

COVERHOLDER HANDBOOK

FEBRUARY 2006



IMPORTANT NOTE

This document (including the 'Application to become a Lloyd's approved coverholder') is not intended to be distributed to, or used by, any person or company in any jurisdiction or country where such distribution or use would be against any local law or regulation. In particular, the contents of this document do not form an offer to sell securities or insurance, or distribute securities in the United States, to a US person, or in any other jurisdiction where it is against local law.

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INTRODUCTION

This handbook is designed to help you if you want to become a Lloyd's coverholder and enter into contracts of insurance or issue insurance documents on behalf of a Lloyd's syndicate. The handbook is a guide to Lloyd's arrangements for coverholders and is effective from 1 March 2004.

This handbook deals with many of the main issues relating to being a Lloyd's coverholder but it is not intended to be a substitute for the Delegated Underwriting Byelaw or the relevant sections of the Underwriting Requirements which are attached to this handbook.

The handbook also contains copies of the documents and forms that you may need when dealing with Lloyd's.

If you have any questions about Lloyd's arrangements for coverholders please contact your sponsor. Up-to-date information about Lloyd's is available from the Lloyd's website at www.lloyds.com where you will also find information about coverholders and binding authorities.

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Appendices to the handbook

Please note you can access the appendices by clicking on the relevant link below.

Appendix 1: [Underwriting Requirements](#)

Appendix 2: [Application Form to become an approved coverholder](#)

Appendix 3: [Delegated Underwriting Byelaw \(No. 1 of 2004\)](#)

Appendix 4: [Lloyd's approved coverholder application form – Guidance notes](#)

Appendix 5: [Definitions Byelaw \(No. 3 of 2003\)](#)

INTRODUCTION TO THE LLOYD'S MARKET

How underwriting is carried out at Lloyd's

In the Lloyd's market, risks are insured by Lloyd's members who provide the capital to support the underwriting. Members can be either individuals (often known as 'names') or corporate entities.

Members of Lloyd's underwrite insurance by forming groups of members known as syndicates. Syndicates are annual ventures (meaning the syndicate members are different every year) and operate as independent business units within the Lloyd's market. A syndicate may have several members or one corporate member.

Syndicates are managed by Lloyd's managing agents who are approved by Lloyd's. The Lloyd's managing agent has authority to accept risks on behalf of the members of the syndicate and it appoints the underwriting team. Each member gives this authority to the Lloyd's managing agent through a standard agency agreement. Lloyd's managing agents are regulated by the UK Financial Services Authority (FSA) and are also subject to Lloyd's requirements.

The role of Lloyd's brokers is to place risks in the Lloyd's market on behalf of clients (although in certain circumstances, the Lloyd's managing agent may deal directly with clients). The Lloyd's broker also acts as the interface (point of contact) between its clients and the underwriter. Lloyd's brokers use their specialist knowledge to negotiate terms and conditions for clients and have a good understanding of the Lloyd's market. Many specialise in particular types and classes of risk.

What are coverholders and binding authorities?

Whilst a Lloyd's managing agent has authority to enter into contracts of insurance on behalf of a syndicate it manages, it can delegate its authority to another company or partnership (referred to as a company throughout this handbook). At Lloyd's, such a company is referred to as a coverholder. The document setting out the terms of the coverholder's delegated authority is known as a binding authority.

When a Lloyd's managing agent delegates its authority to a coverholder, the general principle is that the coverholder acts as agent of the Lloyd's managing agent (rather than as agent of the policyholder). So a coverholder acts as agent of the Lloyd's managing agent when, under the terms of a binding authority, it enters into contracts of insurance, or issues insurance documents as evidence of contracts of insurance, on behalf of Lloyd's underwriters.

A coverholder may also act as agent for the Lloyd's managing agent for collecting premiums or handling claims. The exact nature of the coverholder's authority to act for the Lloyd's managing agent is set out in the binding authority.

The role of the Lloyd's broker, as far as coverholders are concerned, is to arrange and administer binding authorities in the Lloyd's market on behalf of coverholders and to sponsor prospective coverholders.

In certain circumstances, a company that acts as a policyholder's broker may also be appointed to act as a coverholder and enter into contracts of insurance with policyholders on behalf of a Lloyd's managing agent. An insurance broker is normally the agent of the policyholder. However, when the broker is acting as a coverholder, it is acting as the agent of the Lloyd's managing agent.

Approval of coverholders

Lloyd's coverholders need to be approved. Approved coverholders may be based anywhere in the world and usually have authority to enter into contracts of insurance, or issue insurance documents as evidence of risks accepted, under what is known as a 'registered binding authority'.

THE ROLE OF LLOYD'S

The Lloyd's franchise

Legislative background

Lloyd's itself is not an insurer and does not insure risks. It is the Lloyd's managing agents that enter into contracts of insurance on behalf of syndicates. Lloyd's has the statutory responsibility to manage and supervise the Lloyd's market and those who operate in it. The Council of Lloyd's (the Council) is the governing body under the terms of the relevant UK Act of Parliament, Lloyd's Act 1982.

In order to carry out its functions, the Council can make byelaws. One such byelaw is the Delegated Underwriting Byelaw (No 1 of 2004) that sets out the current arrangements for coverholders and binding authorities at Lloyd's. Detailed requirements are also made under that byelaw and are referred to as the Underwriting Requirements. They set out certain fundamental requirements for Lloyd's coverholders and binding authorities.

The Lloyd's franchise

In September 2002, Lloyd's members voted in favour of a series of proposals to introduce a new franchise system for the Lloyd's market. The Lloyd's Franchise Board was established on 1 January 2003 with the goal 'to create and maintain a commercial environment at Lloyd's in which the long-term return to all capital providers is maximised'.

Lloyd's has set the franchise the following 'strategic imperatives' (requirements) which must be met. Those strategic imperatives are set out in the Chairman's strategy document and are as follows.

- To make sure the franchise's profitability consistently outperforms the competition.
- To have an outstanding ability to manage risk throughout the franchise.
- To be the market of choice for policyholders and brokers.
- To have a competitive international trading platform.
- To protect, strengthen and promote the Lloyd's brand.
- To have a high-quality, cost-effective business process within the franchise.
- To attract, retain and develop the best people throughout the franchise.

The Lloyd's Franchise Board is primarily responsible for decisions relating to strategic and policy issues, but also has some important operational responsibilities. It guides the commercial management of the market as well as setting market supervision and solvency policy in line with the requirements of the Financial Services Authority. The Lloyd's Franchise Board oversees the admission and removal of organisations operating under the Lloyd's brand and works to make sure that the market's business processes are more attractive to policyholders, brokers and those who provide capital.

Why does Lloyd's supervise coverholders?

Lloyd's supervises coverholders as part of its statutory role in managing and supervising the Lloyd's market. This supervision is carried out through the approval process and then through Lloyd's ongoing supervision of all approved coverholders.

The separate supervision of coverholders by Lloyd's itself is important. Lloyd's wants Lloyd's managing agents to delegate underwriting only to well-managed and financially secure coverholders. This will make sure that policyholders' interests are properly protected and will also protect and further improve Lloyd's reputation in the local territory since in certain overseas jurisdictions. Coverholders are considered by the local regulators to be branch offices of Lloyd's.

Lloyd's also supervises coverholders since, in many jurisdictions, Lloyd's is authorised to operate as a single entity, with a single collective licence. Local regulators may require Lloyd's to demonstrate that it has control over, and responsibility for, the business carried out under the terms of Lloyd's authorisation in that jurisdiction. Local regulators will often look to Lloyd's centrally to help solve any problems. Indeed supervision by Lloyd's can help to avoid such problems arising and help provide speedy and effective solutions if they do.

However, the primary responsibility to supervise coverholders and binding authorities on a day-to-day basis rests with Lloyd's managing agents. Lloyd's firmly believes that the best way of achieving the objective of promoting well-managed and successful delegated underwriting arrangements is to promote long-term partnerships between the coverholder, the Lloyd's managing agent and the Lloyd's broker.

APPLYING TO BECOME AN APPROVED COVERHOLDER

What an approved coverholder can do

If a Lloyd's managing agent has delegated its authority to an approved coverholder under a binding authority, the approved coverholder may enter into contracts of insurance and issue insurance documents as evidence that contracts of insurance have been accepted.

An approved coverholder will normally also be allowed to collect premiums, and may be allowed to handle claims or perform other functions. The scope of its authority will be set out in the binding authority.

Who applies for approval?

A company or partnership (an applicant) makes the application to be an approved coverholder. However, the application must be made through a sponsor (a Lloyd's broker or Lloyd's managing agent – see page 9 'The role of the sponsor').

Guidance on filling in the application form

The application to become an approved coverholder is attached to the coverholder handbook which can be found on www.lloyds.com.

The application form itself is in three sections.

- Part A is filled in by the applicant.
- Part B is filled in by the applicant's sponsor.
- Part C is filled in by a Lloyd's managing agent intending to delegate its authority to the applicant under a binding authority. (If that Lloyd's managing agent is also the sponsor, it will still need to fill in part C as, in that section, the Lloyd's managing agent confirms to Lloyd's that it has carried out an assessment in line with the managing agent's code of practice for delegated underwriting.)

When filling in the form it is essential that the applicant and the sponsor provide full and accurate answers to all the questions. If there is any doubt as to whether any fact or matter is relevant, it should be given. The applicant and its sponsor should remember that they will need to demonstrate to Lloyd's that the applicant is suitable to be an approved coverholder.

Explanation of the coverholder's undertaking to Lloyd's

An important part of the application form is the coverholder's undertaking to Lloyd's (section 20 of part A in the form).

The main purpose of the undertaking is to set out, in clear terms, the basic expectations Lloyd's has of coverholders when they deal with Lloyd's, their customers and clients, and Lloyd's managing agents and Lloyd's brokers.

By signing the undertaking, the applicant agrees to act in line with the terms of its binding authority and any local requirements of the territory in which it is based or in which it will trade, provide services or do business. The applicant also agrees to certain conditions that would apply if Lloyd's withdrew its approval or otherwise stopped it from accepting business under a binding authority.

By signing the undertaking, the applicant also agrees that it will answer any questions and produce any information to Lloyd's, when asked, if that information relates to the applicant's binding authorities or ongoing approval. The applicant also agrees to allow Lloyd's (or its agents, including its local representative) to visit its premises to inspect relevant documents.

In practice, Lloyd's would normally expect Lloyd's managing agents, rather than Lloyd's itself, to get such information from coverholders as part of its routine monitoring of their binding authorities. However, there may be times when Lloyd's (or its agents, including its local representative) may want to get information relating to the binding authority directly from the coverholder. This may be when the Lloyd's managing agent is unable, for whatever reason, to act or where Lloyd's has decided to review the coverholder's approved status. If Lloyd's exercises these rights under the undertaking, it will act reasonably and will do its best to co-operate with the coverholder, the sponsor and the Lloyd's managing agent of the lead syndicate as far as possible.

The role of the sponsor

An application must be sponsored by either a Lloyd's broker or a Lloyd's managing agent. The sponsor must check the accuracy of the answers provided by the applicant in part A of the application form and will also need to fill in part B of the application form. As well as its formal role in sponsoring the application, the sponsor will no doubt want to give the applicant advice on the Lloyd's market and the application process.

The role of the sponsor is extremely important in the application process. Lloyd's will rely on the sponsor's assessment of the applicant as the sponsor will have used its knowledge of the applicant, as well as its expertise in the relevant type of business, when assessing the applicant.

For this reason, Lloyd's will normally expect the sponsor to have known the applicant for a sufficient period in order to be satisfied about the applicant's suitability. Ideally, the sponsor will have had some insurance dealings with the applicant. If this is not the case, Lloyd's will expect the sponsor to explain the assessment it carried out in order to be satisfied with the applicant's dealings with other insurers.

When filling in part B of the application form, the sponsor should feel free to expand upon any answers it gives. This will help Lloyd's consider the application as quickly as possible.

The sponsor should:

- make sure that the applicant reads the Coverholder's Handbook and understands the duties and responsibilities of a Lloyd's coverholder;
- advise the applicant to take particular notice of the undertaking at section 20 in part A of the application form; and
- ideally provide the applicant with a sample wording of a binding authority.

What Lloyd's will do once it receives your application

The application will be handled by a member of the Coverholders Department at Lloyd's.

Lloyd's will check the application to make sure it has been filled in correctly and make sure that all necessary supporting documents have been provided.

In exceptional circumstances, it may not be appropriate to provide some documents with the application. In these cases, the reason for the documents not being provided should be given in the relevant box on the application form's checklist. Not providing documents may result in the application being delayed or returned.

If the application is incomplete, it will be returned and this will delay the application process.

The information provided on the application form will be assessed and verified. As part of this process, Lloyd's may ask the applicant, the sponsor or the Lloyd's managing agent of the lead syndicate to provide further information.

Lloyd's will consider the suitability of the applicant by assessing the information and documents provided with the application form as well as making further investigations. These further investigations may include the following.

- A pre-application audit report from an independent auditor or a managing agent visit report. This provides an opinion on the applicant's suitability to manage the proposed binding authority and gives explanations to support this opinion.
- Assessing the applicant's management and controls, financial position and operations (including, but not limited to, IT systems, premises and human resources).
- Where Lloyd's has a General Representative (including an attorney in fact for Illinois, Kentucky and USVI), a report from the Lloyd's General Representative confirming that the applicant meets Lloyd's requirements on local reputation, regulation, reporting, licensing, taxation and marketing requirements and that the General Representative supports the application.
- For US applicants (excluding Illinois and Kentucky), a report from a third party provider that supplies information, including details of the local reputation and financial security of the applicant.
- For other territories, a report by a firm appointed by Lloyd's for this purpose.

We strongly recommend that sponsors get an audit report or managing agent's visit report before they support an application. Although the Lloyd's General Representative's report is for the benefit of Lloyd's, we recommend that applicants tell the General Representatives that they intend to support an application so the General Representative can start their investigations. Contact details for the Lloyd's General Representatives can be found on lloyds.com. Taking these steps before making the application will speed up the approval process.

Extra information that may be asked for

Lloyd's may need to contact the sponsor, the applicant, the Lloyd's managing agent of the lead syndicate or others for further information about matters that may have come to light as a result of Lloyd's enquiries.

The most common requests for further information arise when:

- an underwriting plan has not been provided for the proposed Lloyd's business, and Lloyd's thinks that such a plan would help it to consider the application;
- there are questions arising from the financial information provided;
- there is not enough information about necessary licences; or
- the professional indemnity cover does not appear to be adequate.

If there are any further questions about the application, the Coverholders Department will ask the relevant parties to discuss those matters with them or with the relevant local Lloyd's representative. This is often an effective way to help resolve outstanding issues.

Finally, as part of the application process the applicant may be asked to provide funds or other security (for example, letters of credit, legal charges over property, guarantees) for settling and paying of insurance transactions. If Lloyd's believes that such funds or security may be necessary, it will discuss the matter with the applicant before making any decision.

How will Lloyd's reach its decision?

Before approving an application, Lloyd's will want to be sure that the applicant is suitable to be an approved coverholder and will add value to the Lloyd's franchise.

Lloyd's will take the following matters into account when deciding whether an applicant is suitable.

- a. Whether the applicant is a competent, proficient and capable organisation and in considering that Lloyd's may have regard to the following matters.
 - i) The applicant's compliance with appropriate principles of good corporate governance.
 - ii) The applicant's membership of any body or organisation that Lloyd's considers to be necessary or desirable.
 - iii) The quality and adequacy of the applicant's human resources including-
 - the competence, reputation, character and suitability of the applicant's directors, officers and staff; and
 - the knowledge and experience of the applicant's directors, officers and staff of the conduct and regulation of insurance business in the Lloyd's insurance market and in any other relevant jurisdiction.
 - iv) The quality and adequacy of the applicant's other resources, including the quality and adequacy of the applicant's -
 - systems, procedures, protocols and arrangements for the conduct of its business
 - resources to comply with appropriate service standards for its customers
 - resources to comply with such principles and standards for the conduct or administration of insurance business in the Lloyd's insurance market as the Franchise Board may from time to time prescribe, recognise or endorse
 - resources and systems for underwriting administration and for the administration and agreement of claims
 - v) The quality and adequacy of the applicant's controls and procedures to manage its business including -

- the applicant's arrangements for identifying, resolving or managing conflicts of interest and
 - the quality and adequacy of the applicant's controls and procedures for the management of underwriting risk and for the management of the administration and agreement claims.
- vi) The nature of the applicant's business including its past, present and forecast underwriting performance.
- b. Whether the applicant is of appropriate reputation and standing.
 - c. Whether any person who controls the applicant, or who is connected or associated with the applicant, is of appropriate reputation and standing.
 - d. Whether the applicant has adequate capital and financial resources.
 - e. Whether the applicant has adequate professional indemnity insurance.
 - f. Whether the applicant is capable and willing to comply with the terms of any undertaking given by it to Lloyd's.
 - g. Whether the applicant possesses all the licences, approvals or authorisations in order to act as an approved coverholder wherever it will conduct insurance business in that capacity."

If an applicant does not meet high professional standards, there may be a risk to the Lloyd's franchise, brand, reputation and licences. If Lloyd's has doubts about the applicant's suitability, it will not be approved.

The risk to Lloyd's of an approved coverholder becoming insolvent or unable to pay its insurance or other debts is an important consideration. So the financial standing of the applicant is thoroughly assessed. This may mean that appropriate financial safeguards have to be put in place before Lloyd's gives its approval.

Lloyd's and Lloyd's managing agents will want to be sure that individuals given either underwriting or claims authority have the necessary experience, reputation and ability.

If your application is successful

If Lloyd's approves your application, you will be told this by your sponsor. Lloyd's normally imposes a condition that you must be granted authority under a binding authority within three months from the date of approval, otherwise your approval will lapse. If this period needs to be extended, your sponsor will need to discuss this with the Coverholders Department.

Lloyd's may also place certain other conditions on your approval. These may include conditions that your approval is:

- restricted to particular types or classes of business;
- restricted to particular territories;
- restricted to certain types of binding authority;
- restricted to contracts led by a particular Lloyd's managing agent;
- restricted to contracts written 100% by a particular Lloyd's managing agent; or
- subject to an audit carried out to the department's specifications within a specified period.

Approval for insurance business does not automatically include reinsurance business. If you intend to operate a binding authority for reinsurance business as well as insurance business, please make this clear in your application.

If your application is rejected

If Lloyd's rejects your application, you will be told by your sponsor.

In those circumstances you must not hold yourself out in any way as being approved by Lloyd's as a coverholder and a Lloyd's managing agent cannot delegate its authority to you under a binding authority.

Where appropriate, Lloyd's may give you an indication of the reasons for the rejection. Lloyd's may also give you an indication of the necessary steps you should take before making any future application.

CONTENT OF BINDING AUTHORITIES

Your agreement to the terms and conditions in a binding authority

An important part of Lloyd's rules relates to the contents of every binding authority contract. Establishing the exact terms and conditions of the binding authority will make sure that you understand exactly what you can do – and how you must act as an approved coverholder. Agreeing these terms at the outset reduces the possibility of misunderstandings or disputes at a later stage.

It is for this reason that your Lloyd's broker (or Lloyd's managing agent) cannot register your binding authority at Lloyd's until you have agreed in writing to its terms and conditions. So you must not operate the binding authority until your Lloyd's broker (or Lloyd's managing agent) has confirmed to you that your binding authority has been registered with Lloyd's. This applies to both new and renewal business.

CONTENT OF INSURANCE DOCUMENTS

Contents to be included in insurance documents issued by coverholders to policyholders

As a coverholder there are certain items that you must include in all insurance documents you issue to policyholders as evidence of contracts of insurance. These documents should make policyholders aware of all the main terms of their policy and give them the necessary contact information so they can check the details of the policy or make a claim.

If you do not include all the necessary information in your insurance documents Lloyd's may take steps to remove your approval.

Your sponsor and Lloyd's managing agent will tell you what information you need to include in your insurance documents.

You must also make sure that insurance documents you issue contain all other provisions necessary under the laws or requirements of the jurisdiction where the contract of insurance was concluded or the insured is domiciled, or of any other relevant jurisdiction.

IMPORTANT ISSUES TO BEAR IN MIND

There are a number of standards that Lloyd's expects from all approved coverholders. These standards are set out together in the undertaking (section 20 of part A in the application form).

However, you should pay particular attention to the following.

Local requirements

As an approved coverholder, at all times you must comply with relevant laws, regulations and requirements of the territory in which you are domiciled, or in any other jurisdiction in which you trade, provide services or do business. This includes complying with all relevant insurance, financial and taxation requirements. Failure to comply with these requirements may have serious consequences for you, the relevant Lloyd's managing agent and for Lloyd's itself.

You must also comply with any requirements, guidelines or service standards set by the relevant Lloyd's representative.

If you have any questions about the standards expected of you in any particular territory, contact the relevant local Lloyd's representative and your sponsor. If there is no local Lloyd's representative in that territory, e-mail Worldwide Markets Services at market.services@lloyds.com. You can get contact details for Lloyd's representatives by selecting the relevant country on the 'Lloyd's Worldwide' area on the www.lloyds.com website.

Ban on sub-delegation

If a coverholder sub-delegates its authority to another party, this can undermine Lloyd's ability to supervise that coverholder. It may also prevent the Lloyd's managing agent from properly monitoring its binding authority. So only a Lloyd's managing agent can delegate the authority it has granted to a coverholder under a binding authority to another party. Lloyd's considers this to be such an important rule that if a coverholder does sub-delegate its authority, Lloyd's will normally withdraw that coverholder's approval. (A coverholder may, of course, delegate its authority to its own directors, partners or employees). A coverholder must never delegate its authority to enter into contracts of insurance, or to issue documents as evidence of contracts of insurance, to a third party.

Using the Lloyd's name and brand

Lloyd's issues guidelines to make sure that the Lloyd's brand is used consistently and to protect the Lloyd's trademark, which has been registered worldwide. You must comply with these guidelines. The current version of these guidelines may be found on the www.lloyds.com/coverholder_branding website. These guidelines may be updated so you should consult the guidelines on the website when necessary.

However, these guidelines do not address local insurance regulatory requirements including advertising restrictions and prohibitions which apply to intermediaries in some jurisdictions. Certain use of the Lloyd's name and logo, which might be allowed under the general guidelines below, might be against local law. So you should consult the relevant local Lloyd's representative

about such requirements. If there is no local Lloyd's representative in that territory, e-mail Worldwide Market Services at market.services@lloyds.com

You should comply with all local requirements relating to advertising (in whatever form, for example, in literature and on websites) and comply with all local requirements on selling insurance. Again, you should contact the Lloyd's local representative in the relevant jurisdiction (or e-mail Worldwide Market Services at market.services@lloyds.com) for further details.

Using the Lloyd's name

An approved coverholder may use Lloyd's name for advertising or on insurance documents which it issues for contracts of insurance 100% underwritten at Lloyd's. However, the Lloyd's name cannot be incorporated into a registered company name or trading title.

Once approved, you may describe yourself as a 'Lloyd's coverholder'.

An approved coverholder may use Lloyd's name to promote an insurance product, or on insurance documents it issues where that product or documents relates to a contract of insurance underwritten at Lloyd's. However, the name 'Lloyd's' cannot be used as part of the product name itself.

If a contract is not 100% underwritten at Lloyd's, the identity of the actual insurers must be made clear by using the appropriate statement (as set out in Lloyd's guidelines). The proportion of the risk being accepted by Lloyd's underwriters and other insurers must also be stated.

For those products which are not 100% underwritten at Lloyd's, an approved coverholder must make it clear that if any other subscribing insurers become insolvent, each underwriter at Lloyd's is liable for the portion of the risk it has underwritten and is not liable for the portion of risk underwritten by any other insurer, either at Lloyd's or elsewhere. Again you should refer to Lloyd's guidelines published on the Lloyd's website.

Using the Lloyd's logo

An approved coverholder may only use the Lloyd's logo for advertising on its website, on brochures and on insurance documents in limited circumstances. These circumstances are explained in Lloyd's guidelines published on the Lloyd's website.