

MARKET BULLETIN

From	Head Market Reporting (extn 5129)
Date	8 May 2006
Reference	Y3807
Subject	Half Year Interim Results for Capital Purposes
Subject areas	Coming-into-line and release of surplus assets
Attachments	
Action points	Managing agents, members agents and direct corporate members to note
Deadlines	Immediate

The purpose of this bulletin is to advise managing agents, members' agents and direct corporate members that the Franchise Board has agreed that half year interim results should be recognised for capital setting within the November Coming-into-line (CIL) exercise and for Release Test purposes. The recognition of half year interim results implements the objective in the Three Year Strategy – Building the Optimal Platform that Franchisees may pay out excess funds through the twice yearly release of booked profits, and capital providers are able to reduce their commitment where there is surplus capital.

The bulletin also advises of the timetable to be followed this year for submitting applications for release of profits and funds at Lloyd's and coming-into-line.

Recognition of interim profits

From a prudential viewpoint when recognising half year interim profits it will be necessary to take into account all interim half year results. Following the reporting of the half year interim results on 17 August 2006, Lloyd's will calculate a half year credit / deficit for each member. The resulting credit / deficit will be included in the Release Test calculations scheduled to be run towards the end of September and the November 2007 CIL calculations. There will be no physical transfer of funds from syndicate premiums trust funds in an already congested timetable. Only active members (including those ceased members who have made funds interavailable to an active member or where a ceased corporate member is part

of an ongoing corporate group and there is a cross deficit clause in place) will receive a credit / deficit which may be taken into account in the release of funds at Lloyd's.

To assist spread members in the auction season the half year position will be made available on 8 September 2006. Market Reporting will provide one figure per member being the aggregate credit / deficit across all syndicate participations. Managing agents will note that the timetable is very tight for advising members of their half year results following the submission of the final half year results, as reviewed by syndicate auditors, on 31 August. Late submission of the half year results may therefore lead to members being unable to recognise half year profits within the capital setting exercise.

It is recognised that the first auction will take place before 8 September 2006. At that time members' agents and managing agents may have different levels of information. Managing agents are reminded of their duty of disclosure with regard to auctions and members' agents are requested to ensure their members understand this position.

Please note that the QMR data in its normal format will be dispatched on the 24 August 2006 in accordance with the Business timetable.

Audit

The FSA Prudential Sourcebook (PRU) permits syndicates' externally verified half year interim profits to be recognised for capital purposes. The external verification of half year interim profits does not entail a full audit but may be limited to a review by the syndicate auditors of the managing agent's statement of interim profits with a review being given on a "not unreasonably stated" basis. The exact form of the interim audit report will be notified shortly. We enclose at appendix 1 the existing draft PN20 "Review for Interim Profit" as a guideline to the audit scope and opinion.

Restriction on Credit

Due to the nature of and the seasonal exposures of much of Lloyd's business, half year interim results would not capture the potential risk for the large number of syndicates with US windstorm exposures or other volatile classes of business which may translate into losses in the second half year. In view of this and the limited scope of the external verification any credit will be restricted to a maximum of 10% of a member's economic capital assessment (ECA). Attached at appendix 2 are examples of effect of the half year results. Any credit will be subject to withdrawal in the event of a major catastrophe prior to the November CIL date with exceptions granted on a case by case basis.

For prudence a half year deficit will be required to be covered in full. The potential half year credit has no impact on the mid year CIL requirement.

Timetable

The introduction of half year profits into the Capital Test impacts upon all of those involved in the Coming into Line process and in order to manage the workload the Releases and Coming into Line timetable has been modified as detailed below.

It is very important the members' agents and the MSU together deliver a high quality of service to members. Working to agreed service standards and deadlines forms a major part of this service. However it is accepted that for valid commercial reasons in a limited number of cases it may not always be possible to meet these deadlines. It is intended that a similar process to that in place for CIL assets received after the deadline is applied to the receipt of new member applications and surplus FAL release requests. Any of these requests received after the deadlines will be checked to ensure a valid commercial reason for lateness exists. Based on this check the files will be processed at MSU's discretion subject to additional charges to cover overtime and associated costs incurred in processing the requests after the deadline. It is estimated that the additional new member application charge will be £500 and the additional surplus FAL release charge will be £100, but both of these charges may increase in line with costs incurred.

In addition where an active member is entitled to a surplus FAL release as a result of the half year interim results it is expected that any release request submitted to the MSU takes into consideration the member's Coming into Line requirement, i.e. a surplus FAL release should not be followed by a provision of additional assets for Coming into Line.

28 April 2006	Release Test and Mid Year Coming Into Line funds at Lloyd's (FAL) valuations / calculations. The results of these tests will be available during week commencing 22 May 2006 and are used to determine the release of profits and surplus FAL.
30 June 2006	Deadline for clearing mid year CIL deficits
28 July 2006	Re-calculation of Release Test following the payment of losses deadline. The results of this test will be available during week commencing 25 August and will be used to determine the release of profits and surplus FAL.
28 July 2006	Valuation date for November CIL
29 September 2006	Re-valuation of members' FAL for CIL. Where a member's FAL has fallen in value by more than 10% compared with the 28 July value, the lower value must be used in the CIL calculation.
29 September 2006	Re-calculation of the Release Test for Active members only including an adjustment for half year profits. The results of this test will be available during week commencing 20 October 2006 and will be used to determine the release of surplus FAL.
29 September 2006	Deadline for receipt of new corporate member applications (including LLPs)
7 October 2006	Deadline for submission of surplus FAL release requests for non active members.
29 November 2006	Coming Into Line Date – deadline for the receipt of additional assets OR Surplus FAL release request for active members.

A further bulletin will be issued shortly setting out the detailed arrangements for CIL.

If you have any queries relating to the above timetable please contact Kim Harris ext. 2779 (kim.harris@lloyds.com) in the MSU

Any other queries relating to this bulletin, should be addressed to Kevin Nethersell ext. 6253 (kevin.nethersell@lloyds.com) or Mike Steer ext 5709 (mike.steer@lloyds.com). This bulletin is being sent to all managing agents, members agents, direct corporate members, recognised accountants, and market associations for information.

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Head
Market Reporting

Report on interim net profits

External verification of interim net profits for the purposes of PRU 2.2.14R (where the detailed scope of the work undertaken is set out in the engagement letter)

Review report by the auditors to the board of directors of XYZ Limited (“the company”)

In accordance with our engagement letter dated [date], a copy of which is attached as Appendix A, we have reviewed the company’s statement of interim net profits for the period from [] to [] (“the interim period”) as reported in the reporting statement (“the statement”) attached as Appendix B and dated [date].

The statement is the responsibility of, and has been approved by, the directors of the company. Our review of the statement did not constitute an audit, and accordingly, we do not express an audit opinion on the interim net profits reported therein.

Our review has been carried out having regard to rules and guidance contained in the FSA’s Integrated Prudential Source Book and Practice Note 20 “The Audit of Insurers in the United Kingdom (Revised)” issued by the Auditing Practices Board.

On the basis of the results of our review, nothing came to our attention to indicate that:

- (a) the interim net profits as reported in the statement have not been calculated on the basis of the accounting policies adopted by the Company in drawing up its annual financial statements for the year ended [date] *[except for changes arising from the adoption of revised accounting policies that will first be applied in the financial statements containing the interim period]**;
- (b) those accounting policies differ in any material respects from those required by *[Schedule 9A to the Companies Act 1985, UK financial reporting standards and the Statement Of Recommended Practice on Accounting for Insurance Business issued by the Association of British Insurers / International Financial Reporting Standards adopted by the European Commission in accordance with EC Regulation No 1606/2002]**; and
- (c) the interim net profits amounting to £[] as so reported are not unreasonably stated.

Date

* = delete as applicable

Half year results

	Low volatility risk syndicate: Profit	High volatility risk syndicate: Profit	High volatility risk syndicate: Loss
Economic Capital Assessment %	40	100	100
Capacity £m	100	100	100
Capital requirement £m	40	100	100
First half year result £m	4	25	(25)
Result recognised for capital purposes (10% of capital) £m	4	10	(25)
% of half year profit qualifying as credit	100	40	-