Market Bulletin

LLOYD'S

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FROM:	Director, Worldwide Markets (WWM)
LOCATION:	86/G12
EXTENSION:	5998
DATE:	26 November 2002
REFERENCE:	Y2920
SUBJECT:	GLOBAL (OR MULTINATIONAL) POLICIES
SUBJECT AREA(S):	1. To ensure compliance with Lloyd's international reporting and taxation obligations, more rigorous checks on policies at Xchanging Ins-Sure Services are necessary. 2. Background information and guidance on the identification of individual national exposures within 'multinational' or 'global' policies.
ATTACHMENTS:	1. List of countries where Lloyd's has reporting obligations. 2. Guidance on identifying the country of risk. 3. Background information / Common problems / FAQs.
ACTION POINTS:	**Underwriters and Brokers to action**
DEADLINE:	**Immediately**

Purpose and Scope

This Bulletin is to advise the market of the introduction of new policy checks at Xchanging Ins-sure Services to ensure compliance at market level with Lloyd's overseas regulatory and tax reporting obligations. These checks affect 'global' or 'multinational' policies, i.e. policies having exposure in more than one territory. Although these sorts of policies are typically written in the open market, the issues highlighted in this Bulletin apply equally to policies insured under full or limited binding authorities.

WWM and Lloyd's Taxation Department are instructing Xchanging Ins-sure Services and Xchanging Claims Services to apply a more consistent approach to the checking of global policies as they are presented for signing. The revised procedures will not apply to marine or aviation hulls and associated interest risks (apart from checking that any taxes due are correctly shown), but will apply to risks of a 'non-marine' nature that are written in those markets.

Summary of revised checking procedures

The information provided to Xchanging Ins-sure Services needs to define the nature of the insurance relationship and identify the country or countries of risk in a clear and unambiguous way. Therefore, the following will be queried, and rejected if the query is not resolved within 48 hours:-

- Any references to non-country specific exposures - for example 'Worldwide' or 'Non-UK' or 'Rest of the world' or 'other'.

- Slips which state that only a proportion of the premium is taxable, without justification for the remainder.
- Slips which are allocated a US regulated classification for 100% of the premium where there is non-US exposure (or even no US exposure at all), suggesting regulatory and tax issues may arise in non-US territories. (See Annexe 3, section 4)
- Slips which are not clear as to whether the underwriter is offering coverage on a direct or reinsurance basis and (in the case of reinsurance) do not identify the cedant or cedant's nationality
- Slips which make reference to multi-national exposures, but which do not include a premium breakdown or correctly identify the taxes applicable (either as to fact or amount)

Implementation Date
These new checks will apply strictly to all business (a) in the 2003 underwriting year of account; and to (b) all other business, where reasonably possible. Xchanging Ins-sure Services will for the time being continue to refer pre-2003 inception business to WWM and Taxation for guidance.

Further information
Annexes to this Bulletin provide further information on the need for these changes, a list of the countries involved and also, at annexe 3, guidance and discussion of common problems and frequently asked questions.

A revised and updated presentation explaining the context and issues is available to individual syndicates and brokers in their own offices at no charge. It can be arranged through Zoë Kilminster at WWM on Lloyd's extension 5772, or zoe.kilminster@lloyds.com

Guidance on a case-by-case basis is available from Lloyd's Worldwide Markets and Lloyd's Taxation Dept. **These two departments are the exclusive source of information on licensing and taxation respectively within Lloyd's.**

The manager responsible for Global Policy issues within WWM is Andrew Smith who can be contacted on Lloyd's extension 5349, or at Andrew.d.smith@lloyds.com. WWM's country-specific procedures manuals can be found at www.lloyds.com under the section for 'Lloyd's Worldwide'. Additionally, the Market Services Desk at box 190b, on Lloyd's extension 6677, (or at market.services@lloyds.com) is available to answer queries or issue a password for accessing the web-based information.

Lloyd's Taxation's web-site can be found at www.lloydstaxation.com. Any queries relating to taxation and the Central Taxes System should be addressed to Roger Ramage or Maureen McLeod on Lloyd's extensions 6852 and 6860 respectively or Roger.e.ramage@lloyds.com and Maureen.c.mcleod@lloyds.com

The information on both websites is updated regularly. Hard copy manuals which may still be in circulation are no longer valid and should be disregarded.

Any queries relating specifically to changes to Xchanging Ins-sure Services procedures should be addressed to Enquire on 01634 39 2999 or ins-sure.enquire@ins-sure.com.

Julian James
Director
Worldwide Markets

ANNEXE 1

LIST OF 'LICENSED' COUNTRIES REPORTING REQUIREMENTS EXIST IN THOSE COUNTRIES SHOWN IN CAPTIAL LETTERS

ANGUILLA
ANTIGUA
ARGENTINA[+]
AUSTRALIA
AUSTRIA
BAHAMAS
BARBADOS
BELGIUM
BELIZE
BERMUDA
BRITISH VIRGIN ISLANDS
CANADA
CAYMAN ISLANDS
CHILE[+]
COLOMBIA[+]
CYPRUS
DENMARK
DOMINICA
Ecuador[+]
FINLAND
FRANCE (AND TERRITORIES)[✷]
Gambia[#]
GERMANY
Gibraltar
GREECE
GRENADA
GUERNSEY
HONG KONG
ICELAND
IRELAND
ISLE OF MAN
ISRAEL
ITALY
JAMAICA
JAPAN[✞]
JERSEY
Labuan[+]
LIECHTENSTEIN
LUXEMBOURG
Malawi
MALTA
MAURITIUS
MEXICO[+]
MONACO
NAMIBIA
NETHERLANDS
NEW ZEALAND
NORWAY
PAPUA NEW GUINEA
PORTUGAL
SINGAPORE
SOUTH AFRICA
SPAIN
ST. KITTS & NEVIS
ST. LUCIA
ST. VINCENT
SWEDEN
SWITZERLAND
TRINIDAD AND TOBAGO
UNITED KINGDOM
US VIRGIN ISLANDS
USA – ILLINOIS
USA – KENTUCKY
USA – OTHER STATES[⇳]
Vanuatu
Venezuela[+]
ZIMBABWE

[+] Lloyd's is specifically registered or licensed to write reinsurance business only.
[✷] France and its overseas departments, territories and territorial collectives.
[#] Licensed for motor business only.
[✞] Through lloyd's japan inc. Only.
[⇳] Lloyd's is an eligible surplus lines insurer in all states except kentucky and the us virgin islands. It is also an accredited reinsurer in all states.

ANNEXE 2

IDENTIFYING THE COUNTRY OF RISK

It is important to stress that the regulatory and tax rules applying to a global policy are complex. The applicable rules may well follow the country of risk and are unlikely simply to be where the insured pays the premium from, or where the insured's head office is located. In such circumstances it will be incorrect to code the whole slip exclusively to one country when in fact there is multi-territorial exposure. Syndicates writing multinational business including US locations must consider the extent to which US classification rules will apply. Regulatory Bulletin 015/2002 of 26th April 2002 provides guidance on this issue

Where a slip states that the definition of the insured includes any subsidiary, affiliate, associated company, branch, representative office, agency or other similar presence, then these entities are multiple insureds under the slip. Care should be taken to ensure that premium is allocated to each country where there is an insured entity.

Once the country or state of risk has been identified, the gross premium allocated to the country in question may be subject to local taxes and/or parafiscal charges, which also need to be shown on the slip. This needs to be done for 100% of the slip premium. Specific country-by-country web-based information is available, maintained by Lloyd's Taxation Dept.

Annexe 1 to this bulletin lists countries for which 'global' premium needs to be split.

The following general guidance may assist the market in deciding the country (or countries) of risk. Specific country-by-country web-based information is available, maintained by WWM.

European Risks

The EU 2nd non-life Directive lays down rules for locating a risk in an EU member state. The 15 EU member states are Austria, Belgium, Denmark, Italy, Finland, France, Germany, Greece, the Republic of Ireland, Luxembourg, the Netherlands, Portugal, Spain, Sweden and the UK. Certain EU rules have been extended to non-EU members who are members of the EEA (European Economic Area). The EEA comprises the EU countries, plus Iceland, Norway and Liechtenstein.

1. **Property risks –** the general rule is that the country of risk will be the country where the insured property is physically located. In a few countries (for example Switzerland), it may be necessary to resolve an apparent conflict between this principle and other local rules. Further guidance can be provided by WWM.

2. **Vehicles of any type** (this includes Marine and Aviation hulls) **–** the country of risk will be the country where the vehicle is registered.

3. **PA and short period travel risks –** the country of risk will be the country where the buyer of insurance takes out the policy (this is likely to be the country where the buyer is normally resident).

4. **Other categories of insurance** (This includes liability and pecuniary loss risks) – the country of risk will be the country where the insured's business is established. This is particularly relevant to professional risks. Furthermore, in the context of Contract Frustration, where the insured entity is located in one country, but the event which may trigger a claim under the policy may happen in another, the country of risk is the country where the insured entity has its 'establishment'. For example where a UK bank buys insurance to protect against contract frustration overseas, it is the UK bank which will receive the indemnity and the risk is thus a UK risk (even though a claim may result from an event overseas).

U.S. Risks

Some U.S. jurisdictions have developed detailed rules on the subject of identifying the "jurisdiction of risk" and, while similar, these rules are not completely uniform from one U.S. jurisdiction to another. Generally, the rules followed by most U.S. jurisdictions will be similar to the rules described above for European risks, but there are some differences. For example:

Vehicles - In the USA, vehicles are usually allocated to the jurisdiction where they are principally garaged, not the jurisdiction where they are registered.

Other categories (cf. EU category 4) – Some US States may allocate a risk based on where services are being performed, rather than where the insured is established.

Reinsurance

Where reinsureds are located in more than one country their locations must be identified on the closing documentation. Xchanging Ins-sure Services will use this information in order to ensure that the necessary data is captured to enable Lloyd's to meet its international regulatory reporting requirements.

ANNEXE 3

BACKGROUND INFORMATION, COMMON PROBLEMS and FREQUENTLY ASKED QUESTIONS

1 Background Information

A condition of an insurer's licence to trade is a requirement to make regular financial returns to the supervisory authorities. The Lloyd's market is no exception to this principle and must make the necessary regulatory returns to a variety of official bodies around the world. This information, comprising premiums, claims and trust fund information, is crucial in maintaining Lloyd's position as a unique trading platform, licensed in over 60 territories.

The obligations to make regulatory filings and returns to overseas authorities are compliance obligations. The information needed to fulfil these obligations is taken from the documentation as it passes through the closing process, overseen by Xchanging Ins-sure Services or Xchanging Claims Services. Where reporting requirements exist, documents must include an agreed allocation of gross premium, and/or paid and outstanding claims for countries to which they apply. For regulatory purposes only, separate LPANs and LCCFs may be required. It is normally necessary to identify the premium or claim at a minimum of individual country level for each country where Lloyd's makes a regulatory return. In some countries, most notably in the USA, Canada and Australia, a more detailed level of information is required, ie at state or provincial level.

1.1 Who imposes these rules? Is it Lloyd's?

Regulatory and tax rules are imposed externally by governments. They are not Lloyd's rules. Funding, tax and reporting rules of the nature described in this bulletin affect all insurers, and not just Lloyd's underwriters. Lloyd's centrally has an important role to play in explaining and applying the relevant rules to the Lloyd's market.

2 Roles and Responsibilities

Underwriters are reminded that it is their responsibility to apportion the premium and taxes, where due, in respect of each country of risk. Bulletin Y2255 highlighted the possibility of Lloyd's regulatory sanctions in the case of non-compliance.

Market Bulletins Y2255 (dated 9th March 2000) and Y2594 (dated 8th August 2001) dealt with international licence and tax issues respectively. Additionally, Regulatory Bulletin 015/2002 highlighted compliance issues relating to US classification issues. Market Bulletin Y803 dated 28th January 1998 also provided guidance on the applicable procedures.

Lloyd's Market Supervision includes overseas licensing issues in their syndicate review programme, and may ask Underwriters to explain and justify their underwriting decisions in the context of international regulatory environment.

The international obligations take little or no account of the traditional roles of the broker and underwriter in the Lloyd's marketplace. Clearly, the underwriter's stamp or initial on a slip confirms satisfaction with, and acceptance of, the slip content, whether the underwriter is employed by a representative of an insurer, syndicate or other capital provider. However, in the London market, and particularly at Lloyd's, slips are drafted by the broker, to whom the slip is returned by Xchanging should queries arise.

Therefore, the broker has a key role in providing a variety of information which will assist the underwriter in meeting compliance obligations. This includes:-

- Obtaining details from the client sufficient to identify risk exposures
- Clearly showing tax details on slips in the correct format
- Providing sufficient information to leader for tax assessment

3 Consequences of non-compliant slips

3.1 Effect on Payment Warranties

Failure to include the required level of information on a slip will inevitably delay signing and may result in rejection. Cashflow to underwriters will be adversely affected.

Underwriters are reminded that premium payment warranties are not permitted in some jurisdictions (including certain states in the USA), and in others, their effect may be muted by local laws which allow different timescales for payment.

In some other cases, the delay in signing a non-compliant slip will mean that the eventual premium payment would prima facie be in breach of a PPW deadline. Underwriters should be aware that in these cases it is their own omission of key information from the slip which has caused the delay, with no fault attaching to the part of the insured client. In such circumstances, it is doubtful that an attempt to enforce a warranty by underwriters could be successful.

3.2 Regulatory and other sanctions

Lloyd's centrally monitors the compliance performance of the market with regard to international licensing and tax obligations. In order to protect the Society's licenses, it may be necessary for WWM or Lloyd's Taxation to involve Market Supervision and/or Investigations Dept where it becomes clear that Managing Agents do not have the necessary controls in place to discharge their compliance obligations.

In addition to the possibility of these Lloyd's regulatory sanctions, underwriters may become liable to pay fines, back taxes and interest to overseas regulators and tax authorities.

4 Parent and subsidiary companies

Slips typically define the insured to include subsidiary, associated, affiliated and other entities on a 'sui generis' basis. These terms have generally been litigated in a variety of jurisdictions and indicate the slip is covering multiple insureds. Each subsidiary is likely to be a separately identifiable legal entity in its own right, established in its own country, and have its own contractual relationship with underwriters. The majority of enquiries referred to WWM by Xchanging are cases where Underwriters have been presented with risks with this sort of very wide/loose description of the insured.

This issue has been the subject of market association guidance to its membership. The (then) NMA Information and Agreements Book first contained the "X Co" circular in 1964. *"The X Co Ltd and Subsidiary and/or Associated and/or Affiliated Companies"* circular advised against use of the term "subsidiary, affiliate or associate companies" in the description of the Assured without limitation. The advice was reissued after the conclusion of the Maxwell case litigation in 1996 and remains valid today.

4.1 US parent / other subsidiaries / US Surplus Lines Brokers and exemptions / Separate Policies

4.1.1 Is the policy a 'Surplus Lines' policy?

The key driver to determining this matter is to identify where the insurance transaction has taken place. For example it is important to consider whether or not a local broker in the US is involved in securing the insurance contract with underwriters. (Remember though that the transaction may be deemed to have a US 'situs' even if no US broker is involved, as would be the case where a US insured acting in the US, communicated directly with a Lloyd's Broker in London.)

Unless the business is placed at Lloyd's

(a) in accordance with the terms of Lloyd's licences in Illinois, Kentucky, or the US Virgin Islands; or

(b) with a US classification of 'reinsurance' because underwriters are reinsuring a US-domiciled cedant; or

(c) In such a way where the entire transaction takes place outside the State(s) where the insured risk is located; or

(d) Is written pursuant to some recognised exemption other than the excess/surplus lines law (e.g. industrial insured exemptions),

risks placed from the USA into Lloyd's will generally have a US 'Surplus Lines' classification.

4.1.2 Need for a 'Surplus Lines' Broker

Underwriters are reminded that Surplus Lines business can only be placed via the intermediary of a registered Surplus Lines Broker licensed by the State where the transaction takes place, triggering the State's 'doing business' laws.

4.1.3 'Surplus Lines' funding applies to non-US exposures at policy level

For global policies allocated a 'Surplus Lines' classification, it is important to note that *all liabilities under the policy, including those attributable to risk exposures outside the USA*, are subject to Surplus Lines Trust Fund obligations. This is because US Trust Fund rules operate at policy level. Prima Facie therefore it falls to underwriters to ensure that funding for such business is at Policy level.

4.1.4 Possibility of separate policies for non-US exposures

If a global programme with both US and non-US risk exposures is written as two separate policies – one for the US risk exposures and one for the non US risk-exposures, the US classification (and the US Surplus Lines liabilities funding obligation) would apply only to the policy covering the US risk exposures. The commercial practicality of splitting policies in this way is something for Managing Agents, Underwriters and Brokers to determine for themselves.

It can therefore be seen that Managing Agents and Underwriters may derive some benefit from issuing separate policies. However, individual layers which form part of an overall global programme, or slips which contain wording suggesting that underwriters intend separate policies to be issued, will not constitute a separate policy if the client ultimately only receives a single contract document. A 'separate policy' is a discrete insurance contract with its own specific documentation and premium.

The practice of issuing a single policy to a US parent may, in effect, to result in unnecessary overfunding by syndicates of trust funds. Such a practice may additionally lead to the neglect of reporting and tax obligations in non-US countries.

4.1.5 Exemptions from Surplus Lines rules

Underwriters will wish to consider whether or not the risk qualifies for exemption from the Surplus Lines rules. Exemptions may be available for large and sophisticated buyers of commercial insurance (sometimes called “industrial insureds”). Exemptions may also be available for certain kinds of coverage (e.g. marine, aviation and transportation insurance). It should be noted that the excess/surplus lines rules potentially apply only if some part of the insurance transaction takes place in the State. Rules on exemption vary from State to State. Information on State exemption rules can be obtained from WWM.

4.1.6 Surplus Lines Taxes

The insured will be subject to Surplus Lines Tax(es) in those cases placed pursuant to the Surplus Lines law; or, if exempt, the insured may subject to Direct Procurement Tax(es). Although these taxes are handled and payable locally in the USA, underwriters may find themselves having to fund these taxes should the insured default. Premium still needs to be apportioned for the purposes of premium reporting in the USA and for tax purposes in other countries, and the applicable rate of tax identified and the amount of tax calculated.

The method used to apportion premium amongst jurisdictions needs to be just and reasonable. On this basis, it is accepted by most US State tax authorities that, if it can be shown that tax has been paid in one country, it should not be paid on the same exposure in the US. States may object to a method of apportionment which is designed to maximise premium allocation to jurisdictions with low tax rates where such allocation bears little resemblance to the the actual ‘situs’ of the risk(s).

4.1.7. Slips requiring a US Classification.

Underwriters are reminded that they are responsible for ensuring that are assigned the correct US Classification, where

- a) The premium is expressed in US Dollars; and
- b) The insurance covers US-regulated risks, but the premium is not expressed in US Dollars

4.2 EU Parent / non-EU (including US) subsidiaries / no need for a US Surplus Lines Broker

A US subsidiary of a non-US parent will not qualify as a US risk if the insurance transaction takes place outside the USA. Thus underwriters do not have Surplus Lines Trust Fund obligations where cover is purchased on behalf of a US subsidiary by its non-US-based parent.

If a subsidiary is located in Kentucky, Illinois or the USVI, then the policy wording will have to conform to the rules required by those States. If the risk has not been placed from within the USA, it is not a Surplus Lines risk.

4.3 EU premium tax exposure

However, in the EU context, it makes no difference which part of the insured multinational pays the premium, nor whether the subsidiary instructs insurance to be arranged on its behalf, or even is aware that this occurs. Premium in respect of a risk in an EU country is subject to tax by the fiscal authorities in the country of risk.

5 Direct vs. Reinsurance / slip references to 'local policies'

Many 'multinational' slips include a condition to the effect that 'underwriters agree to sign as a reinsurance if necessary' or 'agree local policies may be issued'. Whilst it may be deduced that underwriters' intention in such cases is only to write on a direct basis where Lloyd's is licensed, and to offer reinsurance of local companies in other countries, this intention is not often given effective force on the slip. The result of this is that it is impossible to tell which part of the contract is direct, and which is reinsurance, which may lead to ambiguity on the drafting of policy documentation evidencing the contract.

Reinsurance and Direct Insurance are normally subject to very different regulatory and tax régimes. It is preferable to have separate sections on the slip (or even two slips), which clearly identify the countries and premiums resulting from a reinsurance and direct relationship respectively. This Bulletin and annexes deal elsewhere with direct insurance. Underwriters are also reminded that reinsurance which is exported cross border may be subject to local regulatory requirements, for example compulsory cessions, premium and claims reserves, local collateralisation requirements and taxes.

It is quite common for Lloyd's underwriters to reinsure a UK cedant on a retrocession basis, the cedant reinsuring locally licensed members of its parent group who in turn issue local policy documents. This route into Lloyd's will avoid the regulatory or tax issues which may be present elsewhere.

6 DIC/DIL coverage

Frequently underwriters provide 'global' clients with coverage for 'Difference in Conditions' or 'Difference in Limits'. The objective of this coverage is to ensure that the same policy coverage, both in terms of insured perils and sums insured, applies to all locations, irrespective of local regulatory rules which may restrict the width or financial limit(s) of cover. Underwriters are reminded that, prima facie, there is a direct insurance relationship in respect of these insured entities requiring regulatory premium and tax recording and reporting.

However, it may be preferable for underwriters to think in terms of expressing this sort of coverage in terms of a financial product. The insured would simply be the parent or holding company alone, who is protecting itself against the possibility of fulfilling a guarantee in favour of one of its group members. Further information and guidance on this is available from Lloyd's WWM and Taxation Depts.

7 Layered placements

Each layer needs to have attention paid to its own regulatory and tax exposures. Sometimes, slips indicate an intention to deal with the apportionment of regulatory and tax matters for the whole multi-layered placement on a single layer (often the primary layer). This practice is not compliant with Lloyd's international obligations – either for regulatory or tax purposes. The slip for a single layer may be the only layer of the programme involving Lloyd's underwriters. Additionally, an individual slip may be selected for audit in isolation of the wider programme of which it is a part.

It is therefore essential that the information on each layer properly reflects the necessary regulatory and tax information.

8 Stand-alone terrorism cover for warehouse risks

By marine market custom and practice, and as accepted by some regulators and tax authorities, warehouse risks are often included as incidental in cargo placements where the stay risk exposure in any one warehouse is less than 60 days in duration. For example, UK Customs and Excise allow a dispensation from UK IPT for the 'stay' risk on this basis. However, this '60 day rule' is dependent upon the 'stay' risk being both incidental to transit coverage, and in the same policy.

Underwriters are reminded that stand-alone cover for the stay/warehouse risk only amounts to property coverage in respect of the contents of buildings. It is not covered by the normal '60 day dispensation' because the coverage is in a separate policy which has no transit exposure. A territorial split of premium is therefore necessary for this sort of risk.

9 "Sign now and split later"

Lloyd's WWM and Taxation often have to intervene in cases where the market wants to sign premium through without the necessary regulatory and tax splits being complete. As a rule this practice is not acceptable. This is for a variety of reasons, including the length of time during which it takes some outstanding issues to be resolved when flexibility has been permitted – in some cases this has run into years. Significantly, the signing number and date creates a tax point.

10 Guidance on Taxes

Underwriters are reminded that the responsibility for identifying and apportioning premium taxes is theirs, at the time of writing the business. The first stage in the process is to locate the risk in the right country, and the second stage will be to consider the tax(es) which may be applicable.

10.1 Method of apportionment

Underwriters must use a 'just and reasonable' method to apportion premium between countries and states. The method may reflect the underwriter's view on exposed values, perceived physical hazard, claims history, litigation system and court awards.

10.2 Slip Notation Best Practice

Undewriters' responsibility will not be discharged by the following recently seen examples of slip notation:

- "Taxes to be split as determined by broker"
- "Xchanging to sign premium immediately without tax but to await tax details in due course"
- "Taxes as per the NMA" (the NMA does not exist any longer, nor does its tax book)
- "Taxes as Applicable"
- "Underwriters agree/instruct the LPSO that policy is not subject to tax" - when it plainly is.