the adequacy of a syndicate ICA or balancing amount with respect to syndicate risks and controls, it must notify the Society immediately.

19.4.24 R If the Society has, at any time, a significant doubt about the adequacy of any member's capital resources held by it in support of any balancing amount, it must notify the relevant managing agent immediately.
Annex O

Amendments to the Lloyd's sourcebook, Chapter 20

In this Annex, all the text is new and is not underlined.

20 Application of PRU 3 to Lloyd's

20.1 Section 150 of the Act (Actions for damages)

20.1.1 R A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

20.2 Credit risk management systems and controls

Application of PRU 3.1

20.2.1 R Subject to LLD 20.2.2R, PRU 3.1 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.

20.2.2 R In accordance with LLD 18.4.2R, the rules and guidance in PRU 3.1 relating to the establishment and maintenance of a business plan do not apply to the Society.

20.3 Credit risk in insurance funds

Application of PRU 3.2

20.3.1 R Subject to LLD 20.3.2R, PRU 3.2 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.

20.3.2 R PRU 3.2.23R to PRU 3.2.32G (Large exposure calculation for reinsurance exposures) do not apply to the Society.

Overall limitation of credit risk

20.3.3 G For Lloyd's, counterparty exposure is:
(1) for managing agents, the amount by which the net assets managed by or under the direction of a managing agent in respect of a syndicate together with any relevant balancing amount would decrease if the counterparty were to default;

(2) for the Society, the amount by which its net assets (which include those of its subsidiary undertakings) would decrease if the counterparty were to default; and

(3) for the Society's management of each member's funds at Lloyd's, the amount by which the member's net assets would decrease if the counterparty were to default.

Large exposures

20.3.4 R For the purposes of PRU 3.2.20R (Large exposure limits: counterparty exposure and asset exposure), the Society may determine the exposure to any letters of credit, guarantees or members' life assurance policies as an exposure of the members in aggregate.

20.3.5 R For the purposes of PRU 3.2.22R (Large exposure limits: market risk and counterparty limits), the Society must calculate the amount of and deduct from capital resources:

(1) an exposure (expressed as a percentage of the relevant member's capital resources held as funds at Lloyd's), other than to the assets identified in LLD 20.3.5R(2)(a) to (c), of a member's capital resources held as funds at Lloyd's to a counterparty, in excess of the limits in PRU 3.2.22R;

(2) an exposure in excess of 20% (expressed as a percentage of the aggregate of capital resources held as funds at Lloyd's) of the aggregate of capital resources held as funds at Lloyd's to a single issuer of:

(a) letters of credit;

(b) guarantees; or

(c) members' life assurance policies;

(3) an exposure of its own to a counterparty, in excess of the limits in PRU 3.2.22R, expressed as a percentage of the Society's own assets.

20.3.6 R For the purposes of PRU 3.2.22R (Large exposure limits: market risk and counterparty limits), managing agents must calculate the amount of and deduct from capital resources an exposure (expressed as a percentage of the admissible assets held in respect of the relevant syndicate) of admissible assets held in respect of a syndicate to a counterparty in excess of the limits in PRU 3.2.22R.

20.3.7 R If the exposures of capital resources held as funds at Lloyd's for members in
the aggregate do not exceed the limits in PRU 3.2.22R(3)(c), then, for each *individual member*, that limit may be replaced by 10%.

Exposures excluded from the large exposure limits

20.3.8 R For *managing agents*, in PRU 3.2.33R and PRU 3.2.35R, references to an exposure do not include exposure arising from *balancing amounts*.

20.4 Asset-related Capital Requirement

Application of PRU 3.3

20.4.1 R PRU 3.3 applies to *managing agents* and to the *Society* in accordance with:

(1) for *managing agents*, LLD 16.3.3R; and

(2) for the *Society*, LLD 16.3.1R.

20.4.2 G This chapter applies to the *Society* for each *member*, including the capital charge relating to *central assets*, to the extent that those assets are held to support a particular *member*. 
Annex P

Amendments to the Lloyd's sourcebook, Chapter 21

In this Annex, all the text is new and is not underlined.

21 Application of PRU 4 to Lloyd's

21.1 Section 150 of the Act (Actions for damages)

21.1.1 R A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

21.2 Market risk management systems and controls

Application of PRU 4.1

21.2.1 R PRU 4.1 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.

21.2.2 R In accordance with LLD 18.4.2R, the rules and guidance in PRU 4.1 relating to the establishment and maintenance of a business plan do not apply to the Society.

21.3 Market risk in insurance

Application of PRU 4.2

21.3.1 R PRU 4.2 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R, subject to LLD 21.3.4R below; and

(2) for the Society, LLD 16.3.1R.

Resilience capital requirement (applicable to long-term business only)

21.3.2 R Managing agents must calculate the amount of the resilience capital requirement for the long-term insurance business carried on through the syndicates they manage.

21.3.3 R The Society must determine the resilience capital requirement for the
insurance business of each member under PRU 4.2.10R as the member's proportionate share of the resilience capital requirement calculated by the managing agent for the long-term insurance business carried on through the syndicate.

Currency risk: matching of assets and liabilities

21.3.4 R For the purposes of PRU 4.2.53R, a managing agent must ensure that:

(1) syndicate liabilities are covered by matching syndicate assets as required by PRU 4.2.53R; or that

(2) it immediately notifies to the Society the nature and extent of any syndicate liabilities not covered by matching assets under (1).

21.3.5 G Notwithstanding the terms of PRU 4.2.53R, a managing agent may comply with PRU 4.2.53R by notifying unmatched currency liabilities to the Society.

21.3.6 R On receipt of a notification by a managing agent under LLD 21.3.4R(2), the Society must ensure that the liabilities in respect of the insurance business of the members in aggregate are covered with matching assets complying with PRU 4.2.53R.

21.3.7 G The Society should consider the need to cover the unmatched currency liabilities notified under LLD 21.3.4R(2) with assets in the same currency held as funds at Lloyd's for any relevant member or, if necessary, with central assets meeting the currency matching requirements.

21.4 Derivatives in insurance

Application of PRU 4.3

21.4.1 R PRU 4.3 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.
Annex Q

Amendments to the Lloyd's sourcebook, Chapter 22

In this Annex, all the text is new and is not underlined.

22 Application of PRU 5 to Lloyd's

22.1 Section 150 of the Act (Actions for damages)

22.1.1 R A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

22.2 Liquidity risk systems and controls

Application of PRU 5.1

22.2.1 R PRU 5.1 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.

22.2.2 R In accordance with LLD 18.4.2R, the rules and guidance in PRU 5.1 relating to the establishment and maintenance of a business plan do not apply to the Society.
Annex R

Amendments to the Lloyd's sourcebook, Chapter 23

In this Annex, all the text is new and is not underlined.

23 Application of PRU 6 to Lloyd's

23.1 Section 150 of the Act (Actions for damages)

23.1.1 R A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

23.2 Operational risk: prudential systems and controls

Application of PRU 6.1

23.2.1 R PRU 6.1 applies to managing agents and to the Society in accordance with:

(1) for managing agents, LLD 16.3.3R; and

(2) for the Society, LLD 16.3.1R.

23.2.2 R In accordance with LLD 18.4.2R, the rules and guidance in PRU 6.1 relating to the establishment and maintenance of a business plan do not apply to the Society.
Annex S

Amendments to the Lloyd's sourcebook, Chapter 24

In this Annex, all the text is new and is not underlined.

24  Application of PRU 7 to Lloyd's

24.1  Section 150 of the Act (Actions for damages)

24.1.1  R  A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

24.2  Insurance risk systems and controls

Application of PRU 7.1

24.2.1  R  PRU 7.1 applies to managing agents in accordance with LLD 16.3.3R.

24.3  Capital resources requirements and technical provisions for insurance business

Application of PRU 7.2

24.3.1  R  PRU 7.2 applies to the Society in accordance with LLD 16.3.1R.

24.3.2  R  The following rules and guidance apply to managing agents in accordance with LLD 16.3.3R:

(1)  PRU 7.2.13R to PRU 7.2.20G (except PRU 7.2.13R(1));

(2)  PRU 7.2.42R to PRU 7.2.43G; and

(3)  PRU 7.2.74G to PRU 7.2.80R.

Establishing technical provisions

24.3.3  G  Managing agents are advised by the syndicate actuary in relation to the long-term insurance business carried on through long-term insurance business syndicates. The standards and guidance issued by the Faculty and Institute of Actuaries to assist syndicate actuaries are important sources of evidence as to generally accepted actuarial best practice, as referred to in PRU 7.2.16R(1).

General insurance capital requirement

24.3.4  G  PRU 2.1.30R and LLD 19.3.10R to LLD 19.3.12G set out the calculation of
the general insurance capital requirement for Lloyd's.

24.3.5 R The Society must calculate the brought forward amount for the members in aggregate in accordance with PRU 7.2.51R, using the result of LLD 19.2.6R for the prior financial year and the aggregate of all members' technical provisions for the relevant periods.

Accounting for premiums and claims

24.3.6 R For the purposes of PRU 7.2.66R and further to that rule, in the case of Lloyd's members, amounts of premiums and claims must be adjusted for approved reinsurance to close to exclude any amount included in, or adjustment made to, premiums and claims to reflect the consideration for an approved reinsurance to close.

24.3.7 G Members of Lloyd's can effect contracts of approved reinsurance to close with other members in accordance with LLD 17.5. For the purposes of PRU as it applies to Lloyd's, the capital requirement relating to business transacted through an approved reinsurance to close is calculated for the reinsuring and not the reinsured member under the contract.

24.4 Mathematical reserves

Application of PRU 7.3

24.4.1 R PRU 7.3 applies to managing agents in accordance with LLD 16.3.3R.

Approved reinsurance to close

24.4.2 R In respect of business that has been subject to an approved reinsurance to close, managing agents must calculate mathematical reserves (before and after deduction of reinsurance cessions) for the reinsuring and not for the reinsured member.

24.5 Equalisation provisions

Application of PRU 7.5

24.5.1 R PRU 7.5 applies to the Society in accordance with LLD 16.3.1R:

(1) with the modification set out in LLD 24.5.2R; and

(2) except PRU 7.5.11R to PRU 7.5.37G.

24.5.2 R The Society must calculate a credit equalisation provision for the aggregate insurance business of all members; it is not required to calculate a credit equalisation provision separately for the business of each member.
24.5.3 R The *Society* must allocate the result of *LLD 24.5.2R* between itself and each of the members on a fair and reasonable basis.

24.6 Internal-contagion risk

Application of PRU 7.6

24.6.1 R *PRU 7.6* applies to managing agents and to the *Society* in accordance with:

(1) for managing agents, *LLD 16.3.3R*; and

(2) for the *Society*, *LLD 16.3.1R*.

Restriction of business to insurance

24.6.2 R The *Society* and managing agents must take all reasonable steps to ensure that:

(1) a corporate member does not carry on any commercial business other than insurance business and activities arising directly from that business; and

(2) individual members do not, in their capacity as underwriting members, carry on any commercial business other than insurance business and activities arising directly from that business.

Syndicates not to carry on both general and long-term business

24.6.3 R A managing agent must not permit both general insurance business and long-term insurance business to be carried on together through any syndicate managed by it.

24.6.4 G *PRU 7.6.17G* contains guidance setting out the FSA policy (reflecting requirements of the Insurance Directives) in relation to the carrying on together of general and long-term insurance business.
Annex T

Amendments to the Lloyd's sourcebook, Chapter 25

In this Annex, all the text is new and is not underlined.

25 Regulatory intervention points for Lloyd's

25.1 Section 150 of the Act (Actions for damages)

25.1.1 R A contravention of the rules in this chapter does not give rise to a right of action by a private person under section 150 of the Act (Actions for damages) and each of those rules is specified under section 150(2) of the Act as a provision giving rise to no such right of action.

25.2 Application

25.2.1 R The rules and guidance in SUP App 2 apply to the Society:

(1) with the modifications set out in LLD 25.3.1R to LLD 25.8.1G; but

(2) except SUP App 2.8.1R to SUP App 2.8.5G, SUP App 2.9.1G, SUP App 2.10.1G, SUP App 2.12.1R(2)(a), SUP App 2.12.2G and SUP App 2.12.7R.

25.3 Interpretation

25.3.1 R For the purpose of this Chapter LLD 25 and the application of SUP App 2 to the Society:

(1) "capital resources", as the context requires:

(a) in relation to the Society's own capital resources, means its own capital resources calculated in accordance with PRU 2.2.12R;

(b) in relation to a member's capital resources, means the member's capital resources calculated in accordance with LLD 19.3.10R;

(c) in relation to the aggregate capital resources of the Society and the members supporting the insurance business of the members, means the aggregate of the capital resources in (1)(a) and (b) but excluding the Society's callable contributions.

(2) "guarantee fund":

(a) in relation to the general insurance business carried on by members, means the amount of capital resources required in
order to comply with PRU 2.2.18R, LLD 19.3.4R and LLD 19.3.14R; and the "member's share of the guarantee fund" for general insurance business means the result of the calculation set out in LLD 19.3.15R;

(b) in relation to the long-term insurance business carried on by members, means the amount of capital resources required in order to comply with PRU 2.2.17R and LLD 19.3.4R; and the "member's share of the guarantee fund" for long-term insurance business means the result of the calculation set out in LLD 19.3.13R;

(3) "required margin of solvency":

(a) in relation to the general insurance business carried on by members, means the higher of the Society GICR and the general insurance capital requirement for the members in aggregate; and

(b) in relation to the long-term insurance business carried on by members, means the long-term insurance capital requirement for the members in aggregate.

25.3.2 G The calculations of the base capital resources requirement, the long-term insurance capital requirement and the general insurance capital requirement for members and for the members in aggregate are set out in PRU 2.1 and in LLD 19. LLD 19.2.13R requires the Society to calculate the Society GICR. PRU 2.2.17R and PRU 2.2.18R, as applied to Lloyd's and modified by LLD 19.3.4R and LLD 19.3.13R to LLD 19.3.15R, contain requirements for the calculation of the guarantee fund and the member's share of the guarantee fund.

25.4 Purpose

25.4.1 G Under PRU and LLD 19 the Society must, separately in respect of the general insurance business and long-term insurance business carried on by members, ensure:

(1) its own capital resources are sufficient to cover the aggregate of, for each member, any amount by which the member's capital resources are inadequate to meet the member's CRR; and

(2) that the aggregate capital resources of the Society and the members supporting the insurance business of the members comply with the requirements of PRU 2.2.15G to PRU 2.2.26R.

The PRU provisions as applied to Lloyd's reflect requirements under the Insurance Directives.
25.4.2 G Regulatory intervention is triggered under SUP App 2 if:

1. the capital resources of the Society are insufficient to meet the aggregate of, for each member, the amount, if any, by which the member's capital resources fall short of the member's share of the guarantee fund (the guarantee fund required by Article 17, First Non-Life Directive and Article 29, Consolidated Life Directive);

2. the capital resources of the Society are insufficient to meet the aggregate of, for each member, the amount, if any, by which the member's capital resources fall short of the member's share of the required margin of solvency (the solvency margin required by Article 16a, First Non-Life Directive and Article 28, Consolidated Life Directive);

3. the capital resources of the Society and of each of the members supporting their own insurance business, in the aggregate, no longer comply with PRU 2.2.16R and PRU 2.2.24R. PRU 2.2.16R and PRU 2.2.24R prescribe limits on the forms of capital resources which a firm must hold. (For Lloyd's, the Society must comply with PRU 2.2.16R and PRU 2.2.24R in relation to the aggregate of its own capital resources and the capital resources of the members supporting their own business: see LLD 19.3.4R);

4. the capital resources of the Society are insufficient to meet the aggregate of, for each member, the amount, if any, by which the member's capital resources fall short of the member's share of the CRR for the members in aggregate.

25.4.3 G PRU requires the Society to ensure that the financial resources supporting the insurance business of each member are adequate at all times. Under PRU 2.3.13G, the FSA may give individual capital guidance to the Society stating the amount and quality of capital resources that it considers ought to be held to meet PRU 1.2.22R. If the Society's own capital resources fall below individual capital guidance given to the Society in respect of those resources, the FSA may take further action as set out in SUP App 2.7.1.G to SUP App 2.7.5G.

25.5 Capital resources below guarantee fund

25.5.1 R For the purposes of SUP App 2.4.1R and SUP App 2.4.2G, capital resources will have fallen below the guarantee fund if the Society's own capital resources are such that they are no longer sufficient to meet the aggregate of, for each member, the amount, if any, by which the member's capital resources fall short of the member's share of the guarantee fund.

25.6 Capital resources below required margin of solvency
25.6.1 R For the purposes of SUP App 2.5.1R to SUP App 2.5.3R, capital resources will be such that they no longer equal or exceed the required solvency margin if the Society's own capital resources are insufficient to meet the aggregate of, for each member, the amount, if any, by which the member's capital resources fall short of the member's share of the required solvency margin.

25.7 Capital resources below capital resources requirement

25.7.1 R For the purposes of SUP App 2.6.1R, capital resources will have fallen below the capital resources requirement if the Society's own capital resources are insufficient to meet the aggregate of, for each member, the amount, if any, by which the member's capital resources fall short of the member's share of the capital resources requirement for the members in aggregate.

25.8 Capital resources below the level of individual capital guidance

25.8.1 G For the purposes of SUP App 2.7.1G to SUP App 2.7.5G, capital resources will have fallen below the level of individual capital guidance if the Society's own capital resources have fallen below the level advised in individual capital guidance given to the Society in respect of those capital resources.
Annex U

Part 1

Amendments to the Supervision manual, Chapter 3

In this Part, underlining indicates new text and striking through indicates deleted text.

3 Auditors

3.1 Application

3.1.2 R Table: Applicable sections

<table>
<thead>
<tr>
<th>(6)</th>
<th>Insurer, the Society of Lloyd’s, underwriting agent or members’ adviser (Note 5)</th>
<th>SUP 3.1 – SUP 3.7</th>
<th>SUP 3.1, SUP 3.2, SUP 3.8</th>
</tr>
</thead>
</table>

Note (5) = In row (6):

(a) **SUP 3.1 – SUP 3.7** applies to a managing agent in respect of its own business and in respect of the insurance business of each syndicate which it manages; and

(b) **SUP 3.1, SUP 3.2 and SUP 3.8** apply to the auditors of a managing agent and the auditors of the insurance business of each syndicate which the managing agent manages.

3.1.9 G A firm which is a bank, building society, friendly society or other insurer, investment management firm, personal investment firm, securities and futures firm, or the Society of Lloyd’s, or a Lloyd’s managing agent in respect of each syndicate managed by it, should see the Interim Prudential sourcebooks for further provisions as set out in **SUP 3.1.10G**. For the categorisations employed in **SUP 3.1.2R** and **SUP 3.1.10G** see **SUP App 1**.

3.1.10 G Table: other relevant sections of the handbook

| Investment management firm, personal investment firm, securities and futures firm | IPRU (INV) |
| Society of Lloyd’s and Lloyd’s managing agents | LLD |
Lloyd’s

Enabling provision and application

3.1.11 G The **insurance market direction** in this chapter is given under section 316(1) of the *Act* (Direction by Authority) and applies to **members**.

Purpose

3.1.12 G The **insurance market direction** in this chapter is intended to enable the rules in SUP 3 and SUP 4 to be applied to a **managing agent** in respect of the **insurance business** of each **syndicate** which it manages.

Insurance market direction on rules concerning auditors and actuaries

3.1.13 D (1) With effect from 1 January 2005, Part XXII of the *Act* (Auditors and Actuaries) applies to the carrying on of **insurance business** by **members** as modified by paragraph (3).

(2) For the purposes of (1) "**insurance business**" means the **regulated activities** of **effecting or carrying out contracts of insurance** written at Lloyd's.

(3) Regulations made by the Treasury under section 342(5) and section 343(5) of Part XXII of the *Act* apply only to **actuaries** appointed by a **managing agent** in respect of the **insurance business** of a **syndicate**, in relation to the **long-term insurance business** of that **syndicate**.

(4) In Part XXII of the *Act* (Auditors and Actuaries) as applied by this **insurance market direction**:

(a) a reference to an auditor of an **authorised person** is to be read as including an auditor appointed by a **managing agent** in respect of the **insurance business** of a **syndicate**; and

(b) a reference to an **actuary** acting for an **authorised person** is to be read as including an **actuary** appointed by a **managing agent** in respect of the **insurance business** of a **syndicate**.

3.1.14 G Part XXII (Auditors and Actuaries) is a **core provision** mentioned in section 317(1) of the *Act* (The core provisions).

3.1.15 G Section 317(2) of the *Act* (The core provisions) provides that references in an applied **core provision** to an **authorised person** are to be read as references to a **person** in the class to which the **insurance market direction** applies. The effect of this, and of the **insurance market direction** set out at SUP 3.1.13D, is that Part XXII of the *Act* (Auditors and Actuaries), applies also to auditors and **actuaries** who
are appointed to report on the underwriting business of members. Part XXII is modified in its application to members by paragraph (3) of SUP 3.1.13D with the effect that the regulations made under sections 342(5) and 343(5) of the Act relating to communications by actuaries will only apply where the actuary is appointed to evaluate the long-term insurance business of the syndicate. The regulations made under sections 342(5) and 343(5) in relation to communications by auditors will apply in relation to both general insurance business and long-term insurance business.

3.16 G SUP 3.3 sets out rules the effect of which is to require a managing agent to appoint an auditor in respect of its own business and the insurance business of each syndicate which it manages.

3.17 G References in SUP 3, as applied by SUP 3.1.2R, to a firm include, where appropriate:

(1) a managing agent; and

(2) one or more members carrying on insurance business at Lloyd’s through a syndicate,

and references to an actuary of a firm should be read accordingly.

3.18 G SUP 4.6 sets out rules the effect of which is to require a managing agent to appoint an actuary in respect of the insurance business of each syndicate which it manages.

3.3 Appointment of auditors

The Society of Lloyds

3.4 D [deleted]

With a view to achieving the objectives of promoting confidence in the market at Lloyd’s and protecting the interests of policyholders and potential policyholders, the Society is directed under section 318 of the Act (Exercise of powers through Council), to take reasonable steps to ensure that:

(1) every managing agent appoints an auditor for every syndicate which it manages, and

(2) the auditor of every syndicate has the skill, resources and experience required to perform his duties.

3.5 R [deleted]

Paragraph (2) applies if the notifications required by SUP 3.3.2...
R (2) or (5) are within the scope of any arrangements made by the FSA with the Society of Lloyd's under paragraph 6 (2) of Schedule 1 to the Act.

(2) An underwriting agent must submit a notification in (1) to the Society of Lloyd's rather than to the FSA.

3.3.6 G [deleted]
An underwriting agent should see SUP 15.7.13G and SUP 15.7.14G for further guidance on the arrangements in SUP 3.3.5R.

3.7 Notification of matters raised by an auditor

3.7.3 G [deleted]
An underwriting agent should submit any notifications under this section in accordance with the arrangements made between the FSA and the Society of Lloyd's. For guidance on those arrangements see SUP 15.7.13G and SUP 15.7.14G.

3.8 Rights and duties of auditors

3.8.10 G Auditors are subject to regulations made by the Treasury under sections 342(5) and 343(5) of the Act (Information given by auditor or actuary to the FSA). These regulations oblige auditors to report certain matters to the FSA. Sections 342(3) and 343(3) of the Act provide that an auditor does not contravene any duty by giving information or expressing an opinion to the FSA, if he is acting in good faith and he reasonably believes that the information or opinion is relevant to any functions of the FSA. These provisions continue to have effect after the end of the auditor's term of appointment. In relation to Lloyd's, an effect of the insurance market direction set out at SUP 3.1.13D is that sections 342(5) and 343(5) of the Act (Information given by an auditor or actuary to the Authority) apply also to auditors appointed to report on the insurance business of members.

3.8.13 R [deleted]
(1) An auditor of an underwriting agent must submit a notification under SUP 3.8.11R or SUP 3.8.12R to the Society of Lloyd's
rather than to the FSA if (2) applies.

(2) This paragraph applies if the notification is within the scope of any arrangements made by the FSA with the Society of Lloyd's under paragraph 6(2) of Schedule 1 to the Act.

3.8.14 G [deleted]
For guidance on these arrangements, see SUP 15.7.13G and SUP 15.7.14G. Notification to the Society acting on behalf of the FSA in accordance with SUP 3.8.13R also satisfies the obligation to notify the FSA in accordance with section 344 of the Act (Duty of auditor or actuary resigning etc. to give notice).
Annex U

Part 2

Amendments to the Supervision manual, Chapter 4

In this Part, underlining indicates new text and striking through indicates deleted text.

4 Actuaries

4.1 Application

…

4.1.2 G This chapter applies to long-term insurers (including friendly societies) and other friendly societies and to the Society of Lloyd's and managing agents at Lloyd's. This chapter does not apply to the Society of Lloyd's or to Lloyd's underwriting agents. Requirements dealing with the appointment and duties of actuaries in relation to Lloyd's insurance business are contained in LLD. This chapter does not apply to actuaries advising the auditors of long-term insurers under IPRU(INS) 9.35(1A) or IPRU(FSOC) 5.11(2A), as they are not appointed to act on behalf of the firm.

4.1.3 R Table: applicable sections

<table>
<thead>
<tr>
<th>(1) Category of firm</th>
<th>(2) Applicable sections</th>
</tr>
</thead>
<tbody>
<tr>
<td>…</td>
<td></td>
</tr>
<tr>
<td>(3) A Lloyd’s managing agent, in respect of each syndicate it manages</td>
<td>SUP 4.1, SUP 4.2, SUP 4.5, SUP 4.6</td>
</tr>
<tr>
<td>(4) The Society of Lloyd’s</td>
<td>SUP 4.1, SUP 4.2, SUP 4.5, SUP 4.6</td>
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<td>…</td>
<td></td>
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</tbody>
</table>

4.2 Purpose

…

4.2.2 G This chapter…purpose of this chapter is to ensure that:

(1) long-term insurers (other than…

(2) other friendly societies carrying on…the liabilities of that
businesses; and

(3) managing agents of Lloyd's syndicates employ or use an actuary of appropriate seniority and experience to evaluate the liabilities associated with insurance business carried on at Lloyd’s.

…

4.5.7 G ………..These provisions continue to have effect after the end of the actuary's term of appointment. In relation to Lloyd's, an effect of the insurance market direction set out at SUP 3.1.13D is that sections 342(5) and 343(5) of the Act (Information given by auditor or actuary to the FSA) apply also to actuaries who are appointed to evaluate the long-term insurance business of a syndicate.

…

4.6 Lloyd’s Appointment of the Lloyd’s actuary and syndicate actuaries

4.6.1 R The Society must:

(1) appoint an actuary to perform the Lloyd’s actuary function;

(2) notify the FSA, without delay, when it is aware that a vacancy in the office of Lloyd’s actuary will arise or has arisen, giving the reason for the vacancy;

(3) appoint an actuary to fill any vacancy in the office of Lloyd’s actuary that has arisen; and

(4) ensure that the replacement actuary can take up office at the time the vacancy arises or as soon as reasonably practicable after that.

4.6.2 G The functions performed by the actuary appointed as the Lloyd’s actuary under SUP 4.6.1R are specified as controlled functions in SUP 10 (Approved persons). As a result, an application must be made to the FSA under section 60 of the Act (Applications for approval) for approval of the person proposing to take up such an appointment. Section 61(3) of the Act (Determination of applications) gives the FSA three months to grant its approval or give a warning notice that it proposes to refuse the application. An actuary should not be appointed until the FSA has approved the actuary. In order to comply with SUP 4.6.1R, the Society should ensure it applies to the FSA as soon as practicable before the date when it needs the actuary to take office. The FSA will need time to consider the application before deciding whether to grant approval.
Qualifications

4.6.3 R Before the Society applies for approval of its proposed appointment of the Lloyd’s actuary under SUP 4.6.1R, it must take reasonable steps to ensure that the actuary:

(1) has the required skill and experience to perform his functions under the regulatory system; and

(2) is a Fellow of the Institute of Actuaries or of the Faculty of Actuaries.

4.6.4 G To comply with SUP 4.6.3R and Principle 3, before the Lloyd’s actuary takes up his appointment the Society should ensure that the actuary:

(1) has skills and experience appropriate to the nature, scale and complexity of the Society’s business and the requirements and standards under the regulatory system to which it is subject; and

(2) has adequate qualifications and experience, which includes holding an appropriate practising certificate under the rules of the Institute of Actuaries or the Faculty of Actuaries;

and seek confirmation of these from the actuary, or the actuary’s current and previous employers, as appropriate.

Disqualified actuaries

4.6.5 R The Society must not appoint under SUP 4.6.1R as Lloyd’s actuary an actuary who is disqualified by the FSA under section 345 of the Act (Disqualification) from acting:

(1) as an actuary for the Society; or

(2) as a syndicate actuary; or

(3) as an actuary for any other relevant class of firm.

4.6.6 G If it appears to the FSA that an actuary has failed to comply with a duty imposed on him under the Act, it may disqualify him under section 345 of the Act. For more detail about what happens when the disqualification of an actuary is being considered or put into effect, see ENF 17. A list of actuaries who are disqualified by the FSA may be found on the FSA website.

Conflicts of interest

4.6.7 R The Society must take reasonable steps to ensure that an actuary who is to be, or has been, appointed under SUP 4.6.1R:
(1) does not perform the function of chairman or chief executive of the Society; and

(2) does not perform any other function on behalf of the Society which could give rise to a significant conflict of interest.

The Lloyd’s actuary function

4.6.8 R An actuary who has been appointed to perform the Lloyd’s actuary function must:

(1) prepare the statement required under LLD 15.9.1R(2) to be annexed to the Lloyd’s Return; and

(2) take reasonable steps to ensure that the general insurance business technical provisions for each syndicate year have been reviewed by the syndicate actuary and that an appropriate opinion has been obtained under SUP 4.6.15R; and

(3) where a syndicate actuary’s opinion has not been provided, sets appropriate technical provisions and, within six months of the end of the financial year, submits a report to the FSA on the setting of those technical provisions.

Appointment of syndicate actuaries

4.6.9 R Each managing agent must, in respect of each syndicate it manages:

(1) appoint an actuary (the “syndicate actuary”) to carry out the duties described in SUP 4.6.15R or SUP 4.6.16R; and

(2) appoint a replacement for that actuary if he ceases to hold office before he has carried out the duties described in SUP 4.6.15R or SUP 4.6.16R; and

(3) ensure that the replacement syndicate actuary can take up office at the time the vacancy arises or as soon as reasonably practicable after that.

4.6.10 G (1) The insurance market direction and guidance set out in SUP 3.1.4G to SUP 3.1.15G is relevant to actuaries appointed to report on the insurance business of members.

(2) References in SUP 4, as applied by SUP 4.1.3R, to a firm include, where appropriate:

(a) a managing agent; and

(b) one or more members carrying on insurance business at Lloyd’s through a syndicate;
and references to an actuary of a firm should be read accordingly.

Syndicate actuaries’ qualifications

4.6.11 R Before a managing agent appoints a syndicate actuary, it must take reasonable steps to ensure that the syndicate actuary:

(1) has the required skill and experience to perform his duties; and

(2) is a fellow of an actuarial body or (except for a syndicate actuary of a long-term insurance business syndicate) is a fellow of the Casualty Actuarial Society who is a member of an actuarial body.

4.6.12 G To comply with SUP 4.6.11R and Principle 3, before a syndicate actuary takes up his appointment a managing agent should ensure that the syndicate actuary:

(1) has skills and experience appropriate to the nature, scale and complexity of a syndicate’s business and the requirements and standards under the regulatory system applicable to the activities of managing agents in relation to each syndicate which they manage; and

(2) has adequate qualifications and experience, which includes holding an appropriate practising certificate under the rules of the Institute of Actuaries or the Faculty of Actuaries; and

and seeks confirmation of these from the syndicate actuary, or the syndicate actuary’s current and previous employers, as appropriate.

Disqualified actuaries

4.6.13 R A managing agent must not appoint under SUP 4.6.9R as syndicate actuary an actuary who is disqualified by the FSA under section 345 of the Act (Disqualification) from acting:

(1) as a syndicate actuary; or

(2) as a Lloyd’s actuary; or

(3) as an actuary for a relevant class of firm.

4.6.14 G If it appears to the FSA that an actuary has failed to comply with a duty imposed on him under the Act, it may disqualify him under section 345 of the Act. For more detail about what happens when the disqualification of an actuary is being considered or put into effect, see ENF 17. A list of actuaries who are disqualified by the FSA may be found on the FSA website.
Duties of syndicate actuaries

4.6.15 R The syndicate actuary of a long-term insurance business syndicate must:

(1) make an investigation at the end of each financial year into the financial condition of the business carried on through each syndicate year (other than a closed year);

(2) make an abstract of his report of the investigation; and

(3) prepare the certificate required under LLD 15.9.1R(3) to be annexed to the Lloyd's Return.

4.6.16 R The syndicate actuary of a general insurance business syndicate must:

(1) review the technical provisions (both gross and net of reinsurance recoveries) of each syndicate year (other than a closed year); and

(2) provide his opinion confirming that the technical provisions for each syndicate year are no less prudent than his best estimate of the amounts required.

4.6.17 R If a managing agent becomes aware that the syndicate actuary of a general insurance business syndicate will or may be unable to produce an unqualified opinion under SUP 4.6.16R, the managing agent must promptly inform the FSA that this is the case.

4.6.18 R In carrying out his duties a syndicate actuary must pay due regard to generally accepted actuarial best practice.

4.6.19 G The standards and guidance issued by the Institute of Actuaries and the Faculty of Actuaries are important sources of actuarial best practice.
Annex U

Part 3

Amendments to the Supervision manual, Chapter 10

In this Part, underlining indicates new text and striking through indicates deleted text.

10.4 Specification of functions

10.4.5 R Table: controlled functions

<table>
<thead>
<tr>
<th>Type</th>
<th>CF</th>
<th>Description of controlled function</th>
</tr>
</thead>
<tbody>
<tr>
<td>…</td>
<td></td>
<td></td>
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<tr>
<td>Required functions*</td>
<td>…</td>
<td>…</td>
</tr>
<tr>
<td>12B</td>
<td>…</td>
<td>Lloyd’s actuary function</td>
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</tbody>
</table>

Appointed actuary function (CF12)

Lloyd’s actuary function (CF12B)

10.7.22 R The Lloyd’s actuary function is the function of acting in the capacity of the actuary appointed under SUP 4.6.1R to perform the duties set out in SUP 4.6.7R.

10.7.23 G The effect of SUP 4.6.1R is that the Society of Lloyd’s must appoint an actuary (the “Lloyd’s actuary”).
Annex U

Part 4

Amendments to the Supervision manual, Schedule 2

In this Part, underlining indicates new text and striking through indicates deleted text.

<table>
<thead>
<tr>
<th>2</th>
<th>Table</th>
</tr>
</thead>
<tbody>
<tr>
<td>…</td>
<td>…</td>
</tr>
<tr>
<td><strong>SUP 3.3.5R</strong></td>
<td>Vacancy in the office of auditor to a Lloyd’s <strong>underwriting agent</strong> or the auditor of the insurance business of a Lloyd’s syndicate.</td>
</tr>
<tr>
<td>Appointment of auditor by Lloyd’s <strong>underwriting agent</strong></td>
<td>The fact of the appointment, name and business address of the auditor and the date the appointment takes effect. (NB—notification to be made to the Society of Lloyd’s).</td>
</tr>
<tr>
<td>…</td>
<td>…</td>
</tr>
</tbody>
</table>
Annex V

Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text. New definitions are to be inserted at the appropriate alphabetical position.

approved reinsurance to close

(a) a reinsurance to close effected before 1 January 2005; or

(b) an agreement under which members of a syndicate in one syndicate year ("the reinsured members") agree with the members of that syndicate in a later syndicate year or the members of another syndicate ("the reinsuring members") that the reinsuring members will discharge, or procure the discharge of, or indemnify the reinsured members against, all known and unknown insurance business liabilities of the reinsured members arising out of the insurance business carried on by the reinsured members in that syndicate year that is:

(i) effected after 1 January 2005; and

(ii) not a balance transfer between two syndicate years where the syndicate has only one member and the member is the same in each of those years.

balancing amount

in respect of a syndicate, any part of the capital resources that:

(a) the managing agent of the syndicate has assessed to be necessary to support the insurance business carried on by the members of the syndicate through the syndicate, including those capital resources required to support the risks arising at syndicate level that affect that business; but

(b) are not managed by or at the direction of the managing agent of the syndicate.

callable contribution

amounts that members are liable to pay to the Society (or may by resolution of the Society be liable to pay) as contributions to the Central Fund.

central assets

(in LLD) assets that the Society owns and amounts that members are liable to pay to the Society (or may by resolution of the Council be liable to pay) as contributions to the central fund excluding amounts which, if paid by a member, would cause his assets to fall short (or shorter) of the required amount; the Society’s own assets that are available at its discretion to meet a member’s liabilities in respect of insurance business.

corporate member

a member that is a body corporate or a Scottish Limited partnership.

Council

the governing body of the Society. (in LLD) the Council constituted by section 3 of Lloyd’s Act 1982.
funds at Lloyd’s assets (not being syndicate assets) provided by or on behalf of a member to meet the liabilities arising from the member's insurance business at Lloyd's, which are held in a Lloyd's trust fund and managed by the Society as trustee, held by the Society, not being part of their premium trust funds, to meet the liabilities arising from their the member's insurance business at Lloyd's.

IPRU(INS) (1) (except in LLD) the Interim Prudential Sourcebook for insurers;

(2) (in LLD) the version of IPRU(INS) in force immediately prior to the coming in to force of the Interim Prudential Sourcebook (Insurers and Other Amendments) Instrument 2004.

Lloyd’s actuary the actuary appointed by the Society under LLD 10.9.1R SUP 4.6.1R.

Lloyd’s member’s contribution assets:

(a) provided to a managing agent in response to a cash call; or

(b) held by the Society as funds at Lloyd’s.

Lloyd’s trust fund a fund held on the terms of a Lloyd’s trust deed.

Lloyd’s trust deed a trust deed in the form prescribed by the Society and notified to the FSA, for execution by a member in respect of his insurance business.

managing agent’s agreement an agreement in the form prescribed by the Society, between a managing agent and a member, under which the managing agent manages the insurance business of that member.

secured debt (1) (in LLD) a debt owed to (or an obligation to be fulfilled for the benefit of) a member, secured by an admissible asset.

(2) (in PRU) …

Society GICR the general insurance capital requirement calculated by the Society as if it were an insurer under LLD 19.2.13R.

syndicate actuary an actuary appointed to a syndicate as required by LLD 10.9.4R(1) SUP 4.6.9R(1)

syndicate assets assets managed by or at the direction of a managing agent in respect of insurance business carried on through a syndicate and overseas business regulatory deposits funded from those assets.

syndicate ICA the capital assessment performed by a managing agent under PRU 1.2.26R, LLD 18.2.1R(1), PRU 2.3 and LLD 19.4.1R(1) in respect of each syndicate managed by it.