



FROM: The Secretary to the Disciplinary Board  
LOCATION: 58/NW1  
EXTENSION: 5530  
DATE: 13 November 1998  
REFERENCE: 109/98  
SUBJECT: LLOYD'S DISCIPLINARY PROCEEDINGS -  
CASE NO. LDB9712/40  
(CUTHBERT HEATH UNDERWRITING LTD)

ATTACHMENTS: None  
ACTION POINTS: For information  
DEADLINE: None

On 9 November 1998 a Lloyd's Disciplinary Tribunal found the former managing agent of Syndicate 404, Cuthbert Heath Underwriting Ltd ("CHUL"), guilty of 12 separate breaches of Lloyd's Syndicate Accounting Byelaw (No. 11 of 1987) ("MB 1987") and ordered that the following penalties should be imposed on the company:

1. The revocation permanently, of CHUL's right to act as a managing agent at Lloyd's in any capacity whatsoever;
2. An aggregate fine of \$125,000.

In addition, CHUL was ordered to pay \$90,000 in costs to the Council of Lloyd's ("the Council").

The charges

CHUL was charged by the Council with breaching the provisions of paragraph 6(b)(vi) and paragraph 1.9(a) of Schedule 4 of SAB 1987 in relation to the preparation of each of the 1987 to 1990 annual reports of Syndicate 404, by failing to disclose adequately or at all in each such report, inter alia, the following information:

- (i) The fact that no provision had been made in the reserves of the closing year of

account for so-called "potential" asbestos, pollution and loss of hearing ("APLH") claims beyond an amount for defending such claims and the fact that reliance was being placed by CHUL on the "unused" cover (i.e. cover which was not formally earmarked in the accounts) that was available under Syndicate 404's time and distance ("T&D") policies to meet such claims should they become payable. The existence and amount of the "unused" cover that was relied upon for this purpose was not disclosed.

- (ii) The fact that no specific provision had been made in the reserves of the closing year of account for APLH and other exceptional claims which had been incurred but not yet reported ("IBNR") to Syndicate 404 and the fact that reliance was being placed by CHUL on the "unused" cover that was available under Syndicate 404's T&D policies to meet such claims should they become payable. The existence and amount of the "unused" cover that was relied upon for this purpose was not disclosed.
- (iii) Information about a run-off protection policy which Syndicate 404 had purchased from GTE Reinsurance Company ("the GTE policy") which was sufficient to explain its nature and effect on the underwriting accounts of Syndicate 404;
- (iv) Information about Syndicate 404's T&D policies which was sufficient to explain their individual nature and effect on the underwriting accounts of Syndicate 404.

It was alleged by the Council that as result of the non-disclosure of the facts and matters referred to in paragraphs (i)-(iv) above:-

- (a) The true liabilities and assets of the closing year of account were understated in each of Syndicate 404's 1987 to 1990 annual reports;
- (b) The increase in Syndicate 404's notified outstanding and IBNR losses before the deduction of anticipated recoveries under the GTE policy and Syndicate 404's T&D policies on the previous year was understated in each of Syndicate 404's 1987 to 1990 annual reports;
- (c) The (increasing) dependence of Syndicate 404 on T&D cover as a means of providing for notified outstanding and IBNR losses was understated in each of Syndicate 404's 1987 to 1990 annual reports;
- (d) It was not possible for the reader of each of Syndicate 404's 1987 to 1990 annual reports to assess the true net benefit taken by the closing year of account in respect of the GTE policy and Syndicate 404's T&D policies;
- (e) The underwriting result of the closing year of account disclosed in the notes to the accounts appeared better than was the case before the deduction of anticipated recoveries due under the GTE policy and Syndicate 404's T&D policies.
- (f) The reader of each of Syndicate 404's 1987 to 1990 annual reports was not alerted to the true uncertainty surrounding Syndicate 404's ultimate liabilities in respect of APLH claims and the CHUL's approach to such uncertainty.

CHUL was separately accused by the Council of breaching the provisions of paragraph 2 of SAB 1987 by failing to keep and preserve accounting records of Syndicate 404's APLH IBNR loss reserve requirements as at 31 December 1987, 1988, 1989 and 1990. CHUL was charged with failing to create such records or, alternatively, if such records were created, with failing to preserve the same.

The settlement of the proceedings

Having unsuccessfully sought to have the disciplinary proceedings stayed as an abuse of process, CHUL reached an agreement with the Council for the termination of the disciplinary proceedings. The terms of this agreement were subsequently approved by the Disciplinary Tribunal in its decision of 9 November 1998. This decision will take effect on 24 November 1998.

Pursuant to the agreement reached between the parties CHUL did not serve a defence to the charges of misconduct. As a result, under Lloyd's Disciplinary Rules, the company was deemed to have admitted the allegations of misconduct which were made against it. The Disciplinary Tribunal issued a decision accordingly save that (by agreement) no findings of misconduct were entered against CHUL in respect of the charges of failing to create accounting records; instead findings of misconduct were entered in respect of the alternative charges of failing to preserve such records. CHUL agreed to accept the penalties and order of costs referred to above and the decision of the Disciplinary Tribunal gives effect to this agreement.

CHUL was charged and found guilty of misconduct as aforesaid notwithstanding the unqualified auditor's opinions contained in each of Syndicate 404's 1987 to 1990 annual reports.

The above summary is based on the decision of the Disciplinary Tribunal, copies of which are available on request from the Secretariat to Lloyd's Disciplinary Committees on extension 6989 or 5530.

This bulletin is being sent to all underwriting agents, Lloyd's advisers, Lloyd's brokers, corporate members, market associations, the ALM and recognised accountants.

A. P. Barber  
Secretary to the Lloyd's Disciplinary Board