CHANGE OF CONTROL

PROCESS AND PROCEDURE
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EXECUTIVE SUMMARY

The purpose of this document is to set out the Lloyd's process and procedures for reviewing and approving prospective controllers of a Lloyd's Underwriting Agent. Underwriting agents are also known as managing agents.

Regulation

Under the Financial Services Market Act (FSMA) 2000, financial businesses (banks, insurance companies, IFAs, brokers, insurance intermediaries) are authorised by the Financial Services Authority (FSA).

The FSA also regulates Lloyd's Underwriting Agents and (since 2005) UK registered Lloyd's brokers.

What is a controller?

In very broad terms, the overriding principle is that where a company or individual acquires 10% or more of the shares and/or voting interests in an underwriting agent or approved run-off company or its parent company, the firm needs prior approval from the FSA and Lloyd's.

For a more detailed definition and thresholds of control over which Lloyd's and FSA will need to be notified of changes please follow the link below:


Note that Lloyd’s will also expect to be notified where a company or individual reduces their share and/or voting interests in an underwriting agent or approved run-off company or its parent company to below 10%.

Corporate Members

The FSA does not regulate Corporate Members. This guidance does not include change of control applications applicable to individual corporate members only. However, where the managing agent change of control does impact one or more Corporate Members, this process and procedure covers these members.

Where a change of control relates only to the Corporate Member the process is detailed here. Alternatively discussions should be held with Lloyd’s Market Services, Lloyds-Market-Services-Compliance-&-Membership@lloyds.com.
PROCEDURE

The approval of controlling interests in an underwriting agent requires both Lloyd’s approval (paragraph 43 of the Underwriting Byelaw) and the approval of the FSA. The processes will be run in parallel of each other but where appropriate activity will be co-ordinated between the FSA and Lloyd’s.

Types of Change of Control

There are three broad types of change of control. These are:

- Structural changes to the company or Group;
- Share ownership changes resulting in a new controller; and
- Acquisition by a third party.

Process Overview

The process for notification of changes of control is summarised as follows (see Appendix A for detailed process):

- Informal notification to Lloyd’s Head of Risk Management, Senior Operational Risk Manager or Risk Executive;
- Electronic notification to Lloyd’s of the intention to change a controller and confirmation that any tax implications have been explored with Lloyd’s Tax Department;
- Lloyd’s has 3 working days to respond to the initial notification and raise any immediate issues or to exercise its right to challenge;
- Detailed due diligence is then undertaken by Lloyd’s (further information on potential areas for consideration are detailed below);
- The firm subsequently submits the application to the FSA;
- The firm notifies Lloyd’s when FSA approval is granted; and
- Lloyd’s gives written approval once satisfied with all aspects of the transaction (including financing, Group and investors);
- Lloyd’s reserves the right to reject an application or perform additional due diligence as material information is presented.

Timing of Notification

Notification to Lloyd’s is to be completed when both parties have signed the Sale and Purchase Agreement.

Additional Information

For many changes of control, the change does not result in any operational, strategic or governance changes within the syndicate and/or the managing agent and the process is therefore straightforward. However, more complex changes of control have a more significant impact on the organisation and in these cases, additional work is required for Lloyd’s to fully understand and become comfortable with these issues. Once such a notification is received, the Lloyd’s Risk Management team coordinates as necessary with other Lloyd’s teams and the relevant managing agent in order to obtain the information required to understand the wider implications of the change of control. New controllers of managing agents are expected to ensure, and to demonstrate, that the managing agent will continue to meet the Franchise Standards, Principles of Relationship as well as Solvency II requirements on an ongoing basis.

Further information on the Franchise Standards is included within Appendix B.

The change of control process normally comprises of a series of internal and external meetings, facilitated by the Lloyd’s Risk Management team, to obtain the necessary information and assurances before the change of
control can be approved by Lloyd’s. A fundamental part of this process is the opportunity to meet with one or more of the new controller’s Board to gain some insight into its overall corporate culture, its understanding of Lloyd’s and its long term vision for the managing agent and its syndicate(s).

Any changes to such plans would be subject to Lloyd’s consideration and approval through the appropriate business as usual processes.

Areas which will be of significant interest to Lloyd’s and the likely subject of meetings with the managing agent and/or the new controller may include:

<table>
<thead>
<tr>
<th>Area</th>
<th>Action as part of change of control process</th>
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<tbody>
<tr>
<td>Capital Arrangements</td>
<td>Any proposed changes to the existing capital arrangements of the managing agent will be discussed to ensure that the capital requirements are adequately met on an ongoing basis. This will include proposed adjustments to the Funds at Lloyd’s (FAL), names and corporate member.</td>
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<tr>
<td>Syndicate Business Plan</td>
<td>Any proposed changes to an existing business plan, including any new shared group reinsurance arrangements, will have to be approved by Lloyd’s Syndicate Underwriting Performance Department. Significant changes to the business plan may require a resubmission of the syndicate solvency capital requirement (SCR).</td>
</tr>
<tr>
<td>Managing Agent’s Governance Structure</td>
<td>Lloyd’s will need to understand any proposed changes to the agent’s senior management team and board membership. Appointments of any new board members and/or changes to the Active Underwriter will require Lloyd’s approval, taking the minimum standards and Solvency II requirements into account.</td>
</tr>
<tr>
<td>Ownership</td>
<td>Lloyd’s will need to understand the new ownership arrangements, ownership structure, strategy and impact on names and members agents.</td>
</tr>
<tr>
<td>Risk Management and/ or Internal Audit</td>
<td>Any proposed changes to the control functions will be discussed with the managing agent and/or the new controller to ensure that the Lloyd’s minimum standards continue to be met and that Solvency II requirements have been taken into account.</td>
</tr>
<tr>
<td>Operations</td>
<td>Lloyd’s will need to understand any operational implications of a change of control, which could include but not be limited to:</td>
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<td>• relocation of office premises and the impact this may have on the firm’s business continuity planning;</td>
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<td>• IT systems migration;</td>
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<td>• changes to staffing levels;</td>
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<td></td>
<td>• changes to any outsourcing arrangements; and</td>
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|                                     | • processes and resources which may become shared functions within the group (for example
Typically, the outcome of this process is that Lloyd’s approves the change of control or approves the change with a number of conditions imposed upon the managing agent.

### Examples of Change of Control

These examples have been set out roughly in order of significance:

<table>
<thead>
<tr>
<th>Example</th>
<th>Description</th>
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<tr>
<td>1</td>
<td>Company A acquires Holding Company B or Managing Agency B. In this scenario it is assumed the new holding company is new to the Lloyd’s market. Our due diligence is likely to necessarily be quite extensive in order to understand the background to the proposed controller and its plans for the agency and syndicate. Change of Control would be subject to detailed review of the areas of focus and due diligence. Series of meetings would be held to meet proposed new controller and understand the specifics of the transaction.</td>
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<td>2</td>
<td>Holding Company A owns Managing Agency A but acquires Holding Company B who in turns owns Managing Agency B. Given that in this scenario the new controller is already essentially a participant in the Lloyd’s market, our focus would most likely need to be in understanding its future strategy, ability to integrate the new business into its group and whether its infrastructure could cope with the increased size in the business. Change of Control would be subject to (but not limited to) review of the areas of focus.</td>
</tr>
<tr>
<td>3</td>
<td>Shareholding of Holding Company or Managing Agency changes. An existing shareholder increases stake to above 10% (hence becoming a change in ownership is fairly small, we may obtain comfort from a fairly minimal amount of due diligence. Change of Control would be subject to (but not limited to) review of the areas of focus.</td>
</tr>
</tbody>
</table>
to (but not limited to) review of the changes within the shareholding of the company.

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<tr>
<th>4</th>
<th>Holding Company A owns Managing Agency A. Holding Company A changes the structure of companies within the group.</th>
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<tr>
<td></td>
<td>This is often a fairly straightforward administrative change, whereby the ultimate shareholdings are often the same, or very similar. A key thing to obtain is a structure chart showing the structure both before and after the change and to confirm whether the ultimate shareholders in the group are actually changing, or whether there are any other changes in the ownership of the agent.</td>
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<tr>
<td></td>
<td>Change of Control would be subject to (but not limited to) review of the changes of the corporate structure.</td>
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<td></td>
<td>A typical example of this is where a group wants to place its ultimate parent in a different domicile, e.g. Bermuda.</td>
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Appendix A
Change of Control Process

Informal Notification to Lloyd's

Internal Team Lloyd's Meeting

Internal Syndicate Risk Committee

Formal Notification via Lloyds.com

FSA Application Submitted

Change Type?

Complex Change

Basic Change

Summary Produced by Lloyd's

Obtain Lloyd's Internal Approval

Complete Lloyd's Executive Briefing Paper

Formal Confirmation to Lloyd's

Lloyd's Approval Letter

Monitor Implementation on an Ongoing Basis

Parallel Process
Appendix B
Franchise Standards and Guidance

FRANCHISE STANDARDS AND GUIDANCE

Lloyd's has overall performance objectives for the franchise. Each managing agent must perform to the standard required for the franchise to succeed overall. To ensure that the requirements are clear, Lloyd's has developed the Franchise Standards.

The Franchise Standards set out Lloyd’s requirements of each managing agent. They are driven by Lloyd's Franchise objectives, and take into account the expectations of the FSA.

The Franchise Standards have been produced in consultation with the Lloyd's Market Association, representing all Lloyd’s managing agents. The Franchise Standards reinforce Lloyd's brand, thereby maintaining Lloyd's Market reputation and the reputation of all firms trading there.

Lloyd’s expectations of new controllers
The Franchise Standards apply to existing managing agents, and new entrants seeking admission. They also apply to Lloyd's (the Corporation), where applicable.

New controllers of managing agents will be expected to ensure managing agents continue to meet the Franchise Standards and implement appropriate actions where they do not.

What are the Franchise Standards?
There are six elements to the Lloyd’s Franchise Standards. These are:

- Underwriting Management
- Claims Management
- Risk Management
- Effective Operational Processes
- Governance
- Protecting Lloyd’s Reputation and Brand

Franchise Standards structure

Principles
These are statements of business conduct required by Lloyd’s. The Franchise Standards are established under relevant Lloyd’s Byelaws relating to business conduct. The Franchise Standards apply to all businesses, regardless of size, complexity, diversity or organisational structure.

Guidance
The ‘Guidance’ notes which accompany the Franchise Standards have been developed with extensive market involvement and support. These provide a more detailed explanation of the general level of performance.
expected. They are a starting point against which each managing agent can compare its current practices to assist in understanding relative levels of performance. These ‘Guidance’ notes are intended to provide reassurance to managing agents and their controllers as to approaches which would certainly meet the minimum standards. However, it is appreciated that there are other options which could deliver performance at or above the minimum level and it is fully acceptable for managing agents to adopt alternative procedures as long as they can demonstrate that the required minimum standards can be achieved or exceeded.

Advice
Advice may also be issued in the future. This potentially could take the form of tools or practical solutions relating to the required business conduct. Advice may include techniques, templates and worked practical examples which may be adopted by businesses to meet their specific needs.

How will managing agents be assessed against the Franchise Standards?

- All managing agents are required to meet the Franchise Standards. These represent the minimum level of performance required of any organisation within the Lloyd’s Market.
- In assessing performance Lloyd’s will take account of the historical record of the syndicate(s) managed and the experience of underwriters, as well as the effectiveness of management procedures.
- Managing agents that manage only to the minimum standard required should expect the level of capital within their SCR}s to reflect that level of operating risk.
- Managing agents able to demonstrate consistently higher levels of performance, by comparison to the minimum standards, may be able to justify lower levels of capital within their SCRs, reflecting lower operating risk.
- As part of any change of control application the applicant will be required to demonstrate their immediate capability to meet the Franchise Standards.

Measurement & Monitoring of the Standards

- Lloyd’s will seek assurance that managing agents meet the Franchise Standards, via existing processes of review wherever possible.
- Data will be required to assess performance across the Lloyd’s Market and every effort will be made to ensure that the number of individual data requests by Lloyd’s is rationalised and duplication avoided.
- Benchmarking information will be provided to managing agents wherever possible, to assist in the management of their own businesses.
- Managing agents should be able to measure and monitor their performance to demonstrate that the Franchise Standards are being met. Internal reporting should enable each managing agent’s board to
assess performance and respond to those areas which may need improvement.

- Lloyd’s will work with managing agents in its ‘business partner’ role to assist them in identifying and implementing necessary improvements where requested.

- As stated above each managing agent is expected to at least meet the Franchise Standards and there will be adequate time allowed to address any gaps. Thereafter, any persistent and significant underperformance will be addressed in proportion to the issues involved.

Where can I find out more information?
For more detailed information on the Franchise Standards including guidance and principles, please click on the following link: Franchise Standards or visit the website.