

MARKET BULLETIN

REF: Y4563

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| Title | Transfer of interests in Lloyd's corporate members |
| Purpose | To publish a <i>Code of Practice for Members' Agents</i> and a Guidance Note in relation to the transfer of interests in Lloyd's corporate members |
| Type | Event |
| From | Chairman of the Capacity Transfer Panel |
| Date | 14 February 2012 |
| Deadline | The implementation date for the Code of Practice will be 20 February 2012 |
| Related links | None |

Background

Greater interest is now being given to acquiring interests in corporate members as a way of acquiring underwriting capacity outside of the capacity auctions. The Capacity Transfer Panel (the "Panel") has recently been considering how Lloyd's may best facilitate the transfer of interests in Lloyd's corporate members (this includes the transfer of shares in a corporate member which is a company, partnership shares in respect of a corporate member which is a SLP and members' shares in respect of a corporate member which is a LLP).

One of the primary reasons behind the Panel's review of this area is that Lloyd's has a regulatory and reputational interest to ensure that:

- where members' agents are involved in the transfer of interests in corporate members they act in the best interests of their client and protect the reputation and standing of the Lloyd's market as a whole; and
- where members' agents are not involved, those seeking to acquire or dispose of interests in corporate members understand the issues that this may raise and how they may obtain expert advice from members' agents and from other professionals.

Panel's Conclusions

The Panel has concluded that Lloyd's should (a) promulgate a Code of Practice for members' agents which sets out clear principles for dealing with the transfer of interests in corporate members and (b) publish a Guidance note (which will be available on lloyds.com) for individuals seeking to buy or dispose of interests in corporate members who may not have instructed members' agents and, as a consequence, may not fully appreciate all of the issues involved. In the Guidance note Lloyd's strongly recommends that such individuals do engage a members' agent or another suitably qualified professional adviser before proceeding in acquiring or disposing of an interest in a Lloyd's corporate member.

The Panel believe that these proposals are an effective way of protecting Lloyd's regulatory and reputational interests but in a way which least affects existing property rights and avoids the introduction of complex rules or central processes

The Lloyd's Legal Department has consulted with relevant Lloyd's market stakeholders on the content of the Code of Practice and the Guidance note and the final versions of both documents accompany this Market Bulletin. The implementation date for the Code of Practice will be 20 February 2012 and the Guidance note will be added to lloyds.com on the same day.

Lloyd's will review the operation of the Code of Practice after it has been implemented for twelve months.

Contact

Any questions with regard to this Market Bulletin should be addressed to Paul Thornton (telephone: 020 7327 6281, e-mail: paul.thornton@lloyds.com).

**Code of Practice for
Members' Agents:
Transfer of Interests in
Lloyd's Corporate Members**

Words and terms shown in italics have the meaning given in the Definitions Byelaw.

The provisions of this Code of Practice apply to *members' agents* where they advise or assist a client (who may or may not be a *member*) in connection with the transfer of an interest in a *corporate member*.

This Code of Practice supplements the Code for Members' Agents: Responsibilities to Members where the *members' agent's* client is also a *member*.

Members' agents must, of course, also act in accordance with its FSA permissions, the FSA Handbook, with all other applicable *requirements of the Council* and, where the client is domiciled overseas, any local requirements.

This Code of Practice has been made under paragraph 31 of the Underwriting Byelaw following consultation with members, *members' agents*, the LMA, the ALM, the HPG and the FSA. This Code of Practice comes into force on 20 February 2012.

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1. **Application**

- 1.1 Where a *members' agent* advises or assists a client (who may or may not be a *member*) in connection with the transfer of an interest¹ in a *corporate member* it is essential that the *members' agent* –
- a. acts in the best interest of that client;
 - b. properly manages its duties to its other clients; and
 - c. seeks to protect the reputation and standing of the Lloyd's market as a whole.

This Code of Practice seeks to promote best practice in this regard. It should not, however, be taken to be exhaustive.

- 1.2 *Members' agents* will be expected to demonstrate that they fulfil their responsibilities to their clients by adhering to this Code of Practice. Failure to do so may lead to the commencement of *enforcement proceedings* especially where failure has in turn led to a failure to deal openly and honestly with, or provide clear and accurate information to *members*, counterparties or other relevant parties (see Lloyd's Principles of Enforcement Action (Market Bulletin ref: Y4202)).
- 1.3 All advice and information provided by a *members' agent* to its client in accordance with this Code of Practice must be clear, comprehensive, impartial and be suitable for the client (having regard to the information disclosed by the client to the *members' agent* and other relevant facts about the client which the *members' agent* is, or reasonably should be, aware).
- 1.4 *Members' agents* must keep records of all material written or oral advice provided to their clients.

2. **General**

Engagement letters

- 2.1 Where a *members' agent* is to advise or assist a client in connection with the transfer of an interest in a *corporate member* (the "interest") the *members' agent* must provide the client with an engagement letter setting out all of the key terms of the engagement including –
- a. that they will act in the best interest of the client;
 - b. the nature of the advice and assistance the *members' agent* has agreed to provide to the client. In particular, the engagement letter must set out whether the advice and assistance will cover –

¹

Interest means share in the case of a corporate member which is a company, partnership share in respect of a corporate member which is a Scottish Limited Partnership and member's share in respect of a corporate member which is a Limited Liability Partnership.

- i. valuation of the interest (see paragraph 2.2 below);
- ii. the tax implications (if any) of the transfer;
- iii. how the transfer will be effected (see paragraph 3.1.c below); and
- iv. the regulatory implications of the transfer including Lloyd's change of control arrangements (see paragraph 8 below).

Where the *members' agent* will not be engaged to advise or assist on any of the matters listed above, the *members' agent* must advise on any risks to which this may expose the client.

- c. how the *members' agent* will be remunerated for the advice and assistance that it provides and what liability the *members' agent* accepts towards the client;
- d. how the *members' agent* will seek to avoid or manage any conflicts of interest it may have in connection with the advice or assistance (see paragraph 7 below); and
- e. to whom a client may address any complaint with regard to the advice or assistance provided by the *members' agent*. This must include that if a complaint cannot be resolved by the *members' agent* within a reasonable period, the client may refer the complaint for review by the Lloyd's Auction Official.

Valuation of interest

- 2.2 Where a *members' agent* has been engaged to advise on or assist in connection with the valuation of the interest the *members' agent* must set out how the *members' agent* will properly value the interest having regard to all relevant matters and consider how to keep the valuation up to date.

3. Advising sellers

- 3.1 Where a *members' agent* has been engaged to offer an interest for sale to its clients generally (or more widely) the *members' agent* must –
 - a. simultaneously offer the interest for sale to the clients of the other *members' agents*. That must be done by advertising the interest on a dedicated web page of the *members' agent's* website which is easily accessible by the other *members' agents*. A *members' agent* must also promptly notify the other *members' agents* by email of all new advertisements, material changes to advertisements and the withdrawal of advertisements shown on their dedicated web page. Where the web page is password protected access must be provided to the other *members' agents* (and to *members* on request);
 - b. clearly set out how due diligence on the *corporate member* may be conducted and provide all relevant information in this regard to interested buyers and their *members' agents* on request;

- c. clearly set out how the successful buyer will be selected (for example, by using sealed bids, reserve prices etc.), when and how the contract for the sale (or the transfer of the interest itself) will be concluded and what steps will be taken if the contract is not, for any reason, concluded and the interest is to be offered for sale again; and
- d. clearly set out in any documentation that it sends to each interested buyer that it is the responsibility of that party to seek their own advice in relation to the purchase of the *corporate member* and the transfer process in general.

3.2 In so doing, the *members' agent* must –

- a. seek to provide an equal, transparent and fair opportunity for the clients of all *members' agents* to buy the interest; and
- b. not depart from the procedures set out by the *members' agent* for due diligence or buyer selection.

4. Advising buyers

4.1 Where a *members' agent* has been engaged to advise or assist in connection with identifying opportunities to acquire an interest for a client the *members' agent* must –

- a. regularly monitor the other *members' agents* web pages on which interests are advertised; and
- b. seek any necessary clarification with regard to the procedures set out for due diligence or buyer selection.

5. Advising members

5.1 Each *members' agents* must ensure that each of its *members* understand the advantages and disadvantages of –

- a. purchasing syndicate capacity in the capacity auctions; and
- b. acquiring an interest in a *corporate member*,

before a *member* first participates in the capacity auctions or seeks to acquire an interest in a *corporate member*.

6. Engaging third parties

6.1 Where a *members' agent* has been engaged to advise or assist in connection with the transfer of an interest and the *members' agent* is to engage a third party to provide all or part of that advice or assistance (for example, engaging an accountant to provide valuation advice or a lawyer to effect the transfer of shares) the *members' agent* shall ensure that –

- a. the third party is suitable to provide such advice or assistance; and
- b. that the third party is properly instructed.

7. Conflicts of interest

7.1 A *members' agent* must seek to avoid any conflicts of interest arising as a consequence of acting for a client in connection with the transfer of an interest in a *corporate member* or must seek to manage the situation in such a way as to ensure fair treatment to all its clients. In particular, a *members' agent* must, in accordance with its fiduciary duties, not place its own interests above those of its clients.

7.2 In circumstances of a conflict of interest, or potential conflict of interest, a *members' agent* must either –

- a. disclose the conflict of interest, or potential conflict of interest, to all of its relevant clients;
- b. especially in cases where a *members' agent* may be acting for both a buyer and a seller of an interest, effect an appropriate “Chinese wall” i.e. an arrangement whereby information known to persons involved in one part of the business is not available (directly or indirectly) to those involved in another part of the business. In each of the parts of the business so divided, decisions will be taken without reference to any interest which any other such part of the business may have in the matter;
- c. take some other effective action appropriate to the circumstances of the case; or
- d. decide that it cannot act for a client.

A *members' agent* must keep appropriate records of all such matters.

8. Lloyd's change of control arrangements

8.1 A *members' agent* must advise its clients that, in accordance with paragraph 12 of the Membership Byelaw:

“No person shall, without the prior written consent of the *Council*, be a *controller* of a *corporate member*”.

Controller for these purposes has the meaning given in section 422 of the Financial Services and Markets Act 2000. Accordingly, *members' agents* must, where relevant, advise their clients on Lloyd's change of control arrangements.

A *members' agent* may seek an early indication from Lloyd's as to whether consent will be given under paragraph 12 before seeking to acquire an interest for a new client.

9. *Protecting the reputation and standing of the Lloyd's market as a whole*

- 9.1 *Members' agents* must at all times seek to protect the reputation and standing of the Lloyd's market as a whole when advising or assisting in connection with the transfer or an interest recognising that their clients may have little or no knowledge of the operation of the market or of the business of insurance at Lloyd's.

Guidance:
Transfer of interests in
Lloyd's Corporate Members

1. Introduction

1.1 This Guidance note is aimed at those who may be considering acquiring or disposing of an interest in a Lloyd's Corporate Member where they are not members of Lloyd's and have not engaged a members' agent or another suitably qualified professional with detailed experience and knowledge of the Lloyd's market.

1.2 **Lloyd's strongly recommends that you do engage a members' agent or another suitably qualified professional adviser before proceeding.**

1.3 The members' agents contact details are as follows:

Alpha Insurance Analysts
107 Fenchurch Street
London
EC3M 5JF
+44 (0)20 7767 3420
www.aianalysts.com

Argenta Private Capital
Fountain House
130 Fenchurch Street
London
EC3M 5DJ
+44 (0)20 7825 7200
www.argentapl.com/argentapl/index

Hampden Agencies
85 Gracechurch Street
London
EC3V 0AA
+44 (0)20 7863 6500
www.hpcgroup.co.uk/hampden-lloyds-members-agency/hampden-agencies-ltd

1.5 This guidance is no substitute for the advice and assistance that a members' agent or another suitably qualified professional can provide. **In particular, Lloyd's accepts no liability to you for the content of this guidance or for any reliance you may place on it.**

- 1.6 The guidance has been provided in order that you can understand –
- a. why the advice and assistance of a members' agent or another suitably qualified professional should be sought; and
 - b. that any change of control of a Lloyd's corporate member requires Lloyd's consent and cannot take effect until that consent has been given.

2. Why the advice and assistance of a members' agent or another suitably qualified professional should be sought

2.1 Those seeking to acquire or dispose of interests in corporate members need to be aware that the valuation of the assets and liabilities of a Lloyd's corporate member is complex and requires careful consideration of a wide range of issues. Some of these issues are set out below but this is not intended to be an exhaustive list. You should always have careful regard to the particular circumstances of the acquisition of a specific corporate member.

- a. A corporate member can be either a company, Scottish limited partnership or a limited liability partnership especially formed to underwrite at Lloyd's. There are a variety of reasons why individuals prefer one form of vehicle over another, the most common one being tax considerations. You will need to consider which form of member best meets your individual needs;
- b. When you acquire a corporate member which is currently underwriting at Lloyd's, you are not only acquiring the corporate member's prospective rights to participate on specific syndicates but also acquiring the underwriting liabilities of that member in relation to its open years of account. This means that the member could either receive profits or be required to pay for losses arising from its underwriting at Lloyd's. It is important that those acquiring a corporate member also fully understand that underwriting insurance business is high risk. In addition, the corporate member may have other liabilities (for example, tax liabilities) which will need to be taken into account;

Analysing the value of the prospective rights of the member to participate on specific syndicates requires knowledge and an understanding of how the syndicates are managed by the relevant Lloyd's managing agents and of their syndicate business plans which have been agreed with Lloyd's. Regard also needs to be given to the historic auction prices (if any) of the syndicate capacity held by the corporate member. It is important that those acquiring a corporate member understand that it is difficult to accurately assess on a particular date the value of the prospective rights of the member to participate on specific syndicates as the only opportunity to definitively establish the value is when such rights are sold in the Lloyd's auctions. The auctions take place on an annual basis in September and October. There is also a risk that circumstances may subsequently arise after such rights have been acquired

which may detrimentally affect the value of some or all of those rights;

In order to assess the extent of the liabilities of the member and ascertain the value of the interest to be acquired, due diligence should be carried out on a corporate member prior to any transfer taking place. This due diligence will assist you in determining what you are prepared to offer by way of consideration to the person disposing of the interest in the member. You should consider engaging a members' agent or professional adviser (for example, an accountant) to assist you with this due diligence and valuation process;

- c. Ownership of a corporate member brings with it a range of financial and regulatory obligations. In particular, the member will be required to lodge capital with Lloyd's to support its underwriting. You will need to understand the basis on which this capital is provided to Lloyd's, what forms of capital are eligible and the circumstances in which that capital will be used to meet the member's liabilities. It is essential that you have a full understanding of these obligations prior to acquiring a member and are able to assess what will best meet your individual needs;
- d. Where you are disposing of your interest in a corporate member, you may have your own contacts for individuals who wish to acquire a corporate member. However, it also may be in your best interests to also consider using a members' agent or professional adviser in order to broaden the pool of potentially interested parties;
- e. Effecting the transfer of an interest in a corporate member from the seller to the buyer will require the parties to enter into a number of legal agreements. The parties will therefore need to instruct legal advisers to assist them in the preparation of these documents and to ensure that the documents accurately reflect the agreement of the parties.

The matters set out above require knowledge of the Lloyd's market as well as an understanding of the complex tax, legal and regulatory issues which may arise from the transfer of a corporate member. For this reason, Lloyd's strongly recommends that you engage a members' agent or other professional adviser to provide this knowledge and experience and guide you through the process of acquiring a member.

3. Lloyd's change of control

Those seeking to acquire an interest in a corporate member should note that there are Lloyd's requirements for changes of control in corporate members. In accordance with paragraph 12 of the Membership Byelaw –

"No person shall, without the prior written consent of the Council, be a controller of a corporate member"

Lloyd's uses the FSA definition of "controller" for this purpose as set out in section 422 of the Financial Services and Markets Act 2000. Accordingly, members are required to obtain Lloyd's approval prior to any change of control.

Those seeking to buy an interest in a corporate member should ensure that they get confirmation from the relevant member that this consent has been sought from Lloyd's as part of the transaction. They should also be aware that Lloyd's will also ask new controllers to sign a declaration confirming that they have read this Guidance.

In the event that Lloyd's prior approval to the change of control is not obtained, Lloyd's may withdraw the corporate member's permission to underwrite.

4. Further information about Lloyd's

More information about Lloyd's can be found on our website –

www.lloyds.com/Lloyds/Investor-Relations/Lloyds-overview

If you have any questions about this Guidance, please contact Paul Thornton of Lloyd's Legal and Compliance Department (+44 (0) 207 327 6281).

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