

GLOBALS

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Global Results 2002

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Chief Executive Officer's report

'Lloyd's ratings remained stable over the year, as Standard & Poor's affirmed its A (Strong) rating of Lloyd's in May, and A.M. Best affirmed its A- (Excellent) rating in August.'

2002 was an important year for Lloyd's. The market returned to profitability while achieving record-high levels of premium income. Worldwide growth across virtually all lines of business has proved that Lloyd's expertise remains in demand. This demonstration of the confidence that international insurance buyers have in the present and future of Lloyd's is, of course, an accomplishment of the individual businesses that comprise the market, and the thousands of underwriters, brokers, agents and supporting personnel.

The Corporation of Lloyd's is the body that provides the physical, supervisory, operating and financial infrastructure that enables the market to function. For the Corporation, too, 2002 marked a turning point: its role was enhanced to encompass that of Franchisor. The Corporation has put, at its core, the creation of an environment in which the profitability of the market can be maximised. This evolutionary development involves some fundamental changes to the functions of the Corporation and as 2002 drew to a close, much progress had been made in driving forward the Corporation's new responsibilities.

Chief among these was the creation of the Lloyd's Franchise Board, which replaced the Lloyd's Market Board and the Lloyd's Regulatory Board. Its members are charged with overseeing the development, implementation and ongoing management of the Franchise. A new executive division has been created within Lloyd's, the Franchise Performance Directorate, to ensure that guidelines set by the Franchise Board are met by all market participants.

During 2002 the Corporation's Market Supervision Division was refocused as the Risk Management Division. They initiated ongoing procedures to identify, monitor and address operational, aggregate and systemic risks that threaten the achievement of the Franchise objectives – including the underperformance of individual syndicates. The work of the Division is intended to protect the value inherent in both the individual businesses operating within Lloyd's and in the market as a whole.

Already the Risk Management Division has conducted themed reviews examining the market's position regarding reinsurance recoveries for 2002, aggregate monitoring systems,



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syndicates' realistic disaster scenarios, terrorism, and compliance with the requirements of the UK insurance regulator, the Financial Services Authority. To improve control over delegated underwriting, changes were made to the system for approving international coverholders, and initial steps were taken to develop an on-line registration system for binding authorities. The development of a comprehensive and modern risk management system will continue in 2003, building on accomplishments in 2002.

Many of the changes arise from the development of the Corporation's role from that of traditional statutory supervisor – the overall responsibility for which now rests with the UK Financial Services Authority – to a wider new role of protecting and enhancing the Franchise. This led to several additional accomplishments that were evident by the end of the year. The market's capital strength was enhanced through the comprehensive application of risk-based capital requirements, which were further strengthened by its prudent assessment of operating risk. The central forecasting and understanding of the development of market results was strengthened through improved analytical techniques.

Many market businesses arranged capital increases, to take advantage of the improved trading conditions prevalent in 2002. This trend has continued into 2003 with increases in capacity from 75% of the managing agents, which in some cases has amounted to increases of over 100% on their capacity in 2002.

This resilience was recognised and while many conventional insurance carriers saw their financial strength ratings downgraded, Lloyd's ratings remained stable over the year, as Standard & Poor's affirmed its A (Strong) rating of Lloyd's in May, and A.M. Best affirmed its A- (Excellent) rating in August. Both agencies have since reaffirmed those ratings, providing Lloyd's with the third-party endorsement of its financial strength that has become essential in the increasingly competitive international insurance market.

As the Franchise Board began to consider the setting of target security ratings and combined ratios for the market as a whole, Lloyd's continued its work with external regulatory authorities to maintain and develop Lloyd's licences and trading status around the world. Some of this work resulted in the formation of a joint working party by the China Insurance Regulatory Committee, to pursue Lloyd's objective of securing an option to access China's on-shore reinsurance market.

With licences to accept direct insurance in over 60 countries, one of the key assets of the Franchise is the Lloyd's brand. We continued to promote and develop the strength and awareness of the brand in all of our key territories. This included the strengthening of relationships with the market's core constituencies – including brokers, capital providers, investment analysts and rating agencies.

Market losses during 2001 and 2002 resulted in claims against the Central Fund sufficient to trigger coverage under the Central Fund insurance. The Central Fund insurers paid £134m during 2002, subject to a reservation of their rights in respect of these claims. The insurers have indicated that they dispute their liability to meet the claims made under the policy. Lloyd's does not accept that the insurers have any grounds for disputing liability and in April 2003 commenced arbitration proceedings to secure payment in full under the terms of the policy. Lloyd's is currently reviewing both the need and the options for further insurance protection for the Central Fund upon expiry of the current policy at the end of 2003.

'The new structure should ensure that Lloyd's remains a thriving, versatile and leading insurance market in the years to come, as well as a modern and efficient one.'

Falling equity markets and weakness in the US Dollar generated a negative investment return for the Central Fund, in sterling terms. However, losses were limited by reduced equity exposure, and when considered in US Dollar terms, the Central Fund generated a small, positive investment return in 2002. These results were achieved alongside the continuing stability of the Corporation's finances. The strength of Lloyd's central balance sheet (including the Central Fund) was greatly enhanced over the year, significant savings were realised under renegotiated information technology contracts and through newly implemented systems, and costs overall were held steady. Despite the Corporation's increased activity, improved budgetary controls have led to a more efficient Corporation of Lloyd's.

Lloyd's demonstrated its commitment to improving processing standards and efficiency in 2001, when it successfully transferred Lloyd's Policy Signing Office into Xchanging Ins-sure. In 2002, Lloyd's continued to support initiatives helping to drive forward the process of modernisation in both the Lloyd's and London markets, such as the London Market Principles (LMP) programme. Project Blue Mountain is also one of the key initiatives to modernise the London market business processes backed by Lloyd's in 2002. Project Blue Mountain is an international venture to enable commercial lines trading partners to communicate front and back office risk data electronically, providing a more secure, efficient and accurate environment for broker and underwriters to exchange data. The project has received considerable support from both brokers and underwriters.

With its focus on the future, the Corporation also devoted resources to legacy issues to ensure that run-off losses are better managed, particularly in those businesses affecting the Central Fund. In 2002 Lloyd's established a team to develop and implement a more active and commercial approach to open years of account. A review of the effectiveness of incumbent management approaches was followed by the implementation of techniques to improve run-off management. Combined run-off reinsurance, which provides better and more effective protection for the Central Fund and for capital providers, was purchased. In addition, the closure of four open years of account through reinsurance to close has enabled 3,300 Names with Centrewrite Exeat policies to cease their membership of Lloyd's and opened the way for more than 2,000 additional Names to cease.

The vast majority of Names have met their commitments to Lloyd's, and the small number of those who refuse to do so were set back in 2002 as the Court of Appeal dismissed all of the allegations that they had brought against Lloyd's. Following this success, the debt enforcement process began in earnest.

Lloyd's performed strongly in 2002. The Corporation and the market as a whole embraced and tackled the challenges placed upon it. The implementation of the Franchise, as directed by the Chairman's Strategy Group and supported overwhelmingly by Lloyd's capital providers, is well underway. The new structure should ensure that Lloyd's remains a thriving, versatile and leading insurance market in the years to come, as well as a modern and efficient one.

Finally, I would like to thank all Corporation staff for their dedication and hard work during this challenging year of change.

Nick Prettejohn

Chief Executive Officer

2 April 2003

Operating and financial review

Operating review

Following the completion of the projects to form Xchanging Ins-sure ('XIS') and Xchanging Claims Services ('XCS'), a new operations function has been established within Lloyd's. The objective of the operations function is to provide value for money services to the market, including Information Technology, Property and Members' Services. Strong focus has been placed on the development of an effective commercial relationship with XIS and XCS, clarifying the relationship between Lloyd's, the market and these new companies.

Lloyd's business continuity plans have been reviewed during 2002; the resulting improvement plan will continue to be delivered through 2003. The initial focus is on franchisor systems and procedures, which can form the hub of market-wide continuity plans.

Information Technology

Substantial cost savings have been achieved in 2002. Contracts with key outsourcing IT suppliers are currently being re-negotiated to provide a reduced cost base for IT and operational services, the benefits of which started to be realised in 2002. The merger of the lloyds.com and lloydsoflondon web sites in November 2002 has also generated a significant cost reduction in the management of Lloyd's Internet presence.

Lloyd's continues to be a major supporter of the London Market Reform programmes, working in conjunction with the key market associations, which are now beginning to generate improvements in contract clarity, quality and efficiency. By working with organisations such as ACORD, Lloyd's is also helping to ensure that through the standardisation of key processes, the Lloyd's market is well positioned to compete globally in both new and existing markets.

Property

Following the sale of the Lloyd's 1958 building in 2001, work continues with the new owners to conclude the second phase of the contract. This provides for Lloyd's to benefit from any enhanced value as a result of the site being redeveloped. This is dependent upon the formal ratification by the Corporation of London of the planning consent for the new redevelopment on the site of the 1958 building and the agreement of the adjoining Landlords.

The successful conclusion of the Lloyd's 1986 building headlease review in early 2002 has enabled good progress to be made in agreeing tenants' sub-lease rent reviews.

Members' Services

A number of projects have been completed during 2002 enabling improved quality of services to customers. All Members' Services staff have now been co-located in Chatham, where a comprehensive training programme is well underway. A further headcount reduction of over 10% was achieved in 2002, in addition to significant reductions in supplier costs for a variety of services.

Key deadlines were met throughout the year, including efficient processing of a considerable volume of loss payments following

September 11. A full review of all processes was completed to identify improvement opportunities and ensure effective control of operational risk.

Financial review

In 2002 total operating expenses reduced by £18.1m to £159.2m and the Corporation's net assets increased by £4.6m from a previously reported £82.6m at the end of 2001 to £87.2m as at 31 December 2002.

The group operating deficit for the year of £29.9m is reduced from a deficit of £34.2m in 2001, which included a positive contribution of £2.2m from discontinued operations. Consequently, the operating deficit from continuing operations has reduced by £6.5m in 2002. Overall operating expenses from continuing operations in 2002 of £159.2m are £2.1m lower than 2001.

2002 includes the Corporation's first full-year share of the profits of the new ventures established in 2001: XIS and XCS. XIS is a partnership consisting of Xchanging, Lloyd's and the International Underwriting Association. XCS is a joint owned company with Xchanging. The Corporation's share of operating profits before taxation and amortisation of goodwill is £2.9m (2001: loss £0.3m) reflecting the financial success of these ventures in 2002.

In 2001 a profit on the sale of the Lloyd's 1958 building of £25.1m was recognised. A further £1.9m has been recognised in 2002 representing an adjustment to the net book value of the building at the date of disposal.

Centrewrite, a group company which is not consolidated, has declared a dividend of £2.75m for 2002 (2001: £7.3m). The dividend reflects the company's ability to release reserves following the closure of all 1995 and prior open years of account which was facilitated by the Lloyd's run-off and open years project.

Operating income from continuing operations has increased in 2002 to £129.3m from £124.9m in 2001. This includes an increase in the amount received from members' subscriptions of £3.9m, which is based on premium limits. The rate at which members' subscriptions have been charged, 0.25% of premium limits, is unchanged since 2000 having been reduced from 0.35% in 1999.

The Corporation's operating expenses from continuing activities have not increased in 2002. This has enabled the Corporation to finance the development costs of Project Blue Mountain in 2002 of £19.9m (2001: £1.9m) without increasing total costs.

Other factors influencing the Corporation's costs in 2002 include the following:

- Professional and other fees relating to the new Franchise structure totalled £3.3m.
- The costs of defending the Society against litigation remain significant. However, the litigating Names' appeal in the Jaffray action was dismissed in July 2002 and leave to appeal to the House of Lords has been refused.

- A long-term incentive plan was introduced in 1998 for executive directors and senior employees that is related to the results of the Lloyd's market. This scheme helps to ensure that objectives of directors and employees are aligned with those of the Lloyd's market. 2002 is the first year for which payments will be made, over a three-year period, and the accounts reflect a provision of £3.5m, including employers' National Insurance. One third of the amounts payable are discretionary and based on performance.

In setting its budgets for 2003 the Corporation has ensured that sufficient resources will be allocated so that the Franchise is successfully implemented.

The Lloyd's market has since 1997 been subject to a premium levy. This levy was used to repay a £285m syndicated bank loan required as part of the market's contribution to the 1996 *Reconstruction & Renewal* settlement. The loan was repaid in 2001. However, post-September 11, in order to boost the central assets of the Society, the Council decided to continue the premium levy in 2002 and 2003 at an increased rate of 2% for most classes of business, except for life and UK motor business which was reduced to 1%. The entire premium levy cash receipts during 2002 of £246.8m have been transferred to the Lloyd's New Central Fund during the year.

Market settlement recoveries in 2002 were £5.6m (2001: £18.0m) arising principally from debt recovery activity. Lloyd's remains determined to secure the maximum amount available from those Names with outstanding liabilities, and who have the ability to pay.

Cash flows and liquidity

Net funds decreased during 2002 from £66.4m to £42.6m reflecting the Corporation's investment in Project Blue Mountain. There were no bank borrowings, as at 31 December 2002.

Accounting policies

The Corporation's accounting policies are set out in the financial statements and are consistent with the prior year with two exceptions. During the year the Corporation adopted FRS 19 'Deferred Tax'. The impact of the resulting prior year adjustment was the inclusion of a deferred tax asset in the restated 2001 balance sheet. In addition, the Society's collection of paintings, antiques and artefacts has been included in the Corporation's balance sheet as at 31 December 2001 and 31 December 2002 at a valuation of £6.9m. This has also been effected by a prior year adjustment.

The Accounting Standards Board has deferred mandatory implementation of FRS 17 'Retirement Benefits' until 2005 and therefore this Standard has not been adopted by the Corporation. However, transitional disclosures are included in the notes to the financial statements. Under the valuation bases required by FRS17 the Lloyd's Pension Scheme shows a net deficit of £47m, after allowance for deferred taxation, as at 31 December 2002 reflecting the fall in asset values during the year. However, based on actuarial advice, a decision to re-commence making contributions to the

scheme will only be made following the completion of the next formal actuarial review as at 30 June 2004. An asset-liability modelling study of the scheme was undertaken during 2002. The objective of the revised long-term asset allocation strategy is to minimise the potential volatility of future contributions.

Treasury policies

The Corporation's objectives and policies for holding financial instruments and similar contracts, and the strategies for achieving those objectives, are described below.

Interest rate risk

Borrowings from the Lloyd's market for the purpose of funding insurance deposits do not bear a fixed rate of interest. Instead, investment returns earned on the borrowed assets are passed on to lenders. Consequently, no interest rate risk arises on such borrowings. The Corporation had no other significant borrowings at 31 December 2002. Short-term assets held by the Corporation, and related companies, may be significant at certain times but such balances cannot be accurately predicted. These are invested in money-market instruments of up to 12 months in duration with the objective of maximising current income whilst meeting liquidity requirements.

Liquidity risk

The value and term of short-term assets are carefully monitored against those of the Corporation's liabilities. The Corporation aims to maintain sufficient liquid assets to meet liabilities as they fall due. However, a total of £40m of standby committed borrowing facilities, negotiated with leading international banks, were also available to the Corporation as at 31 December 2002. There are no plans to utilise these facilities, which are available to meet unforeseen short-term requirements and are renewed annually.

Foreign currency risk

The Corporation enters into a variety of foreign exchange transactions in response to foreign currency requirements of Lloyd's group companies, as well as facilitating certain transactions in connection with the requirements of the Lloyd's market. In managing the exposures arising from such foreign exchange activity, which may involve transactions for forward settlement, the net risk arising from all such exposures is considered and the level of this risk is managed within closely defined parameters. Consequently, whilst some net foreign exchange exposures may accrue to the Corporation, from time to time, as a result of this activity, the level of such exposures is carefully monitored and is not significant in the context of its combined activities.

Separately, the Corporation provides a Currency Conversion Service (CCS) to participating Lloyd's syndicates, converting insurance premiums and claims between sterling and other Lloyd's settlement currencies as required. Foreign exchange exposures arising from the provision of the CCS are again managed on a net basis, within defined parameters. The CCS is operated separately from other

Operating and financial review continued

foreign exchange activity of the Corporation because, under the terms of the Service, any gain (or loss) arising from CCS exposures is distributed to (or collected from) syndicates participating in the CCS. Currency exposures arising from CCS activity consequently do not, ultimately, represent risks to the Corporation.

Credit risk

A list of permissible bank counterparties, for the purposes of money-market investment, is maintained, and restricted to banks having strong balance sheets and credit ratings. Investment parameters exist for all investment assets, ensuring high credit quality and appropriate risk diversification. Permitted counterparties to capital market transactions are also carefully controlled. All applicable parameters are reviewed regularly by the Lloyd's Investment Committee.

Corporate governance

The Council has overall responsibility for the system of internal control and for reviewing its effectiveness. The Corporation's executive team is responsible for the implementation and maintenance of the internal control system. This incorporates an embedded, ongoing process for identifying, evaluating and managing significant business, operational, financial, compliance and other risks. The system is designed to reduce, rather than eliminate, the risk of failure to achieve business objectives and can only provide reasonable but not absolute assurance against material misstatement or loss.

The Audit Committee, on behalf of Council, monitors the effectiveness of the system of internal control of the Corporation. Lloyd's maintains an internal audit function that reports to the Audit Committee. The external auditors also contribute an independent perspective on aspects of financial control and annually report their findings to the Audit Committee and the Council.

An annual budget for the Corporation is reviewed in detail by the executive team and, during 2002 and earlier years, was approved by the Lloyd's Market Board and Council. In 2003 the Franchise Board will consider the Corporation's finances. Monthly financial reports compare actual performance with the annual budget and management action is taken where variances arise. Revised forecasts are prepared at least quarterly.

The operation of effective risk management is the responsibility of all managers. This is kept under review by Internal Audit and the Internal Control Committee (from January 2003, the Operations Executive), which is responsible for ensuring that the Corporation maintains effective and efficient internal control, and compliance with FSA and related requirements. In 2002 Internal Audit services were provided to the Corporation by Ernst & Young LLP, the Corporation's external auditors. Whilst the Internal Audit team were entirely separate from the external audit team, in recognition of developing best practice, this arrangement ceased at the end of 2002 and,

after a competitive tender, KPMG LLP were appointed. As part of these arrangements KPMG LLP will provide a full-time Head of Internal Audit. The Corporation is committed to the highest standards of business conduct and has a clearly defined organisational structure.

Going concern

As part of its normal business practice the Council of Lloyd's has considered whether it is appropriate to prepare the Corporation's financial statements on a going concern basis. The Corporation prepares annual and longer-term plans and in reviewing this information the Council of Lloyd's sees no reason why the Corporation should not remain as a going concern for the foreseeable future. Therefore the Corporation continues to adopt the going concern basis in preparing the financial statements.

Employment policy

Communications and employee involvement

The Corporation actively promotes the understanding and involvement of employees in the business objectives of Lloyd's by a variety of means. Currently these include: Chief Executive Officer briefings for all employees at open forums; regular team meetings to keep employees informed and to provide feedback to management; and a Corporation Intranet (C-net) which provides information rapidly to all employees and also for employees to communicate directly with the Chief Executive Officer.

Equal opportunities

The Corporation takes steps to ensure that all applicants and employees receive equal treatment regardless of sex or sexual orientation, race, colour, ethnic or national origins, religion, marital status or disability.

The Corporation does not just avoid discrimination as required by law, but adopts policies and practices which treat as irrelevant all factors which do not genuinely affect a person's capability to undertake the work in question. The only criteria in selecting employees for recruitment, promotion and development are capability and performance.

The Corporation is a member of the 'Opportunity Now' campaign which works with employers to realise the economic potential and business benefits that women contribute to the workplace and, more generally, encourages diversity and an inclusive culture in the workplace.

Training and development

The Corporation actively encourages employees to obtain relevant qualifications and to develop their full potential. Training and development is available to all staff. A system of internal job advertising is in place and internal transfer and promotion fill many vacancies. Training is provided to facilitate the implementation of Lloyd's values and capabilities aimed at promoting a more commercial culture and improved performance.

Report of the Nominations, Appointments and Compensation Committee

The Council of Lloyd's is assisted in determining the remuneration of members of the Council, and its subsidiary boards and committees by the Nominations, Appointments and Compensation Committee (NACC). The NACC also recommends for approval by the Council, fees, salaries, bonuses and the terms and conditions of the Chairman of Lloyd's and the Chief Executive Officer and also reviews those of the five most senior executives in the Corporation.

This report is based upon best practice as set out in the Combined Code in respect of remuneration disclosures. This code is directed at companies listed on the Stock Exchange, whereas Lloyd's is responsible for the superintendence of a market of many separate and competing trading entities; nonetheless, Council supports its principles in so far as they apply to the governance of the Society.

Composition of NACC

The NACC currently comprises three nominated, three working and two external members of the Council as shown on pages 8 and 9. John Young and Bill Loschert served on the Committee during 2002.

Remuneration policy

Lloyd's remuneration policy for all employees is set out in the Personnel Manual as follows:-

'To provide a package (salary plus benefits) which is competitive, innovative and fair. The remuneration policy is also founded on the proposition that the ultimate source of value is people, which means a reward system that responds creatively to employee needs as well as those of the business. This means a policy which:

- emanates from business strategies and goals;
- is based on business success (ability to pay);
- provides a balanced mix of rewards which will attract, retain and motivate the varied range of experience and skills required by the organisation;
- is externally competitive and regularly monitored by means of salary surveys;
- rewards for performance not cost of living or position in hierarchy.'

Bonuses, which are discretionary, are awarded for performance judged annually against demanding business objectives. The NACC's policy is that an increasing proportion of executive remuneration should be at risk and determined by performance review. A long-term incentive plan was introduced in 1998 which links a proportion of the remuneration of the Chief Executive Officer and senior Corporation executives to the overall profitability of the Lloyd's market. Payments under the scheme will be made for the first time during 2003 with respect to the 2002 year of account.

The Corporation, on behalf of the NACC, engaged remuneration consultants, Watson Wyatt LLP, to assist the NACC in its annual review of executive remuneration to make reference to the terms and conditions prevailing in other comparable organisations operating in the financial services sector.

Remuneration for non-executive positions is designed to attract people of sufficient calibre and experience to govern Lloyd's affairs by providing an appropriate level of fees which reflects the demands made upon them. Reference is also made to independent surveys of fees for non-executive directors of significant private sector organisations.

Levels of remuneration

Saxon Riley, who was Chairman of Lloyd's until November 2002, was appointed on a part-time basis and provided his services for three days per week, on average. His fees, which were non-pensionable, were £300,000 per annum (£200,000 per annum during 2001) and the cost of his benefits were £41,000. He was awarded a bonus of £150,000 for his performance during 2002 (£100,000 in 2001).

The current Chairman, Peter Levene, was elected in November 2002. His fees are £400,000 per annum plus a pension contribution of £34,000 per annum.

The salary of the Chief Executive Officer, Nick Prettejohn, was £410,000 per annum in 2002 (£360,000 per annum in 2001) and the value of his benefits (car and medical insurance) was £11,000. He was awarded a bonus of £200,000 for his performance during 2002 (£150,000 in 2001), and was awarded a discretionary performance award under the long-term incentive plan of £110,000 in respect of 2002 and will receive three further payments in October 2003, October 2004 and October 2005 currently projected at £68,000 each.

Nick Prettejohn is a member of the Lloyd's Pension Scheme and his benefits are subject to the Inland Revenue 'cap'. His accrued benefits are shown below:

- Accrued Pension as at 1 January 2002 £16,139 per annum
- Accrued Pension as at 31 December 2002 £18,880 per annum
- Increase in accrued pension over the year £2,741 per annum
- Transfer Value as at 1 January 2002 £129,621
- Transfer Value as at 31 December 2002 £157,134
- Change in Transfer Value £25,513

In addition Nick Prettejohn has a contribution to a Funded Unapproved Retirement Benefit Scheme (FURBS) of 20% of his salary, grossed up for tax.

Report of the Nominations, Appointments and Compensation Committee

continued

The Chairman of the Lloyd's Regulatory Board during 2002, John Young, who was also a Deputy Chairman of Council, received fees at the rate of £78,750 per annum in 2002 (£75,000 per annum in 2001). The fees for the other Deputy Chairmen of Council were £26,250 per annum (£25,000 in 2001).

Fees for sitting on Council, Lloyd's Market Board (LMB), Lloyd's Regulatory Board (LRB) and Committees were increased by 5% in 2002 having remained unchanged since 2000. The fees for members of Council were £21,000 per annum. Council members who also sat on LMB or LRB received an additional £5,250 per annum. A further £2,625 per annum was paid to those attending Council or LRB Committees, while the people who chaired these Committees received £5,250 per annum.

Contracts of employment

External and working members are elected and nominated members are appointed to Council, usually for a three year period. This is not a contractual arrangement and compensation is not paid if a member leaves early. The Chairman and two Deputy Chairmen are elected by the Council on an annual basis.

The current Chairman of Lloyd's works part-time for the Society and he has a three year service agreement, which may be extended by mutual agreement, and is subject to a 12 month notice period. The contract of the Chief Executive Officer, who works full time, has a one year notice period.

Alastair Ross Goobey

Chairman

Nominations, Appointments and Compensation Committee

Members of the Council of Lloyd's and Lloyd's Market & Regulatory Boards 2002

Council of Lloyd's	Lloyd's Market Board	Lloyd's Regulatory Board
Working members		
Saxon Riley (replaced by Lord Levene of Portsoken November 2002) (Chairman of Lloyd's)	Nick Prettejohn (Chairman of Lloyd's Market Board)	John Young (Chairman of Lloyd's Regulatory Board)
John Coldman† (Deputy Chairman of Lloyd's)	Gilles Bonvarlet	Brian Pomeroy (Deputy Chairman of Lloyd's Regulatory Board)
Bronek Masojada† (Deputy Chairman of Lloyd's)	Brian Carpenter	Rupert Atkin
Stephen Catlin†	Simon Clapham	John Barber
Graham McKean	Christine Dandridge	Lady Delves Broughton
David Robson	Michael Dawson	David Gittings (resigned March 2002)
	David Foreman	Anthony Howland Jackson
External members	David Gittings (resigned March 2002)	Paul Kelly
Wellington (Five) Limited (represented by Julian Avery)	Nigel Hanbury	Bill Knight
Paul Kelly	Judith Hanratty	Bill Loschert
ACE Capital Limited (represented by Bill Loschert †)	Julian James	Andrew Moss (appointed April 2002)
Peter Morgant*	Graham McKean	David Robson
Amlin Corporate Member Limited (represented by Charles Philipps)	Peter Morgan	Alastair Ross Goobey
Camperdown UK Limited (represented by Michael Schell, replaced by Kent Urness in June 2002)	Andrew Moss	John Stace
	Charles Philipps	Paul Swain
	Gary Schmalzriedt	Anthony Townsend
	Roger Sellek	
Nominated members		
Judith Hanratty†*		
Bill Knight*		
Brian Pomeroy*		
Nick Prettejohn (Chief Executive Officer)		
Alastair Ross Goobey†		
John Young† (Deputy Chairman of the Council of Lloyd's)		

† Member of the Nominations, Appointments and Compensation Committee

* Member of the Audit Committee

Statement of Lloyd's responsibilities in respect of the financial statements

Byelaws made under Lloyd's Act 1982 require Lloyd's to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Corporation and of the surplus or deficit for that period. The financial statements are required to be approved by the Council of Lloyd's. The Council has determined that in preparing those financial statements it is appropriate to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Corporation will continue in business.

Lloyd's is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Corporation. The Council is responsible for safeguarding the assets of the Corporation and hence taking reasonable steps for the prevention and detection of fraud and other irregularities.

Independent auditor's report to the members of Lloyd's

We have audited the financial statements for the year ended 31 December 2002 which comprise the consolidated revenue account, consolidated balance sheet, consolidated cash flow statement, consolidated statement of total recognised gains and losses and the related notes 1 to 28. These financial statements have been prepared on the basis of the accounting policies set out therein.

This report is made solely to the members of Lloyd's, as a body, in accordance with the Council of Lloyd's instructions to us as set out under 'Respective responsibilities of Lloyd's and auditors' below. Our audit work has been undertaken so that we might state to the members of Lloyd's as a body, those matters we are required to state to them in this report in accordance with the Council's instructions and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Corporation and the members of Lloyd's as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Lloyd's and auditors

As described in the Statement of Lloyd's Responsibilities, Lloyd's is responsible for the preparation of the financial statements which are approved by the Council of Lloyd's. The Council of Lloyd's has instructed us to audit the financial statements in accordance with United Kingdom Auditing Standards and report to you our opinion as to whether the financial statements give a true and fair view. We also report to you if, in our opinion, Lloyd's has not kept proper accounting records, or if we have not received all the information and explanations we require for our audit.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by Lloyd's in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Corporation's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Corporation as at 31 December 2002 and of its result for the year then ended.

Ernst & Young LLP

Registered Auditor
London
2 April 2003

Consolidated revenue account

for the year ended 31 December 2002

	Note	2002 £000	Restated 2001 £000
Operating income			
Continuing operations		129,263	124,918
Discontinued operations		–	18,251
Total operating income	3	129,263	143,169
Operating expenses			
Continuing operations		(159,154)	(161,279)
Discontinued operations		–	(16,065)
Total operating expenses	4	(159,154)	(177,344)
Operating (deficit)/surplus			
Continuing operations		(29,891)	(36,361)
Discontinued operations		–	2,186
Group operating deficit		(29,891)	(34,175)
Share of operating profits of associates	14	2,873	216
Share of exceptional items of associates	14	–	(495)
Amortisation of goodwill of associates	14	(118)	(78)
Total operating deficit		(27,136)	(34,532)
Profit on sale of the Lloyd's 1958 building – continuing operations	12	1,926	25,069
Deficit on ordinary activities before interest		(25,210)	(9,463)
Interest and dividend income			
Dividends receivable from non-consolidated subsidiaries	14	2,750	7,300
Interest income:	7		
Group		5,022	7,809
Associates		174	80
Interest payable:	7		
Group		(3,322)	(5,384)
		4,624	9,805
Premium levy income	8	256,147	119,855
Market settlement recoveries	8	5,633	17,996
Transfers to Lloyd's New Central Fund	9	(246,809)	(80,000)
Exchange gain on syndicated bank loan		–	142
(Deficit)/surplus before taxation		(5,615)	58,335
Taxation credit/(charge)	10	1,498	(491)
(Deficit)/surplus for the year		(4,117)	57,844

The consolidated revenue account for the year ended 31 December 2001 has been restated for the adoption of FRS19 (see note 10).

Consolidated statement of total recognised gains and losses

for the year ended 31 December 2002

Note	2002 £000	Restated 2001 £000
(Deficit)/surplus for the year		
Group	(6,157)	58,181
Associates	2,040	(337)
Total (deficit)/surplus for the financial year	(4,117)	57,844
Unrealised gain on disposal of subsidiaries	25 554	4,805
Total recognised (losses)/gains relating to the year	24 (3,563)	62,649
Prior year adjustment (as explained in note 1)	1,155	
Prior year adjustment (as explained in note 2B)	6,913	
Total recognised gains since last consolidated report	4,505	

The consolidated statement of total recognised gains and losses for the year ended 31 December 2001 has been restated for the adoption of FRS19 (see note 10) and for the change in accounting policy in respect of the valuation of other investments (see note 14c).

Consolidated cash flow statement

for the year ended 31 December 2002

	Note	2002 £000	2001 £000
Cash flow from operating activities	22	(25,429)	27,445
Returns on investments and servicing of finance	22	1,733	7,604
Taxation		1,228	13,304
Capital expenditure and financial investment:			
Purchase of tangible fixed assets	22	(2,321)	(4,614)
Sale of tangible fixed assets	22	378	49,968
Acquisitions and disposals	22	-	(18,206)
Cash (outflow)/inflow before use of liquid resources and financing		(24,411)	75,501
Management of liquid resources	22	18,640	2,678
Financing	22	6,142	(97,627)
Increase/(decrease) in cash in the year		371	(19,448)
Reconciliation of net cash flow to movement in net funds (note 22)			
Increase/(decrease) in cash in the year		371	(19,448)
Cash (inflow)/outflow from decrease in financing		(6,142)	97,627
Cash inflow from decrease in liquid resources		(18,640)	(2,678)
Change in net funds resulting from cash flows		(24,411)	75,501
Other movements	22	641	1,013
Movement in net funds in the year		(23,770)	76,514
Net funds/(debt) at 1 January		66,407	(10,107)
Net funds at 31 December	22	42,637	66,407

Notes to the financial statements

as at 31 December 2002

1 Purpose of financial statements

Basis of preparation and consolidation and change in accounting policy

The Society of Lloyd's was incorporated under Lloyd's Act 1871 and is subject to the provisions of Lloyd's Acts 1871 to 1982.

The purpose of the financial statements is to demonstrate the income and expenditure, financial position and cash flows of the Corporation of Lloyd's to members in their capacity as members. The financial statements exclude all insurance-related activities arising from members' underwriting at Lloyd's. In meeting this objective certain operating subsidiaries are consolidated whilst others, principally Lioncover Insurance Company Limited and Centrewrite Limited, are excluded since their activities relate to running off the underwriting affairs of certain syndicates and Names. The Council considers that to consolidate such results would be misleading in presenting the financial position of the Corporation of Lloyd's to its membership. For the same reasons the Central Fund, which is held at the Council's direction, has not been consolidated, as it is primarily a fund available for the protection of policyholders. However, the Central Fund financial statements describe how its assets may be used to cover members' solvency shortfalls. In the last resort, the Corporation's assets may also be used for this purpose at the discretion of Council.

Funds administered by the Corporation of Lloyd's on behalf of trustees, or held at the Council's direction as part of the security underlying policies issued at Lloyd's, are not included in the financial statements.

Except for the matters described above, the financial statements have been prepared under the historical cost convention as modified by the revaluation of investments and, in all material respects, in accordance with applicable accounting standards.

FRS13 'Derivatives and other financial instruments – disclosures' has not been adopted as it does not apply to the Corporation. However, certain voluntary disclosures have been given in *note 23*.

The effective date for the full adoption of FRS17 'Retirement benefits' has been deferred until 1 January 2005. The Corporation has not adopted the standard early but has made the transitional disclosures required by the standard in *note 18*.

FRS19 'Deferred Tax' has been adopted and disclosures given in *note 10*. The adoption of FRS19 has resulted in a change in accounting policy for deferred tax. Deferred tax is recognised on a full provision basis in accordance with the accounting policy described in *note 2G*. Previously, deferred tax was provided for on a partial provision basis, whereby provision was made on all timing differences to the extent that they were expected to reverse in the future without replacement. The change in accounting policy has resulted in a prior year adjustment and the restatement of 2001 comparatives. The accumulated reserves at 1 January 2001 have been increased by £1,992,000 and the tax charge for the year ended 31 December 2001 has been increased by £837,000. As a result the previously reported accumulated reserves as at 31 December 2001 of £82,646,000 are increased to £83,801,000 by the inclusion of a deferred tax asset of £1,155,000. The deficit for the current year has been increased by £473,000 as a result of the change in accounting policy.

Lloyd's is regulated by the Financial Services Authority (FSA).

2 Principal accounting policies

A Tangible fixed assets and depreciation

Fixed assets are included at cost.

Freehold land is not depreciated. Depreciation is provided on other assets at rates calculated to write off, on a straight-line basis, the cost less estimated residual value over their expected useful lives. The principal categories of assets and their expected useful lives are as follows:

Freehold buildings	60 years
Plant	15 or 25 years
Fixtures, fittings, furniture, computers, software and equipment	2 to 10 years
Motor vehicles	4 years

Costs incurred in acquiring and developing computer software for internal use are capitalised as tangible fixed assets where the software supports a significant business system and the expenditure leads to the creation of an identifiable durable asset.

The carrying values of tangible fixed assets are reviewed for impairment if events or changes in circumstances indicate the carrying values may not be recoverable.

2 Principal accounting policies continued

B Investments

Statutory insurance deposits comprise securities and cash deposits maintained in the United Kingdom and various overseas countries to comply with local insurance regulations. Investments are shown at market value at the balance sheet date and profits and losses arising on revaluation are dealt with in the consolidated revenue account.

In the consolidated accounts, shares in associates are accounted for using the equity method. The consolidated revenue account includes the group's share of the pre-tax profits and attributable taxation of the associates based on financial statements for the year. In the consolidated balance sheet, the investment in associates is shown as the group's share of the net assets of the associates and any associated goodwill.

Other investments represent Lloyd's collection of various paintings, antiques and artefacts gifted to or acquired by the Society and are included at market valuation. The collection will be revalued at least every three years. This represents a change in accounting policy and has resulted in a prior year adjustment of £6,913,000 (*see note 14c*). Previously, this collection was not valued.

C Acquisitions and disposals

On the acquisition of a business, including an interest in an associate, fair values are attributed to the group's share of the net separable assets acquired. Where the cost of the acquisition exceeds the fair values attributable to such net assets, the difference is treated as purchased goodwill and capitalised in the balance sheet in the year of acquisition and amortised over the estimated useful life.

D Stocks

Stocks are stated at the lower of cost, on a first-in first-out basis, and net realisable value.

E Income

Income is attributable to the continuing activity of the provision of services and infrastructure principally for the operation of the Lloyd's insurance market.

Income, which is stated net of value added tax, represents amounts invoiced for goods and services provided, including members' subscriptions and application fees for corporate members.

Income excludes local premium taxes in connection with overseas underwriting activities.

F Pension costs

The expected cost of pensions in respect of the defined benefit pension scheme operated by the Corporation of Lloyd's is charged to the consolidated revenue account so as to spread the cost over the service lives of employees in the scheme. Variations from regular cost are spread over the expected remaining service lives of current employees to the extent that the resulting credit does not exceed the regular cost. The pension cost is assessed in accordance with the advice of qualified actuaries.

G Taxation

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date will result in an obligation to pay more, or a right to pay less or to receive more, tax.

Deferred tax assets are recognised only to the extent that it is considered that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted. Deferred tax is measured on an undiscounted basis at the rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantially enacted at the balance sheet date.

H Foreign currency and derivative instruments

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities are retranslated at the rate of exchange ruling at the balance sheet date.

The Corporation and its consolidated subsidiaries enter into forward currency contracts to manage exposures to fluctuation in foreign exchange rates, and to provide a service to the Lloyd's market.

Where contracts are entered into to cover foreign exchange exposure, any variances between closing and contracted rates are included in the balance sheet.

Where contracts are entered into to provide a service to the Lloyd's market, these are marked-to-market at the year-end closing rate. Where gains or losses are not expected to be refunded to or recovered from the Lloyd's market, these amounts are taken to the consolidated revenue account.

Notes to the financial statements continued**2 Principal accounting policies** continued

The principal year end exchange rates were:

	2002	2001
US\$	1.61	1.46
Can\$	2.54	2.32
Euro	1.53	1.63

3 Operating income

	2002 Total Continuing £000	2001 Continuing £000	2001 Discontinued £000	2001 Total £000
Market charges				
Managing agents and syndicates	50,776	49,242	18,153	67,395
Members and members' agents	14,888	15,313	–	15,313
Regulatory levy	8,798	8,520	–	8,520
	74,462	73,075	18,153	91,228
Members' subscriptions	31,600	27,687	–	27,687
Other income				
Equitas	286	595	–	595
Rent and building service charges	6,555	8,006	–	8,006
Charges to associates	9,967	7,333	–	7,333
Income from other services	6,393	8,222	98	8,320
	23,201	24,156	98	24,254
Total operating income	129,263	124,918	18,251	143,169

4 Operating expenses

	2002 Corporation Continuing £000	2002 Project Blue Mountain Continuing £000	2002 Total £000	2001 Continuing £000	2001 Discontinued £000	2001 Total £000
Operating expenses include:						
Employment costs (<i>note 5</i>)	39,865	7,377	47,242	36,530	8,263	44,793
Overseas operating expenses (<i>note 6</i>)	21,497	–	21,497	22,112	–	22,112
Professional fees, including legal fees and related costs	17,477	1,490	18,967	26,869	79	26,948
Operating lease rentals – land and buildings	16,867	–	16,867	19,475	–	19,475
Provisions for travel insurance dispute (<i>note 21</i>)	100	–	100	4,901	–	4,901
Audit fee	95	13	108	63	42	105
Other audit services payable to Ernst & Young LLP	741	–	741	187	–	187
Other fees payable to Ernst & Young LLP	1,144	75	1,219	1,316	66	1,382
Depreciation (<i>note 11</i>)	2,425	18	2,443	4,297	169	4,466
Charitable donations	255	–	255	227	–	227

The costs of Project Blue Mountain during 2002 total £19.9m (2001:£1.9m; including employment costs £0.4m and legal and professional fees £1.3m) and have been included in operating expenses. Further details of the activities of Project Blue Mountain are given in the Chief Executive Officer's report on pages 55 to 57.

5 Employment	2002 £000	2001 £000
Salaries and wages (including performance-related bonus)	27,355	31,866
Long-term incentive plan (excluding social security costs – see note 21)	3,100	–
Pension costs	578	330
Social security costs	3,154	3,208
Severance costs	950	2,362
Contract and agency staff	7,619	2,936
Other employment costs	4,486	4,091
	47,242	44,793

	2002 Number	2001 Number
Average numbers of employees during the year	589	825

The emoluments of the Chairman, Chief Executive Officer, members of Council, Market Board and Regulatory Board are included in the report of the Nominations, Appointments and Compensation Committee on pages 61 and 62.

6 Overseas operating expenses	2002 £000	2001 £000
Expenses in connection with underwriting activities in the following areas:		
USA	8,714	8,612
Canada	5,056	6,147
Asia	3,579	3,674
Europe	3,061	2,720
Africa, Australasia, Central and South America	1,087	959
	21,497	22,112
Operating expenses include:		
Employment	5,125	4,855
Legal and professional	6,214	7,072
Systems and communication	4,444	5,580
Premises	1,673	1,713
Other expenses	4,041	2,892
	21,497	22,112

Local premium taxes amounting to £17.7m in 2002 (2001: £18.2m) have been excluded on the basis that the Corporation of Lloyd's is acting only as intermediary between the Lloyd's market and overseas statutory bodies.

Notes to the financial statements continued

7 Interest		Other interest £000	Insurance deposits £000	2002 Total £000	2001 Total £000
Group		1,597	3,425	5,022	7,809
Associates		174	–	174	80
Total interest receivable		1,771	3,425	5,196	7,889
Interest payable:					
Group	Bank loans/overdrafts	(129)	–	(129)	(2,197)
	Other loans	–	(3,127)	(3,127)	(3,505)
	Foreign exchange movement	–	(66)	(66)	318
		(129)	(3,193)	(3,322)	(5,384)

8 Premium levy income and market settlement recoveries		2002 £000	2001 £000
Premium levy income:			
Receivable at 1 January		(9,297)	(8,809)
Collected and paid to banks to repay syndicated bank loan		–	80,238
Continued levy collections		250,926	40,621
Receivable at 31 December		18,635	9,297
Refundable in respect of return premiums at 31 December		(4,117)	(1,492)
		256,147	119,855

The syndicated bank loan was repayable out of a premium levy of 1.1% on premiums written in the Lloyd's market. The Council of Lloyd's agreed to continue to collect the premium levy after the syndicated bank loan was fully repaid in September 2001. In 2002 the premium levy was increased to 2% of premiums received for most classes of business (1% for UK motor and life business). All premium levy collections in 2002, net of amounts refundable in respect of returned premiums, have been transferred to the Lloyd's New Central Fund (see note 9).

	2002 £000	2001 £000
Market settlement recoveries	5,633	17,996

During 1997 Lloyd's discharged its obligation to fund Equitas in accordance with the *Reconstruction & Renewal* Completion Agreement dated 3 September 1996. The market settlement has continued to generate recoveries in 2002, principally from debt recovery activity, which have been credited to income.

9 Transfers to Lloyd's New Central Fund

The Corporation of Lloyd's transferred £246.8m to the Lloyd's New Central Fund during 2002 representing the premium levy received during the year net of amounts to be refunded (2001:£80m, including premium levy received after the syndicated bank loan had been repaid).

10 Taxation	2002 £000	Restated 2001 £000
(a) Analysis of charge in year		
<i>Current tax:</i>		
UK corporation tax based on profits for the year at 30% (2001: 30%)	–	(1,326)
Current year group tax relief from non-consolidated subsidiary	(1,738)	–
<i>Prior year adjustments:</i>		
Tax credits arising from release of prior year provisions	4,624	553
Group tax relief from non-consolidated subsidiary	–	1,191
Foreign tax suffered	(26)	(12)
Share of associate undertakings' current tax	(889)	(60)
Total current tax (<i>note 10b</i>)	1,971	346
<i>Deferred tax:</i>		
Origination and reversal of timing differences	(473)	(837)
Taxation credit/(charge)	1,498	(491)
(b) Factors affecting current tax charge		
The tax assessed for the year is lower than the standard rate of corporation tax in the UK of 30%.		
The differences are explained below:		
(Deficit)/surplus on ordinary activities before tax	(5,615)	58,335
(Deficit)/surplus on ordinary activities multiplied by standard rate of corporation tax in UK of 30%	1,685	(17,501)
Non-taxable and non-deductible items	5,317	16,103
Capital allowances for the year in excess of depreciation	(407)	–
Prior year adjustments	(4,624)	1,744
Current tax credit (<i>note 10a</i>)	1,971	346
(c) Deferred tax		
A deferred tax asset has been recognised in respect of the following timing differences:		
Accelerated capital allowances	682	1,155
Deferred tax asset at 31 December	682	1,155
At 1 January	1,155	1,992
Deferred tax charge in consolidated revenue account (<i>note 10a</i>)	(473)	(837)
At 31 December (<i>see note 17</i>)	682	1,155

Notes to the financial statements continued

	Freehold land and buildings £000	Plant and other fixed assets £000	Total £000
11 Fixed assets			
Cost:			
At 31 December 2001	10,413	60,430	70,843
Additions	–	2,269	2,269
Disposals	–	(17,675)	(17,675)
At 31 December 2002	10,413	45,024	55,437
Depreciation:			
At 31 December 2001	3,176	53,012	56,188
Charge for the year	125	2,318	2,443
Disposals	–	(17,487)	(17,487)
Adjustments to brought forward depreciation	–	(1,926)	(1,926)
At 31 December 2002	3,301	35,917	39,218
Net book value:			
At 31 December 2002	7,112	9,107	16,219
At 31 December 2001	7,237	7,418	14,655

Included in freehold land and buildings is land valued at £2.5m (2001:£2.5m) which has not been depreciated in the year.

12 Profit on sale of the Lloyd's 1958 building

On 8 February 2001 the Corporation entered into an agreement with a subsidiary of British Land plc for the sale and the simultaneous leaseback of the Lloyd's 1958 building. The leaseback expired on 31 December 2001 and Lloyd's vacated the building on that date.

In 2001 a profit on the sale of the Lloyd's 1958 Building of £25.1m was recognised. A further £1.9m has been recognised in 2002 representing an adjustment to the net book value of the building at the date of disposal. The sale agreement provides for Lloyd's to benefit from any enhanced value as a result of the site being redeveloped.

13 Principal investments in subsidiary companies and associates

Entity	Nature of business	Proportion of equity capital held
Subsidiaries		
Additional Securities Limited	Provision of deposits overseas on behalf of Lloyd's underwriters to comply with local insurance regulations	100%
Centrewrite Limited	Authorised UK insurance company	100%
Lioncover Insurance Company Limited	Authorised UK insurance company	100%
lloyds.com Limited (Project Blue Mountain)	Web-based network to connect insurance industry participants and enable international transfer of commercial lines insurance risks	100%
Associates		
Ins-sure Holdings Limited	Provision of premiums and claims accounting and settlement, policy production and ancillary insurance services principally to the London insurance market	25%
Xchanging Claims Services Limited	Provision of claims and recoveries services	50%

Centrewrite and Lioncover are not consolidated (see note 14b).

During 2001 the Corporation acquired interests in Ins-sure Holdings Limited and Xchanging Claims Services Limited.

13 Principal investments in subsidiary companies and associates continued

The issued share capital of Ins-sure Holdings Limited is £4,000. There are three separate classes of shares. The Corporation holds 1,000,000 B shares of 0.1p each that have the following rights with respect to dividends:

- A maximum dividend accrual right of £924,000 following a capital reduction by LPSO Limited. This dividend was received during 2002.
- The B shares participate in 25% of any profits available for distribution after taking account of the dividend rights outlined above.
- In addition, the B shares carry a right to the first £3,000,000 of dividends that would have accrued to the holders of the C shares.

The issued share capital of Xchanging Claims Services Limited is £4,001. There are three separate classes of shares. The Corporation holds 1,000 A shares of £1 each and 2,501 C shares of £1 each. The A and C shares have the following rights with respect to dividends:

- The C shares carry a right to a fixed cumulative preference dividend of 5% calculated on the nominal capital and a variable participating dividend calculated by reference to trading profits.
- A maximum dividend accrual right of £1,500,000 accrues to the A shares provided that a capital reduction by LCO Marine Limited takes place before 31 December 2002. The accrual right in any financial year is equal to the amount of the release during that year of any undertaking given to the court by LCO Marine Limited in favour of its creditors, provided that the aggregate of all dividend rights does not exceed £1,500,000.
- The A shares participate in 50% of any profits available for distribution after taking account of the dividend rights outlined above.

14 Investments

a) Investments in associates	Share of other			2001 £000
	Goodwill £000	net assets £000	2002 £000	
At 1 January / on acquisition	1,097	2,894	3,991	4,328
Share of operating profits	-	2,873	2,873	216
Share of exceptional items	-	-	-	(495)
Amortisation of goodwill	(118)	-	(118)	(78)
Share of interest income	-	174	174	80
Share of tax on profit/loss on ordinary activities	-	(889)	(889)	(60)
At 31 December	979	5,052	6,031	3,991

Goodwill is being amortised over 10 years

b) Subsidiary companies not consolidated	2002 £000	2001 £000
Shares of non-consolidated subsidiary companies at cost	44	44
Current accounts	46	77
	90	121

Non-consolidated insurance related subsidiaries 2002 balance sheet summary	Centrewrite £000	Lioncover £000	Total £000
Investments	64,224	-	64,224
Current assets	6,380	29	6,409
Current liabilities	(5,328)	(28)	(5,356)
	65,276	1	65,277
Insurance fund	(32,666)	-	(32,666)
Shareholders' funds at 31 December 2002	32,610	1	32,611
Shareholders' funds at 31 December 2001 (restated)	30,876	1	30,877
Retained profit for the year	1,734	-	1,734

Dividends amounting to £2.75m have been proposed by Centrewrite in respect of the year ended 31 December 2002 (2001:£7.3m proposed and paid).

Notes to the financial statements continued

14 Investments continued

Centrewrite Limited

Centrewrite, an authorised UK insurance company, was formed to reinsure individual syndicate years of account in run-off and individual members of such syndicates. In addition, it offers an estate protection plan to Names.

Lioncover Insurance Company Limited

Lioncover, an authorised UK insurance company, was formed to reinsure the liabilities of Names on syndicates formerly managed by PCW Underwriting Agencies Limited, WMD Underwriting Agencies Limited and Richard Beckett Underwriting Agencies Limited, and on syndicates 2 and 49 (collectively referred to as the PCW syndicates). On 18 December 1997 all of Lioncover's reinsurance liabilities were reinsured to Equitas Reinsurance Limited.

The financial statements of Lioncover are drawn up to 31 March. As these financial statements are not yet available the figures on the previous page have been produced from management accounts as at 31 December 2002.

c) Other investments

Other investments represent Lloyd's collection of various paintings, antiques and artefacts gifted to or acquired by the Society. They have been included in the balance sheet at 31 December 2002 at an open market valuation of £6,913,000 (2001: £6,913,000). Their inclusion arises as a result of a change in accounting policy in which this collection had not been previously valued. The collection was valued on 8 March 2002 on the basis of open market auction value assuming all items are not sold at the same time taking into account the nature, age, condition and quality of each chattel, by L&J Gull Fine Arts Limited, professional valuers and consultants.

We have no reason to believe that the valuation prepared in March 2002 would have been materially different as at 31 December 2001. A prior year adjustment of £6,913,000 has been included to reflect this change in accounting policy.

	2002 £000	2001 £000
15 Statutory insurance deposits		
Held by subsidiary companies:		
Statutory insurance deposits	67,016	57,757
Funding provided by syndicates and Equitas	(61,586)	(53,665)
	5,430	4,092

	Securities £000	Cash deposits £000	2002 Total £000	2001 Total £000
Statutory insurance deposits				
Market value at 1 January	35,547	22,210	57,757	55,836
Additions at cost	31,436	61,583	93,019	75,635
Disposal proceeds	(28,814)	(57,366)	(86,180)	(73,815)
(Loss)/gain on disposal	(440)	(1,450)	(1,890)	148
Year end revaluation	2,804	1,506	4,310	(47)
Market value at 31 December	40,533	26,483	67,016	57,757

	2002		2001	
	Cost £000	Valuation £000	Cost £000	Valuation £000
Analysis of securities at year end - statutory insurance deposits				
Listed on:				
London Stock Exchange	1,009	992	4,178	4,158
Overseas stock exchanges	33,899	35,920	28,420	28,062
	34,908	36,912	32,598	32,220
Unlisted:				
Fixed interest	3,235	3,621	3,728	3,327
	38,143	40,533	36,326	35,547

15 Statutory insurance deposits continued

Basis of valuation: listed fixed and floating rate securities are valued at their quoted market price at the balance sheet date.

Unlisted fixed interest securities are valued as follows:

	2002 £000	2001 £000
Foreign treasury bills – at market value	3,076	2,566
Foreign government debentures – at par and market value	545	761
	3,621	3,327

Funding provided by syndicates and Equitas

These amounts comprise floating rate advances in foreign currencies and sterling repayable within one year:

	2002 £000	2001 £000
Equitas	–	(1,464)
Lloyd's market – deposit	(61,586)	(52,201)
	(61,586)	(53,665)
Allocated:		
Financing of underwriting deposits	(56,384)	(48,463)
Working capital	(5,202)	(5,202)
	(61,586)	(53,665)

Finance is arranged by advances from syndicates in the Lloyd's market and from Equitas. These advances are renewed annually.

By agreement with the lenders, investment returns earned on these assets, are paid, in appropriate proportions, to the lenders.

In this way, the Corporation avoids any risk arising from a mismatch between borrowing and lending terms (see note 23).

The terms and conditions of these advances are governed by the Membership (Overseas Deposits) Byelaw (No 2 of 1992) which enables the Council of Lloyd's to vary the amount, term and rate of interest of these loans, as appropriate. The provision of funds by members under this Byelaw is in respect of the establishment and maintenance of overseas deposits and is a condition of permission to underwrite insurance business at Lloyd's.

16 Stocks

	2002 £000	2001 £000
Consumables	467	454

17 Debtors and prepayments

	2002 £000	Restated 2001 £000
Due within one year:		
Trade and other debtors	43,737	25,971
Forward foreign exchange asset	708	1,298
Group tax relief receivable	3,189	1,557
Prepayments and accrued income	17,494	22,565
Deferred taxation (see note 10)	682	1,155
	65,810	52,546
Due after more than one year:		
Other debtors	778	2,500
Pension scheme prepayment	24,318	24,592

Notes to the financial statements continued

18 Pension scheme

The Corporation of Lloyd's operates a defined benefit pension scheme with assets held in a separately administered fund. The latest actuarial valuation of the scheme was carried out by Watson Wyatt Partners, consulting actuaries, as at 30 June 2001 using the projected unit method. The principal actuarial assumptions adopted in the valuation were that (in real terms relative to retail price inflation), present and future pensions in payment would remain constant whilst total pensionable remuneration would increase by 1.8% per annum. The real rate of return on investments held at the valuation date was assumed to be approximately 3.65%. The market value of the scheme's assets at the date of valuation was £301m, which equates to some 117% of the benefits that had accrued to members, after allowing for assumed future increases in pensionable remuneration. These figures exclude both liabilities and the related assets in respect of money purchase AVCs and in respect of the accrued benefits of scheme members employed by LPSO Limited, LCO Marine Limited and LCO Non-Marine and Aviation Limited as these companies ceased to be subsidiaries during 2001 (see note 25). The surplus in the scheme is being eliminated by a pension contribution holiday.

The pension scheme prepayment movement of £0.3m in 2002 (2001:£nil) results from actuarial assumptions.

Since the date of the last formal valuation of the scheme the FTSE All Share Index has fallen by approximately 30% up to 31 December 2002 and the assets of the scheme have not been immune to this general trend. The liabilities of the scheme are valued using a discount rate which reflects market levels at the date of the valuation. The fall in the scheme's assets does not, itself, change the estimate of the cost of providing the pension benefits promised which is based on the last formal valuation. The cost will be reassessed following the next formal valuation, anticipated to take place as at 30 June 2004.

The disclosures required in relation to the transitional arrangements within FRS17 'Retirement benefits' have been based on the most recent formal actuarial valuation as at 30 June 2001 updated to 31 December 2002. The major financial assumptions used by the actuary as at 31 December 2002 for the purposes of FRS17 were as follows:

	2002 % per annum	2001 % per annum
General salary and wage inflation	4.10	4.30
Rate of increase in pensions in payment (in excess of GMP's)	2.30	2.50
Increases to deferred pensions	2.30	2.50
Discount rate	5.75	5.75
Price inflation	2.30	2.50

FRS17, if implemented in full, will require immediate recognition in the balance sheet of the net surplus or deficit calculated at the balance sheet date. The standard requires the assets to be measured at their market value at that date and the liabilities to be discounted at the rate of return available at the balance sheet date on high quality corporate bonds.

Were FRS17 to be implemented, the deficit in the pension scheme and the related deferred tax asset shown below would be included in the financial statements in place of the pension prepayment currently included in the balance sheet under SSAP24.

18 Pension scheme continued	2002	2002	2001	2001
	Expected rate of return % per annum	Fair value £m	Expected rate of return % per annum	Fair value £m
Asset analysis of the scheme and expected returns as at 31 December 2002				
Bonds	5.0	59	5.2	46
Equities	8.3	160	8.0	215
Cash and net current assets	3.8	1	4.0	15
Total market value of assets		220		276
Actuarial value of liability		(287)		(284)
Deficit in the scheme		(67)		(8)
Related deferred tax asset		20		2
Net pension liability		(47)		(6)

The table below shows the total reserves of the Corporation as disclosed in the consolidated balance sheet adjusted for the requirements of FRS17 as at 31 December 2002:

	2002 £m	Restated 2001 £m
Total reserves	87	91
Exclude SSAP24 pension scheme prepayment	(24)	(25)
Net pension liability under FRS17	(47)	(6)
Total reserves including pension liability	16	60

	2002 £m
Movement in deficit during the year	
Deficit in scheme at beginning of the year	(8)
Movement in year:	
Current service cost	(5)
Past service cost	(1)
Other finance income	4
Actuarial loss recognised in statement of recognised gains and losses (STRGL)	(57)
Deficit in scheme before tax	(67)
Deferred tax	20
Deficit in scheme at end of the year after tax	(47)

	2002 £m
Analysis of the amount that FRS17 would require to be recognised in the statement of total recognised gains and losses (STRGL)	
Actual return less expected return on pension scheme assets	(60)
Experience losses arising on the scheme liabilities	(9)
Changes in the assumptions underlying the present value of the scheme liabilities	12
Actuarial loss	(57)
Deferred tax movement during the year	18
Actuarial loss net of deferred tax recognised in the STRGL	(39)

Notes to the financial statements continued

18 Pension scheme continued

The increase in the pension scheme deficit during the year results from a fall in the market value of assets. The measurement bases set by FRS17 are likely to give rise to significant fluctuations to the scheme's assets and liabilities. However, this may not necessarily require changes to the contribution rate, as recommended by the independent actuary, which is based on expected long-term rates of return.

Were FRS17 to be implemented, the following amounts would be included in the consolidated revenue account for the year:

	2002 £m
Analysis of the amounts charged to operating profit	
Current service cost	5
Past service cost	1
Total operating charge	6

	2002 £m
Analysis of the amount credited to other finance income	
Expected return on pension scheme assets	20
Interest on pension scheme liabilities	(16)
Net return	4

	2002
History of experience gains and losses (current point only)	
Difference between the expected and actual return on scheme assets:	
amount (£m)	(60)
percentage of scheme assets	(27.0%)
Experience gains and losses on scheme liabilities:	
amount (£m)	(9)
percentage of the present value of the scheme liabilities	(3.2%)
Total amount recognised in statement of total recognised gains and losses:	
amount (£m)	(57)
percentage of the present value of the scheme liabilities	(19.9%)

19 Current asset investments

	2002 £000	2001 £000
Short-term deposits and certificates of deposit	5,610	31,089

Included in the table above are money market instruments not repayable on demand without penalty.

20 Creditors - due within one year	2002 £000	Restated 2001 £000
Accruals and deferred income	32,360	38,869
Forward foreign exchange liability	496	1,265
Trade and other creditors	32,838	25,718
Arbitration awards	2,186	2,966
Taxation and social security	3,969	5,211
	71,849	74,029

It is the Corporation's policy that payments to suppliers are made in accordance with those terms and conditions agreed between the Corporation and its suppliers, provided that all trading terms and conditions have been complied with.

At 31 December 2002, the Corporation had an average of 25 days purchases outstanding in trade creditors (2001: 31 days).

21 Provisions for liabilities and charges	Long-term incentive plan £000	Travel insurance dispute £000	Other provisions £000	Total £000
Balance at 1 January 2002	–	6,436	1,000	7,436
Charged/(credited) to revenue account	3,500	100	–	3,600
Credited to unrealised gain on disposal of subsidiaries	–	–	(554)	(554)
Utilised in the year	–	(6,073)	(146)	(6,219)
Balance at 31 December 2002	3,500	463	300	4,263

Long-term incentive plan

A long-term incentive plan was introduced in 1998 for executive directors and senior employees that is related to the results of the Lloyd's market. This scheme helps to ensure that the objectives of directors and employees are aligned with those of the Lloyd's market. A full provision of £3.5m, including employers' National Insurance of £0.4m, for estimated amounts due in respect of the plan for 2002 based on market estimates of the 2002 pure year underwriting profit, has been made. Payments will be made over three years commencing in 2003. One third of the amounts payable are discretionary and based on performance.

Travel insurance dispute

In 2001 a dispute arose that cast doubt on the validity of the travel insurance policies sold by The Management Company (London) Limited (in liquidation) to members of the public. The Management Company (London) Limited is not a related party to the Corporation of Lloyd's as defined by FRS8 'Related Party Disclosures'. In order to protect the reputation of Lloyd's and the rights of policyholders, Lloyd's announced in July 2001 that it would meet all valid policyholders' claims. In 2001 a charge of £4.9m was recognised after taking account of an agreed contribution, subject to contract, of £2.6m from those parties involved in the dispute. During 2002 the majority of the provision was utilised and parties involved in the dispute entered into a settlement agreement. A further £0.1m has been charged to the consolidated revenue account in 2002 in order to meet estimated outstanding claims.

Other provisions

Other provisions comprise amounts provided for obligations arising from the sale of LPSO Limited during 2001. These provisions have been reassessed as at 31 December 2002 resulting in a release of £0.6m that has been reflected in the consolidated statement of total recognised gains and losses (see note 25).

Notes to the financial statements continued**22 Notes to the cash flow statement**

	2002 £000	2001 £000
A Reconciliation of operating deficit to operating cash flows		
Operating deficit	(29,891)	(34,175)
Depreciation charges	2,443	4,466
(Profit)/loss on sale of other fixed assets	(190)	488
Loss/(profit) on disposal of insurance deposits	1,890	(148)
(Profit)/loss on revaluation of insurance deposits	(4,310)	47
Loss/(profit) on revaluation of underwriting loans	1,779	(912)
(Increase)/decrease in stocks	(13)	295
Decrease/(increase) in debtors	405	(4,642)
Decrease in creditors	(4,673)	(3,265)
(Decrease)/increase in provisions	(2,619)	6,436
	(35,179)	(31,410)
Premium levy collection	250,926	120,859
Market settlement recoveries	5,633	17,996
Transfers to Lloyd's New Central Fund	(246,809)	(80,000)
Net cash (outflow)/inflow from operating activities	(25,429)	27,445
B Analysis of cash flows for headings netted in the cash flow statement		
Returns on investments and servicing of finance:		
Dividends received	–	7,300
Interest received	5,258	7,561
Interest paid	(3,525)	(7,257)
	1,733	7,604
Capital expenditure and financial investment:		
Purchase of tangible fixed assets	(2,321)	(4,614)
Sale of tangible fixed assets	378	49,968
	(1,943)	45,354
Acquisitions and disposals of business operations:		
Sale of businesses	–	(18,206)
Management of liquid resources:		
Purchase of cash deposits	(61,583)	(50,014)
Purchase of securities	(31,436)	(32,768)
Sale of cash deposits	82,845	62,550
Sale of securities	28,814	22,910
	18,640	2,678
Financing:		
Increase in borrowings for insurance deposits	6,142	4,725
Repayment of mortgage loan	–	(24,000)
Repayment of syndicated bank loan	–	(78,352)
	6,142	(97,627)

22 Notes to the cash flow statement continued

C Analysis of net funds	At 01.01.02 £000	Cash flow £000	Other movements £000	At 31.12.02 £000
Cash in hand, at bank	31,226	371	-	31,597
Overnight deposit (see below, b)	2,953	148	-	3,101
	34,179	519	-	34,698
Current asset investments (see below, a)	31,089	(25,479)	-	5,610
Other deposits (see below, b)	54,804	6,691	2,420	63,915
Debt due within one year:				
Funding of statutory insurance deposits	(53,665)	(6,142)	(1,779)	(61,586)
	66,407	(24,411)	641	42,637

- a) Current asset investments comprise short-term deposits and certificates of deposit that are not repayable on demand without penalty.
- b) Overnight deposits and other deposits relating to the funding of subsidiary companies are included in the consolidated balance sheet under statutory insurance deposits.

23 Interest rate exposure of financial assets and liabilities as at 31 December 2002	Financial assets			Financial liabilities			Net financial assets/ (liabilities) £000
	Fixed rate £000	Floating rate £000	Total £000	Fixed rate £000	Floating rate £000	Total £000	
Sterling	993	15,342	16,335	-	(1,562)	(1,562)	14,773
United States dollar	-	3,350	3,350	-	-	-	3,350
Canadian dollar	351	3,321	3,672	-	-	-	3,672
Japanese yen	-	10,304	10,304	-	(1,047)	(1,047)	9,257
Australian dollar	749	36	785	-	(741)	(741)	44
Switzerland franc	34,996	3,364	38,360	-	(37,731)	(37,731)	629
Singapore dollar	-	14,086	14,086	-	(14,240)	(14,240)	(154)
South African rand	-	2,621	2,621	-	-	-	2,621
Cyprus pound	243	2,928	3,171	-	(3,960)	(3,960)	(789)
Others	3,201	9,116	12,317	-	(2,305)	(2,305)	10,012
	40,533	64,468	105,001	-	(61,586)	(61,586)	43,415
Of which:							
Unhedged statutory insurance deposits	40,533	26,483	67,016	-	(61,586)	(61,586)	5,430
Other debtors due after more than one year	-	778	778	-	-	-	778
Investments	-	5,610	5,610	-	-	-	5,610
Cash and deposits	-	31,597	31,597	-	-	-	31,597
	40,533	64,468	105,001	-	(61,586)	(61,586)	43,415

Short-term debtors and creditors, including outstanding foreign exchange transactions, have been excluded from the above table. At 31 December 2002 the asset value, relating to outstanding foreign exchange transactions, included within debtors amounted to £708,000 (2001: £1,298,000) and the liability value of such transactions, within creditors amounted to £496,000 (2001: £1,265,000) giving a net unrealised foreign exchange gain of £212,000 (2001: £33,000).

There are no hedged statutory insurance deposits at 31 December 2002.

Notes to the financial statements continued

24 Reserves	Revaluation reserve £000	Accumulated reserve £000	Total reserves £000
Balance at 1 January 2002 as previously stated	–	82,646	82,646
Restatement of the valuation of other investments	6,913	–	6,913
Restatement of deferred tax assets	–	1,155	1,155
Balance at 1 January 2002 as restated	6,913	83,801	90,714
Total recognised losses for the year	–	(3,563)	(3,563)
Balance at 31 December 2002	6,913	80,238	87,151

	2002 £000	Restated 2001 £000
Accumulated reserves attributable to:		
Corporation of Lloyd's	94,724	80,427
Consolidated subsidiaries	(16,189)	3,711
Associates	1,703	(337)
	80,238	83,801

25 Sale of business operations

In 2001 Lloyd's transferred its wholly owned subsidiary LPSO Limited to Ins-sure Holdings Limited. LCO Marine Limited and LCO Non-Marine and Aviation Limited were also transferred to Xchanging Claims Services Limited. An unrealised profit on disposal of £4.8m arising from these transactions was reflected in the consolidated statement of total recognised gains and losses after deducting a provision for obligations arising from the sale of LPSO Limited of £1.0m. During 2002 the provision was reassessed resulting in a release of £0.6m (see note 21).

26 Commitments**a) Capital expenditure commitments**

No contractual commitments existed at 31 December 2002 other than those included within the financial statements. The same applied at 31 December 2001.

b) Operating lease commitments

The annual commitments under non-cancellable operating leases are as follows:

	2002 Land and buildings £000	2001 Land and buildings £000
Leases expiring:		
Over five years	16,767	16,767

Commitments outstanding under the terms of the lease for the Lloyd's 1986 building have been included at current rental value to the first break of the lease after 25 years. The lease was subject to a rent review in March 2001.

27 Disclosure of related party transactions

In accordance with the exemption allowed by FRS8 'Related Party Disclosures', transactions with entities within the group have not been disclosed.

Services provided to Ins-sure Holdings Limited group in the year ended 31 December 2002 included operating systems support and development, premises and other administrative services. The total value of the services provided was £7,443,000. In addition, Ins-sure Holdings Limited group have charged the Corporation £1,005,000 for services provided in the same period.

27 Disclosure of related party transactions continued

At 31 December 2002 there were no amounts due from Ins-sure Holdings Limited group to the Corporation. The Corporation owed £166,000 to Ins-sure Holdings Limited at the same date.

Services provided to Xchanging Claims Services Limited group in the year ended 31 December 2002 included premises and other administrative services. The total value of the services provided was £2,524,000. In addition, Xchanging Claims Services Limited group have charged the Corporation £267,000 for services provided in the same period.

At 31 December 2002 there was a balance of £262,000 owing from Xchanging Claims Services Limited group to the Corporation.

Services provided to Centrewrite Limited in the year ended 31 December 2002 included premises and other administrative services. The total value of the services provided was £559,000. Centrewrite Limited did not charge the Corporation for any services in the same period.

At 31 December 2002 there was a balance of £46,000 owing from Centrewrite Limited to the Corporation.

Services provided to Lioncover Insurance Company Limited in the year ended 31 December 2002 included accounting and audit services. The total value of the services provided was £13,000. Lioncover Insurance Company Limited did not charge the Corporation for any services in the same period.

At 31 December 2002 there were no amounts due from Lioncover Insurance Company Limited to the Corporation. The Corporation owed £28,000 to Lioncover Insurance Company Limited at the same date.

In the normal course of business the Corporation's own insurance arrangements may be underwritten by Lloyd's syndicates. Any such arrangements are based on independent professional advice.

There were no other related party transactions in 2002.

28 Contingent liabilities

A General average guarantees have been given on behalf of, and secured by, Lloyd's underwriters. It is estimated that the aggregate of the liabilities attaching to these guarantees at 31 December 2002 amounted to £7.6m (2001: £8.5m).

B The Corporation of Lloyd's has given indemnities to Lioncover Insurance Company Limited, Centrewrite Limited and to certain Names under hardship and other agreements in respect of their underwriting losses. The Council has determined that any losses resulting from such indemnities will be met by the Central Fund. The financial statements of the Central Fund on pages 88 to 100 give further details of the indemnities and the exposures arising.

C Bank guarantees and other arrangements have been entered into by the Corporation of Lloyd's and its subsidiary, Additional Securities Limited, to provide security in connection with the underwriting activities of the members of Lloyd's in the countries shown:

			2002 £000	2001 £000
Guarantees provided by the Corporation of Lloyd's:				
USA:	US \$1,500,000	(2001: US\$ 1,500,000)	932	1,027
Guarantees provided by the Corporation of Lloyd's and Additional Securities Limited:				
Cayman Islands:				
liability	US\$ 1,000,000	(2001: US\$ 1,000,000)	621	687
Hong Kong:				
liability	HK\$ 291,500,000	(2001: HK\$ 116,800,000)	23,219	10,341
Malta:				
liability	GBP 1,506,465	(2001: GBP nil)	1,506	–

The Corporation of Lloyd's has established an uncollateralised US\$15m letter of credit arrangement on behalf of an insolvent corporate member. The purpose of the letter of credit facility is to ensure that the insolvent corporate member meets its US Trust Fund funding obligations. The letter of credit is in favour of Citibank N.A., the trustee of the US Surplus Lines Trust Fund, and expires on 21 October 2003.

Notes to the financial statements continued

28 Contingent liabilities continued

D The Corporation of Lloyd's has given indemnities to certain of its subsidiary companies, and the directors thereof, in respect of any claims or actions which may be brought against them or any future operating losses incurred by them in connection with the companies' activities. The Corporation of Lloyd's has also given indemnities to and has agreed to cover certain specific costs that may be incurred by members of the Council, Lloyd's Regulatory Board, Lloyd's Market Board and of their respective sub-committees, Corporation staff and also certain individuals and organisations who have been asked to carry out or provide services to the Corporation or on behalf of or for the benefit of its members. Provision for any costs that may arise from these indemnities and agreements is made annually.

E On 28 February 2000 the trial of an action commenced against the Corporation of Lloyd's in the United Kingdom, the Jaffray action, in which certain Names claimed that Lloyd's, between the years 1978 and 1988, made fraudulent misrepresentations which induced those Names to become members of Lloyd's and continue underwriting. Judgement was given in favour of Lloyd's on 3 November 2000. The Names appeal against this judgement, which commenced on 4 March 2002, was dismissed on 26 July 2002. The House of Lords has refused permission to appeal. Certain Names are seeking permission to amend their pleadings in this action (and others to start fresh actions) alleging statutory and negligent misrepresentation. Lloyd's does not accept any liability in respect of this action.

F In Australia one Name has commenced proceedings alleging similar claims of fraud as in the Jaffray action and breach of Australian statutes. Lloyd's does not accept any liability in respect of this action.

G Five actions have been filed in the United States in respect of the insurance of slaves. Lloyd's does not accept any liability in respect of these proceedings.

In respect of all contingent liabilities noted above in paragraphs (A) – (G), no provision is made in these financial statements.

Five year summary

	1998 £000	1999 £000	2000 £000	Restated 2001 £000	2002 £000
Consolidated revenue account					
Operating income	178,112	164,406	146,240	143,169	129,263
Operating expenses:					
Employment	(74,544)	(70,316)	(53,195)	(44,793)	(47,242)
Premises	(29,166)	(24,551)	(27,874)	(37,853)	(30,244)
Overseas operating expenses	(18,029)	(17,401)	(18,136)	(22,112)	(21,497)
Other expenses	(61,057)	(60,975)	(71,961)	(72,586)	(60,171)
Operating expenses	(182,796)	(173,243)	(171,166)	(177,344)	(159,154)
Operating deficit	(4,684)	(8,837)	(24,926)	(34,175)	(29,891)
Share of operating profits of associates before exceptional items	–	–	–	216	2,873
Share of exceptional items of associates	–	–	–	(495)	–
Amortisation of goodwill of associate	–	–	–	(78)	(118)
Total operating deficit	(4,684)	(8,837)	(24,926)	(34,532)	(27,136)
Profit on disposal of businesses	–	–	319	–	–
Profit on sale of the Lloyd's 1958 building	–	–	–	25,069	1,926
Net interest income/(expenditure)	(16,225)	(13,092)	(7,064)	2,505	1,874
Dividends receivable	–	–	–	7,300	2,750
Market settlement net	53,994	97,607	132,089	137,993	261,780
Transfers to Lloyd's New Central Fund	–	–	–	(80,000)	(246,809)
Taxation credit/(charge)	(8,816)	1,191	18,198	(491)	1,498
(Deficit)/surplus for the year	24,269	76,869	118,616	57,844	(4,117)
	Number	Number	Number	Number	Number
Average numbers of employees during the year	1,833	1,645	1,176	825	589

Lloyd's Central Fund

Purpose of the Fund

The Lloyd's Central Fund continues to be held and administered by the Council of Lloyd's primarily as a fund available for the protection of policyholders, in accordance with the Byelaw of 14 July 1986 (the 'Old' Central Fund) and the Byelaw of 5 June 1996 (the New Central Fund). These financial statements reflect the separate activities of the New Central Fund and of the 'Old' Central Fund.

The 'Old' Central Fund will continue to receive recoveries of amounts contributed as part of the 1996 market settlement and meet any remaining liabilities arising from before the settlement date. The balance of the Fund will eventually be transferred into the New Central Fund.

The New Central Fund was established with a transfer of £110m from the 'Old' Central Fund following authorisation by the Council on 4 June 1997. Members contribute to the Fund each year based on a percentage of their allocated overall premium limit. The rate for 2002 was 1% for all members (2001: 0.75%).

As part of Lloyd's solvency procedures, certain assets of the Fund may be used to cover underwriting deficiencies of members at the preceding 31 December to enable them to pass the solvency test and meet the requirements of the Financial Services Authority. Assets may be made available to discharge the underwriting liabilities of members in the event of default.

Financial commentary

At 31 December 2002, the combined assets of the Lloyd's Central Fund amounted to £476.2m, an increase of £196.1m since reported last year.

The New Central Fund is supported by a five year insurance contract, which commenced in 1999, with six insurers whereby the insurers will meet unrecovered losses to the New Central Fund where it has been applied to meet members' cash calls, up to a ceiling of £350m per annum to the extent that such calls exceed £100m in any one year. The aggregate maximum payment over the lifetime of the policy is £500m. During 2002 the New Central Fund has met the unpaid cash calls of insolvent corporate members totalling £465.5m. This has resulted in a claim of £350m under the insurance contract of which £133.8m had been received by the year end. Further claims are expected to be made in 2003. However, the insurers have indicated that they dispute their liability to meet the claims made under the policy. Lloyd's does not accept that the insurers have grounds for disputing liability and has commenced arbitration proceedings under the terms of the policy for recovery of the sums claimed from the insurers. This is described in *note 7* to the financial statements.

Lloyd's New Central Fund paid insurance premiums of £16.4m in 2002 (2001 : £16.5m).

During 2002 the Lloyd's New Central Fund received contributions amounting to £134.5m and refunded £46.6m in respect of members' special contributions in accordance with *Reconstruction & Renewal*. The corporation of Lloyd's collected and transferred £246.8m to the New Central Fund during 2002 representing the premium levy received during the year. The premium levy is charged on substantially all premiums received at 2% for most classes of business (1% for UK motor and life business).

New Central Fund contributions for 2003 are to remain at 1% of overall allocated premium limits for all members. Contributions due and received on 1 April 2003 totalled £144m.

Lloyd's Central Fund – Independent auditor's report to the Council of Lloyd's

We have audited the financial statements for the year ended 31 December 2002 which comprise the balance sheet, general fund account, statement of total recognised gains and losses, cash flow statement and the related notes 1 to 17. These financial statements have been prepared on the basis of the accounting policies set out therein.

This report is made solely to the Council of Lloyd's in accordance with its instructions to us as set out under the 'Respective responsibilities of the Council of Lloyd's and auditors' below. Our audit work has been undertaken so that we might state to the Council those matters we are required to state in this report in accordance with the Council's instructions and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Council for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the Council of Lloyd's and auditors

The Council is responsible for the administration of the Fund and approval of the financial statements prepared by Lloyd's. You have instructed us to audit the financial statements in accordance with United Kingdom Auditing Standards and report to you our opinion as to whether the financial statements give a true and fair view. We also report to you if, in our opinion, Lloyd's has not kept proper accounting records, or if we have not received all the information and explanations we require for our audit.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by or on behalf of the Council in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Fund's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Fundamental uncertainty

In forming our opinion we considered the adequacy of the disclosures made in note 7 concerning the possible outcome of the arbitration between Lloyd's and the insurers of the New Central Fund insurance contract. The financial statements have been drawn up on the basis that the arbitration will be concluded in favour of Lloyd's. Should the arbitration be concluded in favour of one or more of the insurers, the recoveries that the New Central Fund will be able to make from the policy will be reduced. Details of the circumstances relating to this fundamental uncertainty are described in note 7. Our opinion is not qualified in this respect.

Opinion

In our opinion the financial statements give a true and fair view of the financial transactions of the Fund for the year ended 31 December 2002 and of the disposition at that date of its assets and liabilities.

Ernst & Young LLP

Registered Auditor

London

2 April 2003

Lloyd's Central Fund balance sheet

as at 31 December 2002

	Note	2002 £000	Restated 2001 £000
New Central Fund		444,751	302,898
'Old' Central Fund		31,486	23,931
Total Fund balance	12	476,237	326,829
Represented by:			
Investments			
Listed:			
United Kingdom		120,124	140,177
Overseas		120,593	133,437
Short-term deposits		100,181	87,291
	6	340,898	360,905
Current assets			
Debtors	7	245,297	173,796
Cash		28	566
		245,325	174,362
Total assets		586,223	535,267
Current liabilities			
Creditors	10	(24,876)	(3,995)
Total assets less current liabilities		561,347	531,272
Provisions for liabilities and charges			
Undertakings given to insolvent members	11	(85,110)	(204,443)
Net assets		476,237	326,829

The balance sheet as at 31 December 2001 has been restated for the adoption of FRS19 (see note 9).

Signed on behalf of the Council of Lloyd's on 2 April 2003

Lord Levene of Portsoken

Chairman

NET Prettejohn

Chief Executive Officer

Lloyd's Central Fund general fund account

for the year ended 31 December 2002

	Note	New Central Fund 2002 £000	'Old' Central Fund 2002 £000	Total 2002 £000	Restated Total 2001 £000
Income					
Contribution from members of Lloyd's	5	134,467	–	134,467	84,750
Contribution from 'Old' Central Fund		–	–	–	20,000
Contribution from Corporation	5	246,809	–	246,809	80,000
Profit from sale of investments		–	205	205	11,127
Dividends and interest		12,271	2,138	14,409	17,255
Recoveries		–	8,830	8,830	7,288
		393,547	11,173	404,720	220,420
Expenditure					
Contribution to New Central Fund		–	–	–	(20,000)
Refunds of members' special contributions		(46,591)	–	(46,591)	(48,628)
Income Support Schemes		–	(1,713)	(1,713)	(1,969)
Loss from sale of investments		(6,174)	–	(6,174)	–
Other claims and provisions	8	(87,726)	–	(87,726)	(157,701)
Run-off project costs		(1,343)	–	(1,343)	–
Insurance premiums and brokerage fees		(16,706)	–	(16,706)	(16,657)
Administrative expenses		(410)	(443)	(853)	(732)
Loss on exchange		(2,955)	–	(2,955)	(592)
		(161,905)	(2,156)	(164,061)	(246,279)
Surplus/(deficit) before taxation		231,642	9,017	240,659	(25,859)
Taxation (charge)/credit	9	(70,612)	–	(70,612)	31,401
Net surplus for the year		161,030	9,017	170,047	5,542
(Decrease)/increase in valuation of investments during the year					
Unrealised exchange (loss)/gain	6	(11,916)	–	(11,916)	702
Unrealised decrease in market valuation of investments	6	(18,607)	(1,462)	(20,069)	(28,759)
Deferred taxation credit	9	11,346	–	11,346	6,535
		(19,177)	(1,462)	(20,639)	(21,522)
Increase/(decrease) in general fund for the year		141,853	7,555	149,408	(15,980)

Lloyd's Central Fund statement of total recognised gains and losses

for the year ended 31 December 2002

	New Central Fund 2002 £000	'Old' Central Fund 2002 £000	Total 2002 £000	Restated Total 2001 £000
Increase/(decrease) in general fund for the year	141,853	7,555	149,408	(15,980)
Prior year adjustment (as explained in note 1)	46,653	–	46,653	
Total recognised gains since last annual report	188,506	7,555	196,061	

The Lloyd's Central Fund general fund account and the statement of total recognised gains and losses for the year ended 31 December 2001 have been restated for the adoption of FRS19 (see note 9).

Lloyd's Central Fund cash flow statement

for the year ended 31 December 2002

	Note	2002 £000	2001 £000
Cash inflow from operating activities before claims paid and insurance recoveries			
	13	360,480	93,375
Claims paid in respect of corporate members	11	(465,533)	(39,857)
Claims paid in respect of individual members	8	(2,231)	(1,215)
Insurance recoveries	11	133,777	–
Cash inflow from operating activities		26,493	52,303
Taxation (paid)/received		(6,129)	15,769
Cash inflow before use of liquid resources and financing		20,364	68,072
Management of liquid resources	14	(20,567)	(66,310)
(Decrease)/increase in cash in the year		(203)	1,762
Reconciliation of net cashflow to movement in net funds			
(Decrease)/increase in cash in the year		(203)	1,762
Cash outflow from movement in liquid resources	14	20,567	66,310
Change in net funds resulting from cash flows		20,364	68,072
(Loss)/profit from sale of investments	6	(5,969)	11,127
Loss on exchange		(2,955)	(592)
Movement in valuation of investments	6	(31,985)	(28,057)
Movement in net funds in the year		(20,545)	50,550
Net funds at 1 January		361,471	310,921
Net funds at 31 December	15	340,926	361,471

Lloyd's Central Fund notes to the financial statements

as at 31 December 2002

1 Purpose of financial statements

Basis of preparation

The Central Fund, which is held at the discretion of the Council of Lloyd's, has not been consolidated within the financial statements of the Corporation as it is primarily a Fund available for the protection of policyholders and hence relates to the insurance related activities of the members of Lloyd's.

The financial statements are prepared under the historical cost convention modified for the revaluation of investments.

These financial statements summarise the income, expenditure, assets and liabilities of the Fund at 31 December 2002. The liabilities of the Fund include those amounts contractually committed by the Fund and exclude provision for future discretionary payments. The financial statements therefore do not take account of claims approved after the balance sheet date or future payments that may be made to cover underwriting losses of individual Names except to the extent that the Central Fund is contractually committed to make such payments under hardship and other agreements. No value has been assumed for the assets pledged by hardship Names under the terms of their hardship agreements.

For the year ended 31 December 2002 the Central Fund has adopted FRS19 'Deferred Tax'. The adoption of FRS 19 'Deferred Tax' has resulted in a change of accounting policy for deferred taxation. Deferred tax is recognised on a full provision basis in accordance with the accounting policy described below. Previously, deferred tax was provided for on a partial provision basis, whereby provision was made on all timing differences to the extent that they were expected to reverse without replacement.

The change in accounting policy has resulted in a prior year adjustment. The total fund balances as at 1 January 2001 increased by £15,800,000 and the tax credit for the year ended 31 December 2001 increased by £30,853,000. As a result the previously reported total Fund balances as at 31 December 2001 of £280,176,000 are increased to £326,829,000 by the inclusion of a deferred tax asset of £46,653,000. A net increase in the deferred tax charge of £32,938,000 arises in 2002 as a result of the change in accounting policy.

Lloyd's is regulated by the Financial Services Authority (FSA).

2 Principal accounting policies

A Investments

Investments are shown at market value at the balance sheet date and the profits and losses arising on revaluation are included in the general fund account.

B Dividends and interest

Dividends from equity investments are taken into account on the ex-dividend date of payment. Interest income is created by reference to the amounts earned during the year.

C Claims and recoveries

Claims are charged to the general fund account when approved or contractually committed, net of insurance recoveries.

Insurance recoveries arise from the operation of the New Central Fund insurance contract, which is described on page 88. The contract provides that where the New Central Fund has been applied to meet members' cash calls in respect of any one year, the New Central Fund is entitled to a matching recovery of the claim paid (a 'qualifying debt'), subject to the policy terms. Consequently, insurance recoveries are accounted for when a qualifying debt has been paid or is expected to be paid when undertakings (see note 3) have been given, in accordance with the principles of the Statement of Recommended Practice on Accounting for Insurance Business.

Recoveries, other than insurance recoveries, in respect of claims approved are credited to the general fund account when received.

D Loans and provisions

Loans made to syndicates are only recognised as debtors to the extent that they are expected to be recoverable from solvent members.

E Foreign currency

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the balance sheet date. All differences are taken to the general fund account.

Lloyd's Central Fund notes to the financial statements continued

2 Principal accounting policies continued

F Taxation

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events have occurred at that date will result in an obligation to pay more, or a right to pay less or to receive more, tax. Deferred tax assets are recognised only to the extent that it is considered that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted. Deferred tax is measured on an undiscounted basis at the rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantially enacted at the balance sheet date.

3 Solvency shortfalls

As part of Lloyd's solvency procedures, wherever there is a shortfall in comparing a member's Lloyd's assets with liabilities at the preceding year end, sufficient central and other assets are identified to enable the member to pass the solvency test and meet the requirements of the Financial Services Authority. The results of the 2002 solvency test will not be determined until June 2003.

The Council of Lloyd's has given undertakings with financial limits to certain corporate members to use the New Central Fund to discharge the liability of those members where they have unpaid cash calls and do not have the resources to meet those cash calls. The purpose of these undertakings is primarily to allow valid claims made on policies underwritten by insolvent members to continue to be paid in full as and when the claims fall due. Provision has been made for these undertakings on the basis that they represent contractual commitments (*see note 11*). Unutilised undertakings as at 31 December 2002 were £85.1m. By 31 March 2003 this balance had been reduced to £48.9m by the payment of claims. Included within this balance were undertakings of £36.7m which expired on 1 April 2003. Those undertakings which expired have been replaced and further undertakings have been given on 2 April 2003 that total £205.5m, a net increase of £168.8m. No provision has been included in these financial statements in respect of these further undertakings. When they are charged to the general fund account in 2003 it is assumed that further insurance claims of £150m will be made. However, as described in *note 7*, insurers have indicated that they dispute their liability to meet claims under the contract.

On 11 April 2002 the Corporation of Lloyd's entered into an agreement with Cox Insurance Holdings plc ('CIH') and certain of its subsidiaries. Under the agreement, the underwriting liabilities of Cox Dedicated Corporate Member Limited ('CDCM') will be met from Funds at Lloyd's, profits arising in respect of the 2002 and prior years of account accruing to that member together with profits of the new corporate member, Equity Red Star Limited, arising in respect of the 2002 and prior years of account, a financing charge payable by Equity Red Star Limited and any amounts realised through the use of CDCM's tax losses within the Cox Group. Save as stated above, other assets of CIH shall not be available to meet the underwriting liabilities of CDCM. Based on information available to Lloyd's the underwriting liabilities of CDCM are not expected to exceed the available assets, as above. Therefore, no undertakings have been given in respect of CDCM and no provision has been included in these financial statements.

4 Contingent liabilities

The Society of Lloyd's has taken on the responsibilities of some individual Names under hardship and other agreements. The Society has also given indemnity bonds to Lioncover Insurance Company Limited (Lioncover) and Centrewrite Limited (Centrewrite) respectively against any shortfall in their assets. The Council has determined that any losses resulting from such indemnities will be met by the Central Fund.

In order to quantify the potential liability of the 'Old' Central Fund in respect of hardship Names, quotations have been obtained from Centrewrite for Exeat policies to cover all of those Names with hardship agreements and who continue to have open underwriting years of account (*see note 10*).

Following the implementation of *Reconstruction & Renewal*, Names underwriting in respect of 1992 and prior years, Lioncover and Centrewrite have been reinsured into Equitas. If Equitas were unable to discharge in full the liabilities which it has reinsured any resulting shortfall in respect of Lioncover or Centrewrite could be met out of both the 'Old' Central Fund and the New Central Fund under the terms of their respective Lloyd's bond. Both the 'Old' Central Fund and the New Central Fund would also be available to meet the claims of policyholders of Names who are party to hardship agreements executed before 4 September 1996, to the extent that such an event resulted in a shortfall. However, unless the members of the Society resolve in a general meeting to make the New Central Fund available, only the 'Old' Central Fund would be available to meet the claims of policyholders of Names who are not party to hardship agreements executed before 4 September 1996.

4 Contingent liabilities continued

The Corporation of Lloyd's has established an uncollateralised US\$15m letter of credit arrangement on behalf of an insolvent corporate member. The purpose of the letter of credit facility is to ensure that the insolvent corporate member meets its US Trust Fund funding obligations. The letter of credit is in favour of Citibank N.A., the trustee of the US Surplus Lines Trust Fund, and expires on 21 October 2003. No provision has been included in these financial statements in respect of this contingent liability.

5 Contributions to New Central Fund

The New Central Fund received contributions from members amounting to £134.5m in 2002 (2001: £84.8m). The Corporation of Lloyd's collected and transferred £246.8m to the New Central Fund during 2002 representing the premium levy received during the year. The premium levy is charged on substantially all premiums received at 2% for most classes of business (1% for UK motor and life business).

	2002 £000	2001 £000
Contributions from members:		
Individual members	17,929	13,521
Corporate members	116,538	71,229
	134,467	84,750

6 Investments

	2002 £000	2001 £000
Movement in the year:		
Market value at 1 January	360,905	310,863
Additions at cost	153,316	228,856
Increase in short-term deposits	12,890	62,523
Proceeds from disposals	(148,259)	(224,407)
(Loss)/gain on disposals	(5,969)	11,127
(Decrease)/increase in valuation of investments during the year:		
Unrealised exchange (loss)/gain	(11,916)	702
Unrealised decrease in market valuation	(20,069)	(28,759)
Market value at 31 December	340,898	360,905
Analysis of securities at year end:		
Listed on London Stock Exchange:		
Fixed interest	57,558	69,822
Equities	62,566	70,355
	120,124	140,177
Listed on overseas stock exchanges:		
Fixed interest	70,100	73,330
Equities	50,493	60,107
	120,593	133,437
Short-term deposits	100,181	87,291
	340,898	360,905

Basis of valuation: all securities are valued at their quoted market price at the balance sheet date.

Lloyd's Central Fund notes to the financial statements continued

7 Debtors	2002 £000	Restated 2001 £000
Interest and dividends receivable	2,835	4,123
Prepaid insurance premiums	8,428	8,853
Loans due from syndicates net of provisions	–	8,459
Insurance policy claim receivable (see note 11)	216,223	104,443
Deferred taxation (see note 9)	13,715	46,653
Other debtors and prepayments	4,096	1,265
	245,297	173,796

The New Central Fund is supported by a five year insurance contract, which commenced in 1999, with six insurers whereby the insurers are to meet losses to the New Central Fund where it has been applied to meet members' cash calls, up to a maximum of £350m per annum, to the extent that such losses exceed £100m in respect of cash calls made in any one year. The aggregate maximum payment over the lifetime of the policy is £500m.

Lloyd's has claimed £350m under the policy in respect of cash calls made in 2002. The insurers paid £134m during 2002, subject to a reservation of their rights in respect of these claims. The balance outstanding of £216m is included as a debtor as at 31 December 2002. Insurers have indicated that they dispute their liability to meet the claims made under the policy. Lloyd's does not accept that the insurers have grounds for disputing liability and has commenced arbitration proceedings under the terms of the policy for recovery of the sums claimed from the insurers. If the arbitration is not determined entirely in Lloyd's favour and, in the worst case of a range of possible outcomes, the insurance policy were avoided, the estimated effect on the financial statements as at 31 December 2002 would be to decrease the net assets of the Central Fund from £476m to £279m and to reduce the surplus for the year from £149m to a deficit of £48m. This reduction of £197m would reflect the write-off of the insurance claim receivable included in debtors, the recognition of a liability to return insurance claims paid by the insurers, the return of insurance premiums paid and consequent tax adjustments.

These financial statements include at full value both the receipt of £134m and the sum of £216m in respect of losses for cash calls made in 2002. Further claims will be made under the policy in 2003.

8 Other claims and provisions	2002 £000	2001 £000
Provision for amounts paid and payable under undertakings given to insolvent members (see note 11)	100,533	139,857
Claims paid in respect of individual members	2,231	1,215
(Release)/charge of provision against loans to syndicates	(15,038)	16,611
Other claims	–	18
	87,726	157,701

9 Taxation	New Central Fund 2002 £000	'Old' Central Fund 2002 £000	Total 2002 £000	Restated Total 2001 £000
(a) Analysis of charge in year				
<i>Current tax:</i>				
UK corporation tax based on surplus for the year at 30% (2001: 30%)	(26,301)	-	(26,301)	-
<i>Adjustments in respect of previous periods:</i>				
Tax credits arising from release of prior year provisions	-	-	-	813
Write-off of prior year tax debtors	-	-	-	6,403
Overseas tax charge	(27)	-	(27)	(133)
Total current tax (note 9(c))	(26,328)	-	(26,328)	7,083
<i>Deferred tax:</i>				
Origination and reversal of timing differences	(44,284)	-	(44,284)	24,318
Taxation (charge)/credit	(70,612)	-	(70,612)	31,401
(b) Analysis of charge in year – based on unrealised increase or decrease in valuation of investments for the year				
<i>Deferred tax arising on decrease in valuation of investments during the year</i>				
Origination and reversal of timing differences	11,346	-	11,346	6,535
Deferred taxation credit	11,346	-	11,346	6,535
(c) Factors affecting tax charge for year				
The tax assessed for the year is lower than the standard rate of corporation tax in the UK of 30%				
The differences are explained below:				
Surplus/(deficit) before taxation	231,642	9,017	240,659	(25,859)
Surplus/(deficit) before taxation multiplied by standard rate of corporation tax in the UK of 30% (2001:30%)	(69,493)	(2,705)	(72,198)	7,758
<i>Effects of:</i>				
Expenses not deductible for tax purposes	(1,681)	(549)	(2,230)	(675)
Non-taxable income	562	46	608	-
Additional deductions	-	3,208	3,208	-
Utilisation on tax losses	44,284	-	44,284	-
Current tax (charge)/credit for year (note 9(a))	(26,328)	-	(26,328)	7,083
(d) Provision for deferred tax				
A deferred tax asset has been recognised in respect of the following timing differences:				
Tax losses carried forward	-	-	-	44,284
Revaluation of investments	13,715	-	13,715	2,369
Deferred tax asset at 31 December	13,715	-	13,715	46,653
Deferred tax asset at 1 January	46,653	-	46,653	15,800
Deferred tax (charge)/credit based on the result for the year (note 9(a))	(44,284)	-	(44,284)	24,318
Deferred tax credit on revaluation of investments (note 9(b))	11,346	-	11,346	6,535
Deferred tax asset at 31 December	13,715	-	13,715	46,653

Lloyd's Central Fund notes to the financial statements continued

10 Creditors	2002	2001
	£000	£000
Hardship Names (<i>note 4</i>)	1,214	1,964
Corporation tax	19,343	–
Group relief tax payable	856	–
Other creditors and accruals	1,631	148
Income Support Schemes	1,832	1,883
	24,876	3,995

Under the terms of the Income Support Scheme and the Hardship Income Top-Up Scheme, the Central Fund has a commitment in respect of Support Scheme payments approved by Council for 2003.

11 Provision for undertakings given to insolvent members

The Council of Lloyd's has given undertakings with financial limits to certain corporate members to use the New Central Fund to discharge the liability of those members where they have unpaid cash calls and do not have the resources to meet those cash calls. The purpose of these undertakings is primarily to allow valid claims made on policies underwritten by those insolvent members to continue to be paid in full. For those corporate members in provisional liquidation, the Council has also provided a supporting commitment, which will ensure that in no circumstance will an insurance creditor receive less than the amount it would have received in a winding up commencing on the date of the provisional liquidation. Although the supporting undertaking is a legally enforceable commitment, it is acknowledged that it is not practicable to estimate a value to that commitment. Furthermore, whilst the Society is solvent the likelihood of the supporting undertaking being called upon is extremely remote.

The aggregate amount of all undertakings (excluding the supporting commitment) given by the Council at 31 December 2002 was £590.5m of which £505.4m had been paid by that date. Of the £465.5m paid during 2002, £350m is recoverable under claims made on the New Central Fund insurance policy.

Undertakings	2002		2001	
	£000	£000	£000	£000
Provisions at 1 January		204,443		–
Undertakings given in the year		346,200		244,300
Analysis of paid undertakings by member :-				
Cotesworth Capital Limited (in provisional liquidation)	(139,689)		–	
Crowe Corporate Capital Limited	(9,764)		(12,157)	
Crowe Dedicated Limited	(33,044)		–	
Duncanson & Holt Underwriters Limited	(54,654)		(23,256)	
Margent Capital Management Limited (in provisional liquidation)	(10,227)		(4,444)	
Newmarket Corporate Member Limited (in provisional liquidation)	(73,643)		–	
North American London Underwriters Limited	(6,713)		–	
Riverside Corporate Underwriters Limited (in provisional liquidation)	(13,410)		–	
Shrewsbury Underwriting Capital (Bermuda) Limited and Shrewsbury Underwriting Capital Limited	(122,297)		–	
Other corporate members	(2,092)		–	
Paid during the year		(465,533)		(39,857)
Provision for amounts payable at 31 December		85,110		204,443

11 Provision for undertakings given to insolvent members continued	2002		2001	
	£000	£000	£000	£000
Insurance policy claim receivable				
At 1 January		104,443		–
Undertakings given in the year	346,200		244,300	
Less: drawdowns made against undertakings during year under the excess where not previously provided	–		(39,857)	
Less: drawdowns made against undertakings during year in excess of policy limits	(15,533)		–	
Less: balance of undertakings falling due after 31 December up to the amount of the insurance policy excess	(85,110)		(100,000)	
		245,557		(139,857)
		350,000		104,443
Less: insurance claim recoveries in the year		(133,777)		–
Insurance policy claim receivable at 31 December (<i>note 7</i>)		216,223		104,443
Charge to general fund account				
Drawdowns made against undertakings during the year under excess not previously provided		–	39,857	
Drawdowns made against undertakings during the year in excess of policy limits		15,533		–
Balance of undertakings falling due after 31 December under the Central Fund insurance policy excess		85,110	100,000	
Less: recoveries		(110)		–
		100,533	139,857	

The New Central Fund insurers have disputed their liability to meet claims made under the policy. As a consequence Lloyd's has commenced arbitration proceedings to recover amounts due, as described in *note 7*.

12 Total Fund balance	New Central Fund £000	'Old' Central Fund £000	Total £000
Balance at 1 January 2002 as previously stated	256,245	23,931	280,176
Restatement of deferred tax balances	46,653	–	46,653
Balance at 1 January 2002 as restated	302,898	23,931	326,829
Increase in general fund for the year	141,853	7,555	149,408
Balance at 31 December 2002	444,751	31,486	476,237

13 Reconciliation of operating surplus to operating cash flows before claims paid and insurance recoveries	2002 £000	2001 £000
Surplus/(deficit) before taxation	240,659	(25,859)
Undertakings given to insolvent members	346,200	244,300
Increase in insurance claim receivable	(245,557)	(104,443)
Claims paid in respect of individual members	2,231	1,215
Loss/(profit) on sale of investments	5,969	(11,127)
Loss on exchange	2,955	592
Decrease/(increase) in accrued income	1,288	(865)
Decrease/(increase) in other debtors	6,053	(8,835)
Increase/(decrease) in creditors	682	(1,603)
Net cash inflow from operating activities before claims paid and insurance recoveries	360,480	93,375

Lloyd's Central Fund notes to the financial statements continued

14 Analysis of cash flows for headings netted in the cash flow statement	2002 £000	2001 £000
Management of liquid resources:		
Purchase of government securities	(87,361)	(284,638)
Purchase of equities	(82,267)	(9,500)
Sale of government securities	89,213	216,575
Sale of equities	59,848	11,253
Net cash outflow from management of liquid resources	(20,567)	(66,310)

15 Analysis of net funds	At 01.01.02 £000	Cash flow £000	Other movements £000	At 31.12.02 £000
Cash at bank	566	(203)	(335)	28
Current investments	360,905	20,567	(40,574)	340,898
	361,471	20,364	(40,909)	340,926

Other movements include realised and unrealised exchange differences arising on the revaluation of foreign currency operating cashflows and investments.

16 Tutelle Limited

In 1996 the Council set aside, under a Lloyd's special account, £20m of the 'Old' Central Fund to secure the Society's obligations under staff indemnities and certain indemnities which have been given by Lloyd's to certain individuals and advisers in respect of the *Reconstruction & Renewal* plan. These include members of the Reserve Group, directors and officers of Equitas, members of the Council, Lloyd's Market Board, Lloyd's Regulatory Board and Corporation staff.

Unless and until there is any default under the security documentation, interest earned on the trust fund is paid to the 'Old' Central Fund.

The security was deposited for an initial period of two years and the Council exercised its discretion to renew this in June 1998.

The Council further amended the period of the deposit, in November 1998, so that the security could only be released if the Council was satisfied that there was no reasonable prospect of a claim being made under these indemnities.

Tutelle's position is under biennial review and, having been reviewed in June 2002, will be reviewed again in June 2004. The security may continue for a period of up to 80 years. Any of the funds remaining after this period will be repaid to the 'Old' Central Fund.

17 Lioncover Insurance Company Limited

In 1999, Lloyd's assigned to Lioncover £1m of the 'Old' Central Fund by way of security for a period of 10 years for its obligations to Lioncover under the indemnity bond referred to in *note 4*. The security was provided as consideration to those individual Names whose underwriting liabilities are reinsured by Lioncover for the release of Lloyd's syndicate 9001, for which Lioncover was substituted as direct reinsurer to close of those Names. Any of the funds remaining after this period will be repaid to the 'Old' Central Fund.

Unless and until there is any default under the security documentation, interest earned on the security is paid to the 'Old' Central Fund.

Lloyd's Members' Ombudsman's report

Report by Sir Brian Hayes GCB, Lloyd's Members' Ombudsman

I am pleased to present the annual report of the Lloyd's Members' Ombudsman to the Council of Lloyd's for the year ended 31 December 2002.

The role of the Lloyd's Members' Ombudsman is to investigate complaints by members of the Society who believe that they have suffered injustice in consequence of maladministration in relation to any action taken by or on behalf of the Society. The Byelaw also requires that I consider complaints from former members who were members at any time after 30 November 2001. The Ombudsman's powers do not extend to complaints that Names may have against underwriting agents.

During the year I received two new complaints; six fewer than the previous year. In both cases I decided, in the exercise of my discretion and after making preliminary enquiries, to take no further action, as I was satisfied that considerations of maladministration did not arise. In each case I explained to the complainant why this was so, with a detailed letter of response.

During 2002 I have also been required to consider further representations concerning five complaints that were referred to me in earlier years. In each of these cases it had been my original decision not to uphold the member's complaint, as I was satisfied that considerations of maladministration did not arise. After consideration of the new representations, I was not minded to alter my view in any of these cases.

The expenses incurred by my office amounted to £31,158.

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