5.0

How Lloyd's Works

5.1

How Lloyd's Works
What is Lloyd's / Lloyd's Market Structure

The business written at Lloyd's is brought to specialist syndicates, who price and underwrite risk, via brokers and coverholders.

Under its globally recognised name, Lloyd's acts as the market's custodian and is backed by diverse global resources and a capital structure designed to ensure financial security. Lloyd's works with an international distribution network to increase the use of insurance – building the resilience of local communities and supporting global economic growth.

Led by expert brokers and underwriters operating in more than 200 territories, the Lloyd's market develops and distributes complex and critical insurance to help underwrite human progress.

With expertise earned over centuries, Lloyd's is an influential force in the insurance industry. Its Vision 2025 strategy, launched in 2012, is aimed at ensuring that it remains a global centre for specialist insurance and reinsurance, facing future challenges head-on while grasping the opportunities of a fast-changing world.

Lloyd's Market Structure

Members – providing the capital
The capital to underwrite policies is provided by members of Lloyd's. This capital is backed by many of the world's major insurance groups, listed companies, individuals and limited partnerships, with corporate groups providing the majority of the capital for the Lloyd's market.

Syndicates – writing the insurance
A Lloyd's syndicate is formed by one or more members joining together to provide capital and accept insurance risks. Most syndicates write a range of classes of business but many will have areas of specific expertise. Syndicates are, technically, set up on an annual basis. In practice, they usually operate from year to year with members having the right, but not the obligation, to participate in syndicates the following year. This continuity of capital backing the syndicates means they function like permanent insurance operations. Each syndicate sets its own appetite for risk, develops a business plan, arranges its reinsurance protection and manages its exposures and claims. **At 31 December 2016 there were 99 syndicates at Lloyd's.**

Managing agents – managing the syndicates
A managing agent is a company set up to manage one or more syndicates on behalf of the members. Managing agents have responsibility for employing underwriters, overseeing their underwriting and managing the infrastructure and day-to-day operations. **At 31 December 2016 there were 57 managing agents at Lloyd's.**

Policyholders – transferring risk
Policyholders include businesses, organisations, other insurers and individuals from around the world who seek to mitigate the impact of potential risks. Policyholders may access the Lloyd's market via a broker, coverholder or service company.

Brokers – distributing business

Lloyd's is a broker market in which strong relationships, backed by deep expertise, play a crucial part. Brokers facilitate the risk transfer process between policyholders and underwriters. Much of this business involves face to face negotiations between brokers and underwriters. **At 31 December 2016 there were 258 brokers at Lloyd's.**

Coverholders and service companies – offering local access to Lloyd's

A managing agent may also authorise third parties to accept insurance risks directly on behalf of its syndicates. These businesses, known as coverholders, form a vital distribution channel, offering a local route to Lloyd's in many territories around the world. **At 31 December 2016 there were 3,859 approved Coverholder office locations.**

A service company operates like a coverholder but is a wholly owned subsidiary of a managing agent or its group. Unlike a coverholder, a service company is able to sub-delegate underwriting authority to other coverholders. **At 31 December 2016 there were 380 service companies at Lloyd's, with the majority in the UK and the US.**

Corporation of Lloyd's – supporting the market

The Corporation oversees the Lloyd's market. It provides the market's infrastructure, including services to support its efficient running, and protects and maintains its reputation.

Members' agents – supporting the members

Members' agents provide advice and administrative services to members, including assisting with syndicate selection. **At 31 December 2016, there were four members' agents at Lloyd's.**

The Corporation's role includes:

– Managing and protecting Lloyd's network of international licences;
– Agreeing syndicates' business plans and evaluating performance against those plans. Syndicates are required to underwrite only in accordance with their agreed business plans. If they fail to do so, Lloyd's can take a range of actions including, as a last resort, stopping a syndicate underwriting;
– Monitoring syndicates' compliance with Lloyd's minimum standards; and
– Continuing to raise standards and improve performance across two main areas:
  - overall risk and performance management of the market; and
  - maintaining and developing the market's attractiveness to capital providers, distributors and clients, while preserving its diversity.

The Corporation's Executive Committee exercises the day-to-day powers and functions of the Council of Lloyd's and the Franchise Board. **At 31 December 2016 the Corporation and its subsidiaries had 1,062 staff.**

5.2

How Lloyd's Works
Lloyd's Business Model

The Lloyd's market
Among Lloyd's defining features are the diversity of its underwriting portfolio and its very wide, and expanding, geographic reach.

Access to international insurance markets is one of Lloyd's greatest assets. It has specific trading rights to write insurance business in more than 75 jurisdictions and the ability to write reinsurance in more than 200 countries and territories. While the US and UK remain dominant markets for Lloyd's, in recent years there has been an increase in business from locations such as Singapore, China and Latin America.

Lloyd's has been working to extend and enhance its geographical coverage to reflect the evolution of the global economy and the dispersal of insurance capacity. During 2016, it increased its access in India.

Lloyd's capital structure
Lloyd's capital structure, often referred to as the Chain of Security, provides excellent financial security to policyholders and capital efficiency for members. The capital structure provides the financial strength that ultimately backs all insurance policies written at Lloyd's and the common security that underpins the market's strong ratings and global licence network. Lloyd's capital structure has three elements:

Syndicate assets – members' working capital – the first link in the Chain of Security
All premiums received by syndicates are held in trust by the managing agents as the first resource for paying policyholders' claims and to fund regulatory deposits. Until all liabilities have been provided for, no profits can be released. Every year, each syndicate's reserves for future liabilities are independently audited and receive an actuarial review.

Funds at Lloyd's – members' capital deposited at Lloyd's – the second link in the Chain of Security
Each member, whether corporate or individual, must provide sufficient capital to support their underwriting at Lloyd's. Managing agents are required to assess the Solvency Capital Requirement (SCR) for each syndicate that they manage. This sets out how much capital the syndicate requires to cover its underlying business risks at a 99.5% confidence level.

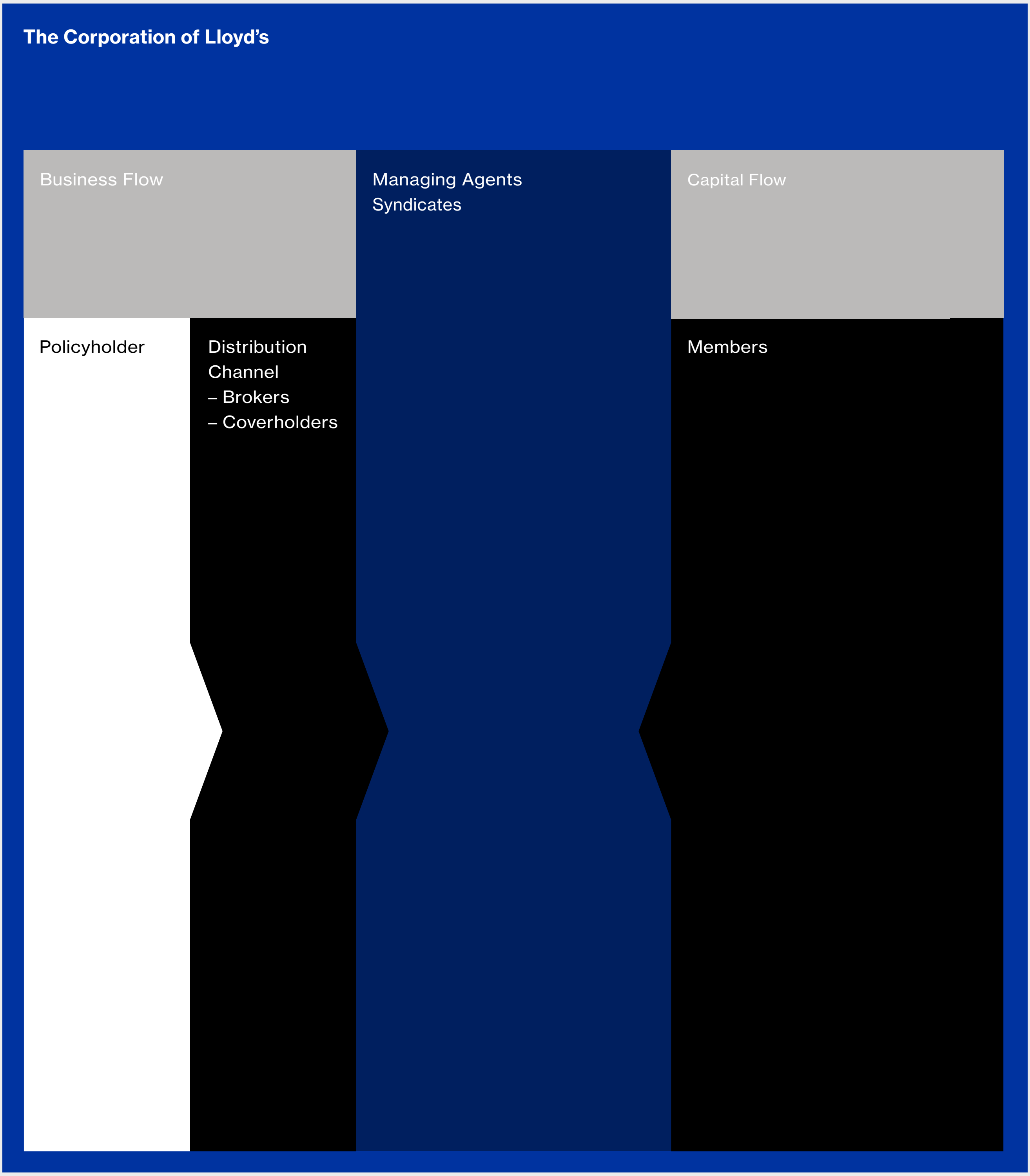
In light of Lloyd's mix of business, it is important that this assessment goes beyond the 12 month horizon required by Solvency II and must cover the risk of such extreme losses until all liabilities are paid and extend to an ultimate basis.

The Corporation reviews each syndicate's SCR to assess the adequacy of the proposed capital level. When agreed, each SCR is then 'uplifted' to ensure there is sufficient capital to support Lloyd's ratings and financial strength. The uplift applied for 2017 is 35%. This uplifted SCR is known as the syndicate's Economic Capital Assessment and drives members' capital levels across all of the syndicates in which they participate in proportion to their share of those syndicates. Each member's capital is held in trust by the Corporation for the benefit of policyholders but is not available for the liabilities of other members.

Lloyd's central capital – the third link in the Chain of Security
Lloyd's central assets, which include the Central Fund, are available, at the discretion of the Council of Lloyd's, to meet any valid claim that cannot be met from the resources of any member.

Should syndicates need additional assets to meet their liabilities, the funds at Lloyd's ensure that members have additional resources available. In the rare event that a member's capital is insufficient and that member is not able to provide further assets to the relevant syndicates, Lloyd's central capital provides further financial support to ensure valid claims are paid. The Corporation calculates the central Solvency Capital Requirement, which is independently validated and overseen by the PRA. The Franchise Board sets the level of economic capital needed above the regulatory minimum to meet its risk appetite and support the market's ratings and global licence network.

Market structure



5.2

How Lloyd’s Works
Lloyd’s Business Model

Lloyd’s Chain of Security

Several assets

First Link	Syndicate level assets £53,890m
Second Link	Members’ funds at Lloyd’s £21,703m

Mutual assets

Third Link	Central Fund £1,952m Corporation £44m	Callable layer £903m
	Subordinated debt/ securities £883m	

Lloyd's ratings

All Lloyd's syndicates benefit from Lloyd's central resources, including the Lloyd's brand, its global licences and the Central Fund. As all Lloyd's policies are backed by this common security, a single market rating can be applied. Lloyd's financial strength ratings apply to all policies issued by Lloyd's syndicates since 1993.

Three of the world's leading insurance rating agencies – Standard & Poor's, Fitch Ratings and A.M. Best – assess Lloyd's capitalisation and financial strength. Additional information on the security underlying policies at Lloyd's can be found on the Lloyd's website.

Lloyd's ratings at 31 December 2016

Standard & Poor's: A+ (Strong)

A+

Fitch Ratings: AA– (Very Strong)

AA-

A.M. Best: A (Excellent)

A

5.3

How Lloyd's Works
The Lloyd's Market

Acappella Syndicate 2014	ADVENT A FAIRFAX Company	AEGIS	ALLIED WORLD
AmTrust at Lloyd's An AmTrust Financial Company	antares	APOLLO Syndicate Management Limited	Arch Underwriting at Lloyd's
ARCUS 1856	Argenta	ArgoGlobal Member Argo Group	Ariel Re Member Argo Group
ARK	ascot	ASPEN	asta
ATRIUM	AXIS	Barbican Insurance Group	Beaufort Underwriting Agency Limited
beazley	BRIT Global Specialty	CAPITA	CATHEDRAL Underwriting Ltd
Charles Taylor Managing Agency	Chaucer	CHINA RE Syndicate 2088 at Lloyd's	CHUBB
CNA / HARDY	Dale Underwriting Partners	DW 1991	Endurance
ERS	EVEREST Everest Re Group, Ltd.	FARADAY	Hamilton at Lloyd's
HISCOX	icat Syndicate 4242	Liberty Specialty Markets	MAP underwriting at lloyd's

MARKEL

MS Amlin

Munich Re Syndicate Limited

Munich RE

Navigators
Insuring A World In Motion®

NEON

Nephila

Newline Group

Novae
LOOKING FORWARD

Pembroke
MANAGING AGENCY

1492
PROBITAS

ProSight
Specialty Insurance

QBE

R&Q

RenaissanceRe

RiverStone
A FAIRFAX Company

S A Meacock & Company Limited

Sirius
International

SKULD

SOMPO CANOPIUS

STARR
COMPANIES

STARSTONE

SYNDICATE
2525

TALBOT
VALIDUS GROUP

The Channel Managing Agency

The Standard Syndicate

TOKIO MARINE
HCC

TOKIO MARINE
KILN

TRAVELERS

VIBE
SYNDICATE MANAGEMENT

W/R/B
UNDERWRITING
a W. R. Berkley Company

XL CATLIN

5.4

How Lloyd's Works
Lloyd's Value Creation

Throughout history, human progress has gone hand-in-hand with risk taking. From the smallest idea to the largest expedition, whether considerable or minimal, risk, to some degree, is an ever-present factor. Properly quantified and managed, it should not be a barrier to success. Indeed, risk taking is key to making progress.

The role of insurance is to transfer risk, so providing individuals and organisations with the confidence to undertake endeavours that might otherwise be avoided.

In this way, insurance – and Lloyd's as one of its most well-known names – can be seen as having played a significant role in underwriting human progress. The 17th century saw Lloyd's insuring ships and their cargoes as new trade routes were opened up around the globe. It has provided cover for ventures such as the first non-stop transatlantic flight, the first airships and missions to the International Space Station.

Today, Lloyd's continues to support technological progress, developing policies that cover the use of aerial drones and pioneering the first cyber-security liability policy.

Lloyd's itself provides a platform for individual commercial business to thrive. It is a varied market, ranging from large international organisations to smaller niche businesses. Lloyd's syndicates often cover complex risks, including categories such as shipping, aviation, nuclear, climate, pandemics, political risk and energy.

For those seeking such protection, whether individuals, companies or even governments, the confidence that their insurance policies have sound financial backing and that their claims will be dealt with fairly and quickly is paramount. This confidence is fundamental to Lloyd's global brand and reputation. Lloyd's is a globally recognised and highly valued brand within the insurance industry.

Benefits to brokers and policyholders

Underwriting expertise and product offering – The Lloyd's market is a recognised centre of specialist underwriting, claims and analytics expertise. This expertise supports a wide range of specialist insurance and reinsurance products, often developed to meet complex and challenging insurance needs.

Claims payment – Lloyd's is proud of its reputation for paying all valid claims in a timely and efficient manner.

Security and ratings – The single market ratings – from Standard & Poor's, Fitch Ratings and A.M. Best – reflect the fact that all contracts underwritten at Lloyd's are backed by Lloyd's Chain of Security. All policyholders benefit from the robust financial position of the market as a whole.

Benefits to syndicates and capital providers

Market access – Through Lloyd’s central licensing arrangements syndicates at Lloyd’s are able to access business from more than 200 countries and territories. The London underwriting room, in which transactions take place on a face to face basis, and Lloyd’s strategically located international hubs are all supported by a global network of representatives with extensive local knowledge.

Lloyd’s has been described (for example, in a 2014 report from Standard & Poor’s) as the ‘natural’ home for some areas of specialist insurance and so is an equally natural choice for those looking to underwrite in these specialist fields.

Capital advantages – Lloyd’s capital framework, under which insurance commitments are underpinned by a Central Fund, is efficient and flexible.

Central processes – Lloyd’s market infrastructure supports its efficient operation. The Corporation provides central cash settlement and up to date information on regulatory and legal changes that could have an impact on underwriting decisions. It provides efficient tax and regulatory reporting to help the market meet its requirements and represents the market’s interests to regulators and governments.

Market oversight – The Corporation aims to strike a proportionate balance between supporting a robust market oversight regime and supporting the entrepreneurial and innovative culture that has contributed to its growth and reputation for more than three centuries. It seeks not only to work with market participants wanting to develop new and innovative products but also to foster new thinking for the market as a whole – for example, through research into emerging risks and their potential mitigation.

Benefits to society and the economy

Economic contribution – Lloyd’s is part of the broader London insurance market, which employs around 48,000 people – 34,000 of them in London. It contributes some £60bn to the UK’s GDP – more than a fifth of the City of London’s GDP contribution. In 2016, 148 of FTSE 250 companies and 29 of the 30 listed in the Dow Jones Industrial Average were insured at Lloyd’s.

Contribution to society – Lloyd’s also has a part to play globally in supporting the communities in which it operates and in taking a lead on wider social and environmental issues. This is reflected in its commitment to Global Corporate Social Responsibility as part of Vision 2025. Lloyd’s continues to be an active member of the ClimateWise initiative, a collaborative endeavour by insurers to drive action on climate change.

Lloyd’s also co-ordinates a number of Corporate Social Responsibility (CSR) programmes. During 2016 these included a week-long series of global events for the UN World Environment Day and the Dive-In festival focusing on diversity and inclusion.

The provision of risk transfer, through insurance and reinsurance, gives Lloyd’s policyholders the confidence to undertake activities that carry risk and the potential to recover when things go wrong.

In this way, Lloyd’s helps to underwrite human progress and it has created – and continues to create – value to society that far exceeds any financial measure.

5.5

How Lloyd's Works
Lloyd's Market Governance

The governance and oversight framework for the Lloyd's market is designed to ensure that both the Corporation and managing agents in the Lloyd's market have robust and comprehensive systems of governance, risk management and internal controls. The underlying objective of this overall framework is that the Corporation and the market actively manage risks to the Central Fund, Lloyd's licences, ratings and brand and to ensure good outcomes for policyholders.

Lloyd's governance and risk management

The Council of Lloyd's is Lloyd's governing body and has ultimate responsibility for overall management of the market. The Council delegates many of its functions to the Franchise Board, whose members are appointed by the Council and come from both inside and outside the Lloyd's market. The Franchise Board is responsible for, among other things, supervising and regulating the market and owns Lloyd's risk management framework.

Lloyd's risk management framework identifies the key risks that Lloyd's faces and enables an assessment of these risks on a common basis.

The Franchise Board has delegated to the Risk Committee responsibility for oversight of risks and providing regular assurance to the Board that those risks are managed in accordance with approved policies and risk appetites.

Oversight of the Lloyd's market

Each managing agent within the market has the responsibility for its own corporate governance. However, the Corporation provides a comprehensive market oversight framework for the governance of these businesses. This covers performance management, capital setting and risk management. The framework includes extensive Minimum Standards, including a Governance Minimum Standard, to which managing agents must adhere. The Corporation regularly assesses compliance with these standards.

The Corporation's oversight activity is published in its 2017 Market Oversight Plan. This provides managing agents with a summary of the Corporation's view of the key risks facing the market in 2017, together with the key oversight activities that the Corporation will undertake during the year.

The Corporation's oversight role through this framework is crucial. The Corporation is accountable to the Prudential Regulatory Authority (PRA) and Financial Conduct Authority (FCA) for this (see below).

Managing agents' boards play an important role in ensuring that their firms' business plans, strategy and key risks are subject to appropriate and effective levels of oversight and challenge.

External regulation

In addition to the oversight and supervision provided by the Corporation as set out above, the Corporation and managing agents are regulated by the PRA and FCA. Members' agents and Lloyd's brokers are regulated by the FCA alone.

The Corporation is required by the PRA to meet various prudential requirements relating to capital and solvency and to demonstrate that the Lloyd's market is soundly and prudently managed.

The FCA's focus is on ensuring that the Corporation and managing agents have systems and controls in place to manage conduct risk arising from business underwritten at Lloyd's, with a view to securing an appropriate degree of protection for policyholders.

5.6

How Lloyd's Works
Managing Agents and Syndicates

The table shows the key characteristics for managing agents and syndicates active as at 31 December 2016.
In 2016, Lloyd's wrote gross premiums of £29,862m.

Managing Agent (MA)	Managed syndicate(s)	2016 GWP* £m	2015 GWP* £m	Percentage of member owned by MA group %
ACE Underwriting Agencies Limited	1882	62	99	100%
	2488	408	378	100%
Advent Underwriting Limited	780	190	157	100%
AEGIS Managing Agency Limited	1225	377	333	100%
Allied World Managing Agency Ltd	2232	164	144	100%
AmTrust at Lloyd's Limited	44	14	17	100%
	1206	238	154	100%
	2526	30	29	99%
AmTrust Syndicates Limited	779	20	14	0%
	1861	259	222	100%
	5820	251	228	68%
Antares Managing Agency Limited	1274	338	261	100%
Apollo Syndicate Management Limited	1969	215	188	20%
Arch Underwriting at Lloyd's Ltd	2012	179	154	100%
Argenta Syndicate Management Limited	2121	281	227	43%
Argo Managing Agency Limited	1200	514	421	85%
	6117	46	24	0%
Ark Syndicate Management Limited	4020	312	337	87%
Ascot Underwriting Limited	1414	573	567	100%
Aspen Managing Agency Limited	4711	404	331	100%
Asta Managing Agency Limited	1686	216	118	0%
	1729	87	66	0%
	1897	113	97	0%
	1910	200	275	0%
	2357	128	47	0%
	2525	50	44	0%
	2786	59	0	0%
	4242	137	111	0%
	6123	14	4	0%
	6126	28	0	0%
Atrium Underwriters Limited	609	413	383	25%
Barbican Managing Agency Limited	1856	85	0	0%
	1955	313	328	100%
	6118	78	48	63%
Beaufort Underwriting Agency Limited	318	137	137	91%
Beazley Furlonge Limited	623	293	248	9%
	2623	1,333	1,131	100%
	3622	17	14	100%
	3623	195	172	100%
	6050	15	12	0%
	6107	36	31	28%
Brit Syndicates Limited	2987	1,412	1,308	100%
Canopius Managing Agents Limited	4444	1,064	827	83%
Capita Managing Agency Limited	1492	43	3	0%

5.6

How Lloyd's Works
Managing Agents and Syndicates

Managing Agent	Managed syndicate(s)	2016 GWP* £m	2015 GWP* £m	Percentage of member owned by MA group %
Cathedral Underwriting Limited	2010	191	197	58%
	3010	41	47	100%
Catlin Underwriting Agencies Limited	2003	2,070	1,919	100%
	2088	99	79	0%
	3002	19	27	100%
	6111	142	131	0%
	6112	40	37	100%
	6119	18	17	0%
	6121	26	22	100%
Charles Taylor Managing Agency Limited	1884	76	33	3%
Chaucer Syndicates Limited	1084	781	839	100%
	1176	28	27	57%
	6130	7	0	0%
Endurance at Lloyd's Limited	5151	236	175	100%
ERS Syndicate Management Limited	218	406	394	61%
Faraday Underwriting Limited	435	275	227	100%
Hamilton Underwriting Limited	3334	62	23	100%
Hardy (Underwriting Agencies) Limited	382	286	268	100%
HCC Underwriting Agency Ltd	4141	118	98	100%
Hiscox Syndicates Limited	33	1,057	847	73%
	3624	533	400	100%
	6104	30	33	0%
Liberty Syndicate Management Limited	4472	1,364	1,151	100%
Managing Agency Partners Limited	2791	171	149	20%
	6103	5	5	9%
Markel Syndicate Management Limited	3000	486	429	100%
MS Amlin Underwriting Limited	2001	1,831	1,654	100%
	3210	378	370	100%
Munich Re Underwriting Limited	457	356	436	100%
Navigators Underwriting Agency Limited	1221	340	272	100%
Neon Underwriting Limited	2468	160	210	70%
Newline Underwriting Management Limited	1218	100	96	100%
Novae Syndicates Limited	2007	901	789	100%
	6129	40	0	0%
Pembroke Managing Agency Limited	2014	145	92	0%
	4000	365	242	100%
	6125	12	0	0%
ProSight Specialty Managing Agency Limited	1110	245	212	100%
QBE Underwriting Limited	386	328	335	70%
	2999	1,073	991	100%
R&Q Managing Agency Limited	1991	103	59	30%
Renaissance Re Syndicate Management Limited	1458	335	244	100%
S.A. Meacock & Company Limited	727	60	68	16%
Sirius International Managing Agency Ltd	1945	115	83	100%
Starr Managing Agents Limited	1919	276	264	100%
StarStone Underwriting Management Limited	1301	209	170	89%
	2008	130	68	100%

Managing agent	Managed syndicate(s)	2016 GWP* £m	2015 GWP* £m	Percentage of member owned by MA group %
Talbot Underwriting Ltd	1183	719	667	100%
The Channel Managing Agency Ltd	2015	241	194	100%
Tokio Marine Kiln Syndicates Limited	308	32	28	50%
	510	1,297	1,163	55%
	557	17	17	0%
	1880	230	184	100%
Travelers Syndicate Management Limited	5000	300	287	100%
Vibe Syndicate Management Limited	5678	54	17	100%
W R Berkley Syndicate Management Limited	1967	169	142	100%
All other syndicates, SPA and RITC adjustments		(607)	73	
Total		29,862	26,690	

* See Glossary.

The following syndicates ceased trading at 31 December 2016:
AmTrust Syndicates Limited 779
ACE Underwriting Agencies Limited 1882
AmTrust at Lloyd's Limited 2526
MS Amlin Underwriting Limited 3210
Catlin Underwriting Agencies Limited 6112
Catlin Underwriting Agencies Limited 6119
Catlin Underwriting Agencies Limited 6121

As at 29 March 2017 the following syndicates commenced trading for the 2017 year of account:
Asta Managing Agency Limited 2689
Brit Syndicates Limited 2988
Ark Syndicate Management Limited 3902
Asta Managing Agency Limited 5886

5.7

How Lloyd's Works
Alternative Performance Measures (APMs)

The following metrics, which are consistently used to analyse financial performance in the Lloyd's Market Results and/or in the Society Report, are considered to be Alternative Performance Measures (APMs) as defined in the European Securities and Markets Authority Guidelines (ESMA Guidelines) on Alternative Performance Measures.

Metric	Applicable part of the Annual Report	Definition	Reason for use
Combined ratio	Market Results	Combined ratio is a measure of the profitability of an insurer's underwriting activity. It is the ratio of net operating expenses plus claims incurred net of reinsurance to earned premiums net of reinsurance.	Combined ratio is used to measure the profitability of the underwriting activity across the Lloyd's market. It also serves as a comparator of Lloyd's market underwriting profitability to its peers.
Underwriting result	Market Results	Underwriting result is a measure of the profitability of an insurer's underwriting activity. It is earned premiums net of reinsurance less net operating expenses and claims incurred net of reinsurance.	Underwriting result is used to measure the profitability of the underwriting activity across the Lloyd's market.
Accident year ratio	Market Results	Accident year ratio is a measure of the profitability of the underwriting activity attributable to the current financial year. It is the ratio of net operating expenses plus claims incurred net of reinsurance and prior year releases to earned premium net of reinsurance.	Accident year ratio is used to measure the profitability of the underwriting activity of the Lloyd's market attributable to the current financial year.
Return on capital	Market Results	Return on capital is a measure of overall profitability. It is the ratio of result for the year before tax to the average of opening and closing total capital and reserves.	Return on capital ratio is used to measure the overall profitability and value-creating potential of the Lloyd's market.

Metric	Applicable part of the Annual Report	Definition	Reason for use
Investment return	Market Results and Society Report	Investment return is a measure of performance of an insurer's investing activity. It is the ratio of total investment return to the average of opening and closing financial investments and cash at bank and in hand.	Investment return ratio is used to measure the performance of the portfolio of investments and cash balances held across the Lloyd's market.
Budgeted operating expenses	Society Report	Operating expenses are budgeted on an annual basis as part of a Corporation-wide exercise. These are calculated on an IFRS basis using a bottom up approach, consolidating figures across the different countries and departments within the Corporation.	The annual Budget is a key part of the financial control process within the Corporation and provides an estimate of expected future cost levels.
Free cash balances	Society Report	Free cash represents the amounts, both at bank and on deposit, held in the UK and overseas, excluding any balances held in respect of insurance and arbitration activities.	Provides a measure of the cash resources available to the Corporation to meet operating expenses.
Operating surplus	Society Report	The operating surplus is calculated as income from members (including subscriptions, central fund contributions and the overseas levy), less any operating expenses. It excludes investment returns and related costs.	The operating surplus provides an indication of how the Society's income covers its cost base. This also provides a comparison of whether Central Fund contributions cover the cost of claims arising on the fund.

5.8

How Lloyd's Works
Glossary of terms

Set out below is a guide to insurance and Lloyd's-related terms. These are not precise definitions but are included to provide assistance to readers as to the general meaning of terms commonly used in the Lloyd's market. Formal definitions are set out in the Definitions Byelaw.

Accident year ratio A measure of the profitability of the underwriting activity attributable to the current financial year. The accident year ratio is calculated as net operating expenses and net incurred losses (paid and reserves) for claims occurring in the year as a proportion of net premiums earned during the year. It excludes movements during the calendar year on claims, expenses and premium estimates for previous years.

Active underwriter A person employed by a managing agent with principal authority to accept insurance and reinsurance risks on behalf of the members of a syndicate.

Binding authority An agreement between a Lloyd's managing agent and a coverholder under which the Lloyd's managing agent delegates its authority to enter into a contract or contracts of insurance to be underwritten by the members of a syndicate.

Budgeted operating expenses Operating expenses are budgeted on an annual basis as part of a Corporation-wide exercise. These are calculated on an IFRS basis using a bottom up approach, consolidating figures across the different countries and departments within the Corporation.

Callable layer Central Fund assets may be supplemented by a 'callable layer' of up to 3% of members' overall premium limits in any one calendar year. These funds would be drawn from premium trust funds.

Central assets The net assets of the Society including the Central Fund, but excluding the subordinated debt liability and the callable layer.

Central Fund The fund financed by (among other things) contributions from Lloyd's members and administered by the Council primarily as a fund for the protection of policyholders, and includes both the 'Old' Central Fund and the New Central Fund.

Central SCR The Lloyd's Central Solvency Capital Ratio is calculated to cover all of the risks facing the Society and the Central Fund at a 99.5% confidence level over a one year time horizon.

Combined ratio A measure of an insurer's underwriting profitability based on the ratio of net incurred claims plus net operating expenses to net earned premiums. A combined ratio of 100% is break even (before taking into account investment returns). A ratio less than 100% is an underwriting profit.

Corporate member A company incorporated with limited liability, a Scottish limited partnership or a limited liability partnership, admitted to membership of the Society.

Council Created by Lloyd's Act 1982, the Council has the management and superintendence of the affairs of the Society and the power to regulate and direct the business of insurance at Lloyd's.

Coverholder A firm either in the UK or overseas that is authorised by a managing agent under the terms of a binding authority to enter into contracts of insurance to be underwritten by members of a syndicate managed by the managing agent. A Lloyd's broker may act as a coverholder.

Economic Capital Assessment The level of capital required to meet Lloyd's financial strength, license and rating objectives.

Financial Conduct Authority (FCA) The FCA supervises the conduct of the UK financial services industry. Lloyd's, managing agents, members' agents and Lloyd's brokers are regulated by the FCA.

Franchise Board The board established by the Council with responsibility for creating and maintaining a commercial environment at Lloyd's in which the long-term return to all capital providers is maximised. This includes setting the Risk Management Framework and profitability targets for the market.

Free cash balances Free cash represents the amounts, both at bank and on deposit, held in the UK and overseas, excluding any balances held in respect of insurance and arbitration activities.

Funds at Lloyd's (FAL) Capital lodged and held in trust at Lloyd's as security for the policyholders and to support a member's overall underwriting business.

Integrated Lloyd's Vehicle (ILV) An arrangement in which a syndicate's capital is wholly provided by corporate members that are under the same ownership and control as the syndicate's managing agent.

Investment return Investment return is a measure of performance of an insurer's investing activity. It is the ratio of total investment return to the average financial investments and cash at bank and in hand.

Managing agent An underwriting agent responsible for managing a syndicate, or multiple syndicates.

Market wide SCR The Market Wide Central Solvency Capital Ratio is calculated to cover all of the risks arising on the syndicate activity, members' capital provided at Lloyd's and the Society taken together at a 99.5% confidence level over a one year time horizon.

Member (of the Society) A person admitted to the membership of the Society.

Name A member of the Society who is an individual and who trades on an unlimited basis.

New Central Fund The New Central Fund constituted by and governed by the New Central Fund Byelaw (No. 23 of 1996).

Non-technical account Under UK GAAP the profit and loss account must be divided between the technical account and the non-technical account. Reported in the latter is all investment return, although an element will be reanalysed to the technical account, and any income and expenses that do not arise directly from the entity's underwriting activity.

Operating surplus The operating surplus is calculated as income from members (including subscriptions, central fund contributions and the overseas levy), less any operating expenses. It excludes investment returns and related costs.

Premiums trust funds (PTF) The premiums and other monies that members receive in respect of their underwriting at Lloyd's are held by their managing agents in trust for them subject to the discharge of their underwriting liabilities.

The premiums trust funds comprise a sterling fund, Lloyd's American Trust Fund, Lloyd's Dollar Trust Funds, Lloyd's Canadian Trust Fund and the Lloyd's Asia trust funds (which cover general business written through coverholders in Singapore). These premiums trust funds are available to fund overseas regulatory deposits, claims, return premiums, underwriting expenses and any profit that is payable to the member after providing for all future liabilities.

Prior years' reserve movements This is calculated as movements in reserves established for claims that occurred in previous accident years.

Prudential Regulatory Authority (PRA) The PRA is responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms. Lloyd's and managing agents are regulated by the PRA.

Realistic Disaster Scenarios (RDS) A series of scenarios, both natural and man-made, which are used to assess the market's risk profile to a variety of different catastrophes to enable better risk management practices within Lloyd's.

Reinsurance to close (RITC) A reinsurance agreement under which members of a syndicate for a year of account to be closed are reinsured by members who comprise that or another syndicate for a later year of account against all liabilities arising out of insurance business written by the reinsured syndicate.

Reinsurance to close (RITC) syndicate A syndicate set up solely to underwrite the Reinsurance to Close of other syndicates.

Return on capital Return on capital is a measure of overall profitability. It is the ratio of result for the year before tax to the average of opening and closing total capital and reserves.

Service company An approved coverholder which Lloyd's has agreed can be classified as a 'service company' by reason of it being a wholly owned subsidiary of either a managing agent or of a managing agent's holding company and which is normally only authorised to enter into contracts of insurance for members of its associated syndicate and/or associated insurance companies.

Solvency ratio The measure of an insurer's solvency based on the ratio by which the net assets for solvency purposes exceed the solvency requirement.

Special Purpose Arrangement (SPA) A syndicate set up solely to underwrite a quota share reinsurance of another syndicate's business for a year of account.

Spread syndicate A syndicate whose capital is provided by a number of different members, including those that have separate ownership and control, to the syndicate's managing agent.

5.8

How Lloyd's Works
Glossary of terms

Spread vehicle A corporate member underwriting on a number of different syndicates.

Syndicate A member, or group of members, underwriting insurance business at Lloyd's through the agency of a managing agent.

Syndicate allocated capacity In relation to a syndicate the aggregate of the member's syndicated premium limits of all the members for the time being of the syndicate.

Technical account Under UK GAAP the profit and loss account must be divided between the technical account and the non-technical account. The technical account reports the results of the underwriting activity, premiums less claims, less expenses and also includes an element of the investment return reanalysed from the non-technical account.

Traditional syndicate A syndicate whose members underwrite insurance business at Lloyd's for the current year of account and which is neither an SPA syndicate nor an RITC syndicate.

Underwriting result Underwriting result is a measure of the profitability of an insurer's underwriting activity. It is earned premiums net of reinsurance less net operating expenses and claims incurred net of reinsurance.

Year of account The year to which a risk is allocated and to which all premiums and claims in respect of that risk are attributed. The year of account of a risk is usually determined by the calendar year in which the risk incepts. A year of account is normally closed by reinsurance to close at the end of 36 months.