

**LLOYD'S SOURCEBOOK (INTEGRATED PRUDENTIAL AND AUDITING AND
ACTUARIAL REQUIREMENTS) INSTRUMENT 2004**

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):

(1)	(2)
LLD Table of Contents	Annex A and Annex G, Part 2
LLD 1	Annex B
LLD 2	Annex C
LLD 9	Annex D
LLD 10	Annex E
LLD 11	Annex F
LLD 12	Annex G, Part 1 and Part 2
LLD 13	Annex H
LLD 14	Annex I
LLD 15	Annex J

- (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):

(1)	(2)
LLD 16	Annex K
LLD 17	Annex L
LLD 18	Annex M
LLD 19	Annex N
LLD 20	Annex O
LLD 21	Annex P
LLD 22	Annex Q
LLD 23	Annex R
LLD 24	Annex S
LLD 25	Annex T

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

Lloyd's			
	LLD TP	1	Lloyd's sourcebook – Transitional provisions
	LLD 1		The Society's regulatory functions
		1.1	Application and purpose
		1.2	Carrying out the Society's regulatory functions
		1.3	Conflicts of interest [deleted]
		1.4	Confidential regulatory information [deleted]
	LLD 2		Provision of information
		2.1	Application and purpose
		2.2	Specification of objective
		2.3	Information on matters likely to be of material concern to the FSA
		2.4	Information on investigations and disciplinary proceedings
		2.5	Co-operations between the FSA and the Society
		2.6	Information about the Society's byelaws [deleted]
	LLD 3		The Central Fund
			...
	LLD 4		Capacity transfer market
			...
	LLD 5		Former underwriting members
			...
	LLD 6		Complaints from policyholders
			...
	LLD 7		Complaints from members
			...
	LLD 8		Compensation arrangements for individual members
			...

	LLD 8A		Compensation arrangements for policyholders
			...
	LLD 9		Prudential requirements for the Society
		9.1	Application and purpose
		9.2	General prudential requirements
		9.3	General guidance on financial resources
		9.4	Accounting principles and records
	LLD 10		Insurance operational risk
		10.1	Application and purpose
		10.2	Systems and controls
		10.3	Carrying of insurance receivables to trust funds
		10.4	Changes in approved trust deeds
		10.5	Requirement to maintain risk-based capital system
		10.6	Requirements relating to monitoring aggregations of risk
		10.7	Requirements relating to syndicate business plans
		10.8	Managing agents systems and controls
		10.9	Requirements relating to the role of actuaries
		10.10	Limitation of business
		10.11	Monitoring of transactions between members
	LLD 11		Required margins of solvency
		11.1	Application and purpose
		11.2	Solvency requirement
		11.3	Member's margin
		11.4	General insurance
		11.5	Society margin
	LLD 12		Determination of liabilities
		12.1	Application and purpose
		12.2	Requirement to determine liabilities
		12.3	Members' liabilities
		12.4	General insurance business technical provisions
		12.5	Long term liabilities
	LLD 13		Assets: valuation and realisability risk
		13.1	Application and purpose
		13.2	Identification and valuation of assets
		13.3	Maturity and marketability of assets
		13.4	Admissible assets
		13.5	Restriction of value to realisable amounts
		13.6	Derivatives

		13.7	Stock lending agreements
		13.8	Debts and other rights
		13.9	Land
		13.10	Equipments
		13.11	Securities and beneficial interests in limited liability partnerships
		13.12	Collective investment schemes
		13.13	Deferred acquisition costs
		13.14	Reversionary interests
		13.15	Related and subsidiary undertakings
		13.16	Debts due or to become due from a related undertaking
	LLD 14		[deleted] Assets: market and credit risk
		14.1	Application and purpose
		14.2	Limitation of general market risk
		14.3	Currency matching and localisation
		14.4	Assets to be taken into account only to a specified extent
		14.5	Permitted asset exposure limits
		14.6	Counterparty exposure limits
	LLD 15		Reporting by the Society
		15.1	Application and purpose
		15.2	Requirement to report to the FSA
		15.3	Content and form of the Lloyd's return
		15.4	Risk groups for general insurance business
		15.5	Major treaty reinsurers
		15.6	Major facultative reinsurers
		15.7	Major reinsurance cedants
		15.8	Additional information
		15.9	Certificates and audit report
		15.10	The Lloyd's global account
		15.11	Public disclosure
		15.12	Other requirements
		15.13	<u>Syndicate-level reporting</u>
	LLD 16		<u>General provisions applying PRU to the Society and managing agents</u>
		16.1	<u>Section 150 of the Act (Actions for damages)</u>
		16.2	<u>Application</u>
		16.3	<u>Application of PRU to Lloyd's</u>
		16.4	<u>Summary of application of PRU to Lloyd's</u>
	LLD 17		<u>Special provisions for Lloyd's</u>
		17.1	<u>Section 150 of the Act (Actions for damages)</u>

	<u>17.2</u>	<u>Management of insurance business</u>
	<u>17.3</u>	<u>Obligations under PRU</u>
	<u>17.4</u>	<u>Management of risk</u>
	<u>17.5</u>	<u>Approved reinsurance to close</u>
	<u>17.6</u>	<u>Provision of information by managing agents</u>
	<u>17.7</u>	<u>Insurance receivables to be carried to trust funds</u>
	<u>17.8</u>	<u>Amendments to byelaws, trust deeds and standard form letters of credit and guarantees</u>
	<u>LLD 18</u>	<u>Application of PRU 1 to Lloyd's</u>
	<u>18.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>18.2</u>	<u>Adequacy of financial resources</u>
	<u>18.3</u>	<u>Valuation and recognition</u>
	<u>18.4</u>	<u>Prudential risk management and associated systems and controls</u>
	<u>LLD 19</u>	<u>Application of PRU 2 to Lloyd's</u>
	<u>19.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>19.2</u>	<u>Calculation of capital resources requirements</u>
	<u>19.3</u>	<u>Capital resources</u>
	<u>19.4</u>	<u>Individual capital assessment</u>
	<u>LLD 20</u>	<u>Application of PRU 3 to Lloyd's</u>
	<u>20.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>20.2</u>	<u>Credit risk management systems and controls</u>
	<u>20.3</u>	<u>Credit risk in insurance funds</u>
	<u>20.4</u>	<u>Asset-related capital requirements</u>
	<u>LLD 21</u>	<u>Application of PRU 4 to Lloyd's</u>
	<u>21.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>21.2</u>	<u>Market risk management systems and controls</u>
	<u>21.3</u>	<u>Market risk in insurance</u>
	<u>21.4</u>	<u>Derivatives in insurance</u>
	<u>LLD 22</u>	<u>Application of PRU 5 to Lloyd's</u>
	<u>22.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>22.2</u>	<u>Liquidity risk systems and controls</u>
	<u>LLD 23</u>	<u>Application of PRU 6 to Lloyd's</u>
	<u>23.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>23.2</u>	<u>Operational risk: prudential systems and controls</u>

	<u>LLD 24</u>		<u>Application of PRU 7 to Lloyd's</u>
		<u>24.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
		<u>24.2</u>	<u>Insurance risk systems and controls</u>
		<u>24.3</u>	<u>Capital resources requirements and technical provisions for insurance business</u>
		<u>24.4</u>	<u>Mathematical reserves</u>
		<u>24.5</u>	<u>Equalisation provisions</u>
		<u>24.6</u>	<u>Internal-contagion risk</u>
	<u>LLD 25</u>		<u>Regulatory intervention points for Lloyd's</u>
		<u>25.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
		<u>25.2</u>	<u>Application of SUP App 2</u>
		<u>25.3</u>	<u>Interpretation</u>
		<u>25.4</u>	<u>Purpose</u>
		<u>25.5</u>	<u>Capital resources below guarantee fund</u>
		<u>25.6</u>	<u>Capital resources below required margin of solvency</u>
		<u>25.7</u>	<u>Capital resources below capital resources requirement</u>
		<u>25.8</u>	<u>Capital resources below the level of individual capital guidance</u>

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

...

1.2 Carrying out the Society's regulatory functions

Delegation

...

Disciplinary arrangements

...

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 his 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 ~~the~~ *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

...

LLD12	Determination of liabilities [deleted]
12.1	Application and purpose
12.2	[deleted]
12.3	<i>Members' liabilities</i>
12.4	[deleted]
12.5	[deleted]

...

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

- 12 ~~Determination of liabilities~~ [deleted]
[Delete *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.

Annex H

Amendments to the Lloyd's sourcebook, Chapter 13

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.]

Annex J

Amendments to the Lloyd's sourcebook, Chapter 15

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

~~IPRU(INS); and,~~

~~(b) — having regard to Guidance Note 9.1 of IPRU(INS);~~

~~as if in the documents referred to in (a) and (b) those Appendices references to an insurer were references to the Society and 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 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 *derivative* contract held at any time during the *financial year* which did not fall within ~~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 *Society* ~~under 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 *syndicate actuary* of each *syndicate* which carries on *long-term insurance business* of the *actuary's* report made under ~~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 managing agent must:

(1) prepare a return for each financial year in respect of the insurance business carried on through each 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

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

			conformity with <i>LLD 15 Annex 4R</i> .
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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

<u>1</u>	<u>The certificate in <i>LLD 15.13.7R</i> must state:</u>		
	<u>(1)</u>	<u>that in the auditors' opinion, the return has been properly prepared in accordance with the instructions referred to in <i>LLD 15.13.2R</i>;</u>	
	<u>(2)</u>	<u>that according to the information and explanations that the auditors have received:</u>	
		<u>(a)</u>	<u>in their opinion, the certificate required to be signed in accordance with <i>LLD 15.13.3R</i> (other than statements to which paragraph 1(3) relates) has been properly prepared in accordance with the instructions; and</u>
		<u>(b)</u>	<u>it was or was not unreasonable for the persons giving the certificate to have made the statements in it (other than statements to which paragraph 1(3) relates);</u>
	<u>(3)</u>	<u>the extent to which, in giving their opinion, the auditors have relied, in respect of <i>long-term insurance business</i>, on the work of the <i>syndicate actuary</i>.</u>	
<u>2</u>	<u>The audit opinion required by paragraph 1 does not extend to cover information on major treaty reinsurers or major facultative reinsurers.</u>		
<u>3</u>	<u>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 <i>LLD 15.13.3R</i> to have made the statements therein, the auditors must add to their report such qualification, amplification or explanation as may be appropriate.</u>		

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

Key PRU requirements	<i>PRU</i>	<i>LLD</i>
Risk management, systems and controls		
The <i>Society</i> to establish and maintain systems and controls to address risks affecting the Lloyd's market		17.4
The <i>Society</i> to establish and maintain systems and controls for the management of prudential, credit, market, liquidity and operational risks affecting <i>funds at Lloyd's</i> and <i>central assets</i>	1.4, 3.1, 4.1, 5.1 & 6.1	17.4, 18.4, 20.2, 21.2, 22.2 & 23.2
<i>Managing agents</i> to establish and maintain systems and controls for the management of prudential, credit, market, liquidity, operational, and insurance risks affecting each <i>syndicate</i>	1.4, 3.1, 4.1, 5.1, 6.1 & 7.1	17.4, 18.4, 20.2, 21.2, 22.2, 23.2 & 24.2
Adequacy of financial resources		
The <i>Society</i> to ensure that <i>members'</i> financial resources are adequate	1.2	18.2

<i>Members</i> taken together to maintain adequate financial resources in respect of the <i>insurance business</i> conducted at Lloyd's		18.2
<i>Managing agents</i> to ensure that financial resources are adequate for each <i>syndicate</i>	1.2	18.2
Valuation		
The <i>Society</i> and <i>managing agents</i> to apply generally accepted accounting principles to valuing assets, liabilities, equity and income statement items for the purposes of the <i>rules</i> and <i>guidance</i> in <i>LLD</i> and <i>PRU</i> unless the contrary is expressly stated	1.3 & 4.3	18.3 & 21.4
Capital resources requirements		
The <i>Society</i> to calculate the <i>MCR</i> in respect of the <i>general insurance business</i> of each <i>member</i>	2.1	19.2
The <i>Society</i> to calculate the <i>CRR</i> (higher of <i>MCR</i> and <i>ECR</i>) in respect of the <i>long-term insurance business</i> of each <i>member</i>	2.1	19.2
Capital resources		
The <i>Society</i> and <i>managing agents</i> to calculate <i>capital resources</i> in accordance with the <i>rules</i> and <i>guidance</i> in <i>LLD</i> and <i>PRU</i>	2.2	19.3
Adequacy of capital resources		
<i>Managing agents</i> to assess the adequacy of <i>capital resources</i> held at <i>syndicate</i> level in respect of <i>insurance business</i> carried on through each <i>syndicate</i> (annual <i>ICA</i> for each <i>syndicate</i>)	2.3	19.4
The <i>Society</i> to assess the adequacy of <i>capital resources</i> available to support each <i>member's insurance business</i> (<i>ICA</i> for each <i>member</i>), both at <i>syndicate</i> level (taking account of <i>syndicate ICAs</i>), and as <i>funds at Lloyd's</i>	2.3	19.4

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 G 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 G 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 R 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

- (4) 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 *callable contributions* in its calculation of its own *capital resources*. *LLD 18.3.11R* specifies the maximum value that may be attributed to *callable contributions*.

- 18.3.11 R For the purposes of *LLD 19.3.7R(2)* and *LLD 19.3.9R*, the amount assumed to be callable from a *member* must not exceed the lower of:
- (1) the maximum *callable contribution* that *member* is or may be liable to make in that *financial year*; and
 - (2) the amount by which the *member's* own *capital resources* exceed the *member's* own *capital resources requirement*.
- 18.3.12 R The *Society* must value *callable contributions* taking appropriate account of any legal, constructive or other limits on its ability to call for contributions from *members* or to realise the amount called.
- 18.3.13 R The *Society* must give the *FSA* adequate advance notice if it proposes to change the maximum amount of the *callable contribution* that *members* may be liable to make in any *financial year*.
- 18.3.14 G The *FSA* would normally expect not less than six months' notice under *LLD 18.3.13R*.

Liabilities

- 18.3.15 R Subject to *LLD 18.3.16R*, the *Society* must recognise and value all of a *member's* liabilities in respect of its *insurance business*.
- 18.3.16 R The *Society* need not recognise or value a *member's* liabilities that are recognised and valued at *syndicate* level by *managing agents* in accordance with *PRU 1.3*.
- 18.3.17 R For the purposes of calculating a *member's* *capital resources*, when valuing a *member's* funds at *Lloyd's* the *Society* must deduct the value of a *member's* liabilities determined under *LLD 18.3.15R*.
- 18.3.18 G The liabilities to be valued under *LLD 18.3.15R* and deducted under *LLD 18.3.17R* include:
- (1) amounts owing to *members' agents*;
 - (2) amounts owing to the *Society*;
 - (3) an appropriate accrual for tax payable on any profits;
 - (4) (where required under any applicable accounting principle in accordance with *PRU 1.3.5R*), any contingent liability relating to liabilities reinsured into Equitas Reinsurance Ltd; and
 - (5) amounts apportioned to *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*.

- 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

...			
(6)	<i>Insurer, the Society of Lloyd's, underwriting agent or members' adviser (Note 5)</i>	<i>SUP 3.1 – SUP 3.7</i>	<i>SUP 3.1, SUP 3.2, SUP 3.8</i>
...			
	<u>Note (5) = In row (6):</u>		
(a)	<u>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</u>		
(b)	<u>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.</u>		

...

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

....	
<i>Investment management firm, personal investment firm, securities and futures firm</i>	<i>IPRU (INV)</i>
<i>Society of Lloyd's and Lloyd's managing agents</i>	<i>LLD</i>

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*.

3.1.16 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.

3.1.17 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.

3.1.18 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

3.3.4 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.~~

3.3.5 R ~~(1) [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

(1) Category of firm	(2) Applicable sections
...	
<u>(3) A Lloyd's <i>managing agent</i>, in respect of each <i>syndicate</i> it manages</u>	<u><i>SUP</i> 4.1, <i>SUP</i> 4.2, <i>SUP</i> 4.5, <i>SUP</i> 4.6</u>
<u>(4) The <i>Society of Lloyd's</i></u>	<u><i>SUP</i> 4.1, <i>SUP</i> 4.2, <i>SUP</i> 4.5, <i>SUP</i> 4.6</u>

...

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

business; 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 GThese 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 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

Type	CF	Description of controlled function
...		
Required functions*	... <u>12B</u> <u>Lloyd's actuary function</u> ...
...		

...

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.

2	Table				
	...				
	<i>SUP 3.3.5R</i>	Vacancy in the office of auditor to a Lloyd's <i>underwriting agent</i> <u>or the auditor of the insurance business of a Lloyd's syndicate.</u>	The fact of the vacancy and the reason for it. (NB— notification to be made to the Society of Lloyd's).	Vacancy in the office of auditor will arise or has arisen.	Without delay
		Appointment of auditor by Lloyd's <i>underwriting agent</i>	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).	Appointment of auditor	Not specified
	...				

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.

<i>funds at Lloyd's</i>	assets (<u>not being <i>syndicate assets</i></u>) provided by or on behalf of a <i>members</i> to meet the liabilities arising from the <i>member's insurance business</i> at <u>Lloyd's</u> which are held in a <i>Lloyd's trust fund</i> and managed by the <i>Society</i> as trustee, held by the <i>Society</i>, not being part of their <i>premium trust funds</i>, to meet the liabilities arising from their <u>the <i>member's insurance business</i> at Lloyd's</u>
<i>IPRU(INS)</i>	(1) (except in <i>LLD</i>) the Interim Prudential Sourcebook for insurers; (2) (in <i>LLD</i>) 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.
<i>Lloyd's actuary</i>	the <i>actuary</i> appointed by the <i>Society</i> under <i>LLD</i> 10.9.1R <u><i>SUP</i> 4.6.1R.</u>
<u><i>Lloyd's member's contribution</i></u>	assets: (a) <u>provided to a <i>managing agent</i> in response to a cash call; or</u> (b) <u>held by the <i>Society</i> as <i>funds at Lloyd's</i>.</u>
<u><i>Lloyd's trust fund</i></u>	a fund held on the terms of a <i>Lloyd's trust deed</i> .
<u><i>Lloyd's trust deed</i></u>	a trust deed in the form prescribed by the <i>Society</i> and notified to the <i>FSA</i> , for execution by a <i>member</i> in respect of his <i>insurance business</i> .
<u><i>managing agent's agreement</i></u>	an agreement in the form prescribed by the <i>Society</i> , between a <i>managing agent</i> and a <i>member</i> , under which the <i>managing agent</i> manages the <i>insurance business</i> of that <i>member</i> .
<i>secured debt</i>	(1) (in <i>LLD</i>) a debt owed to (or an obligation to be fulfilled for the benefit of) a <i>member</i> , secured by an <i>admissible asset</i> . (2) (in <i>PRU</i>) ...
<u><i>Society GICR</i></u>	<u>the <i>general insurance capital requirement</i> calculated by the <i>Society</i> as if it were an <i>insurer</i> under <i>LLD</i> 19.2.13R.</u>
<i>syndicate actuary</i>	an <i>actuary</i> appointed to a <i>syndicate</i> as required by <i>LLD</i> 10.9.4R(1) <u><i>SUP</i> 4.6.9R(1)</u>
<u><i>syndicate assets</i></u>	<u>assets managed by or at the direction of a <i>managing agent</i> in respect of <i>insurance business</i> carried on through a <i>syndicate</i> and overseas business regulatory deposits funded from those assets.</u>
<u><i>syndicate ICA</i></u>	<u>the capital assessment performed by a <i>managing agent</i> under <i>PRU</i> 1.2.26R, <i>LLD</i> 18.2.1R(1), <i>PRU</i> 2.3 and <i>LLD</i> 19.4.1R(1) in respect of each <i>syndicate</i> managed by it.</u>