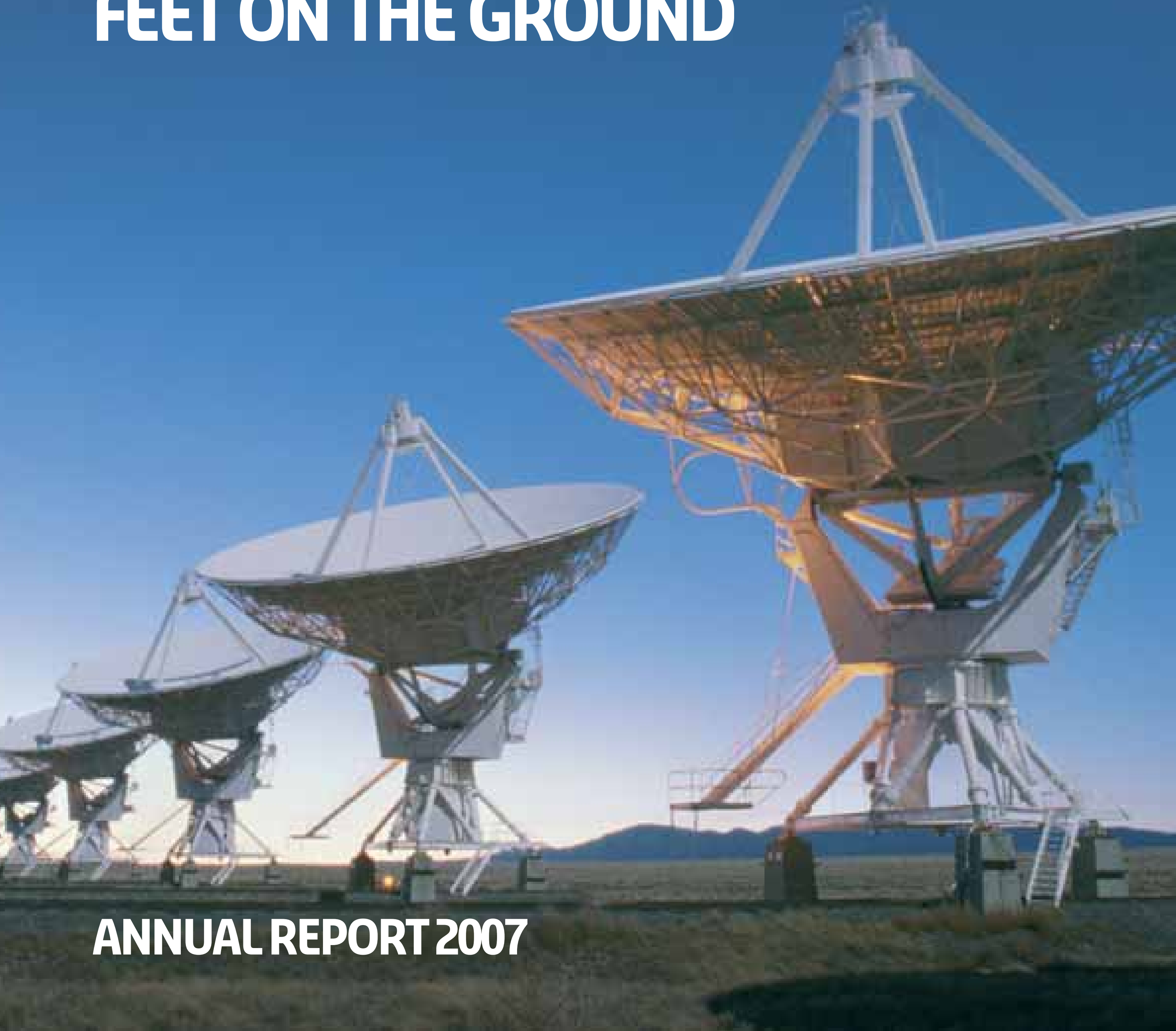
LLOYD'S

EYES ON THE FUTURE
FEET ON THE GROUND



ANNUAL REPORT 2007

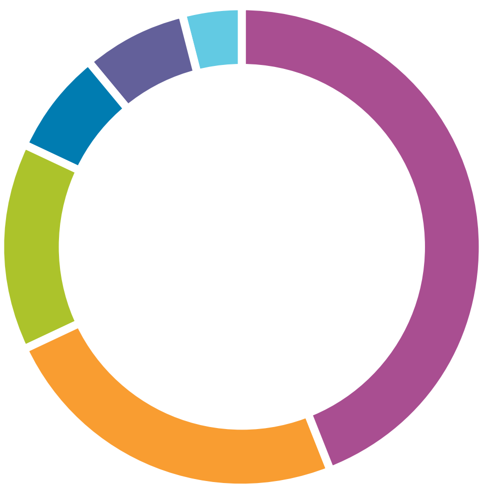
OUR BUSINESS

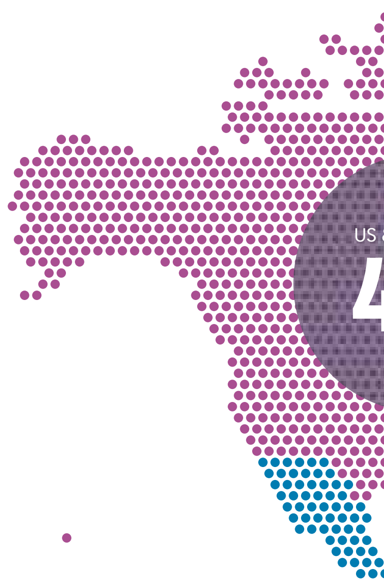
Lloyd's is licensed to underwrite business in 79 territories and can accept risks proposed from over 200 countries and territories in accordance with local laws and regulation. Lloyd's licences offer broad access to major direct and reinsurance markets worldwide.

A full list of countries covered by Lloyd's licences is available at: www.lloyds.com/worldwide

Lloyd's total business by region

US & Canada	**44%**
United Kingdom	**24%**
Europe	**14%**
Other Americas	**7%**
Central Asia & Asia Pacific	**7%**
Rest of the World	**4%**





Lloyd's total business by class

Reinsurance	**33%**
Property	**23%**
Casualty	**21%**
Marine	**8%**
Energy	**6%**
Motor	**6%**
Aviation	**3%**

All figures as at 31 December 2007.

Total business by region*

US & Canada
Lloyd's business by class

Reinsurance	28%
Property	32%
Casualty	21%
Marine	6%
Energy	9%
Motor	1%
Aviation	3%

Other Americas
Lloyd's business by class

Reinsurance	71%
Property	9%
Casualty	8%
Marine	5%
Energy	4%
Motor	1%
Aviation	2%

United Kingdom
Lloyd's business by class

Reinsurance	23%
Property	20%
Casualty	23%
Marine	7%
Energy	3%
Motor	21%
Aviation	3%

Europe
Lloyd's business by class

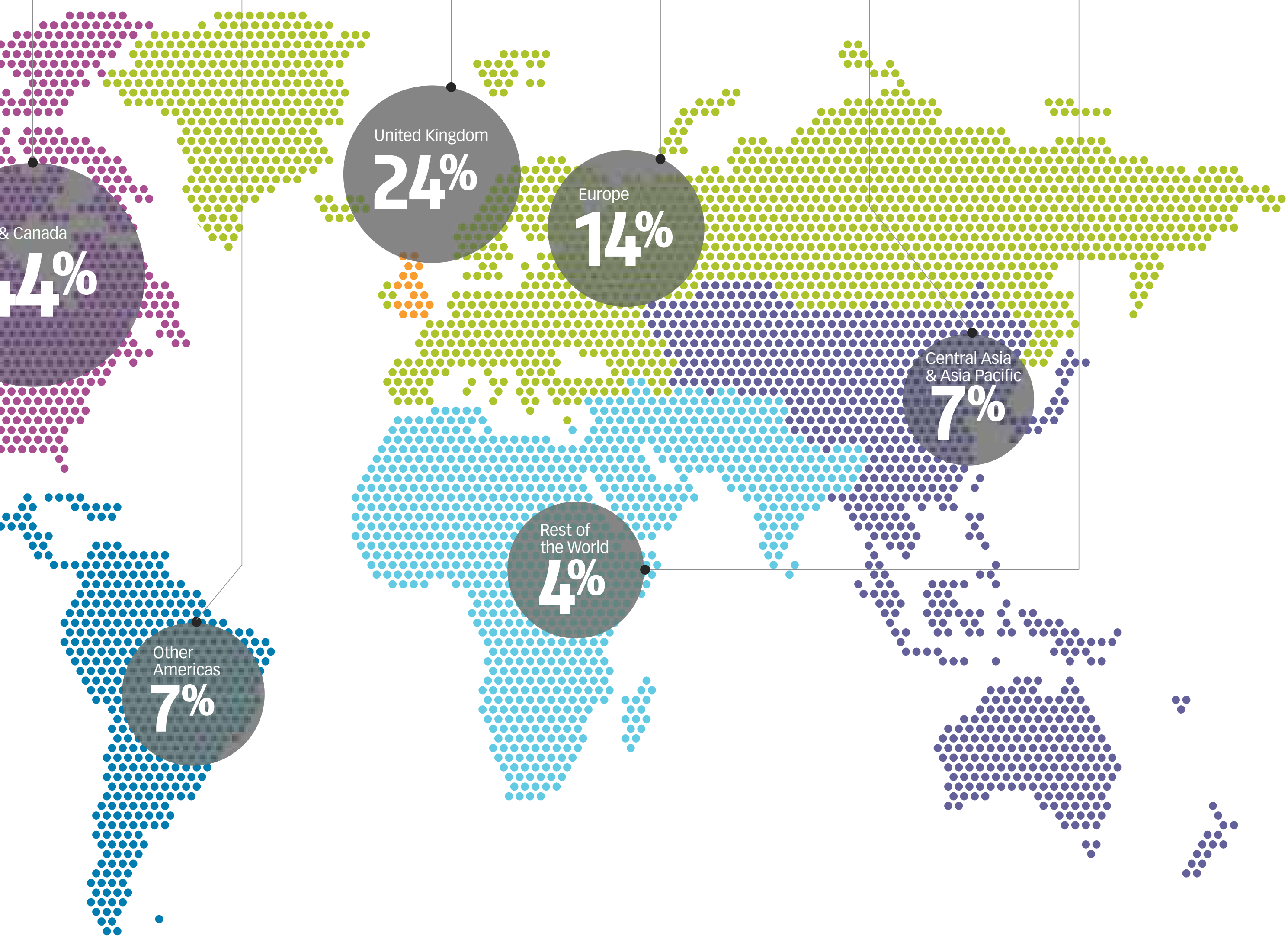
Reinsurance	37%
Property	17%
Casualty	20%
Marine	15%
Energy	6%
Motor	2%
Aviation	3%

Central Asia & Asia Pacific
Lloyd's business by class

Reinsurance	44%
Property	16%
Casualty	26%
Marine	6%
Energy	5%
Motor	0%
Aviation	3%

Rest of the World
Lloyd's business by class

Reinsurance	58%
Property	10%
Casualty	13%
Marine	8%
Energy	4%
Motor	2%
Aviation	5%



*Geographical split is based on Xchanging Ins-sure Services data, as at 31 December 2007.

As an insurer of many of the world's toughest risks, it's only natural that Lloyd's looks to the future. As an institution with many stakeholders, we must also have a secure grounding in the present. This report shows we have just that. 2007 was a strong year where profit before tax rose to £3.8bn and we continue to outperform our international peers*.

These positive results stem from an appetite for risk and an ability to turn risk into reward. While the number of catastrophic events was higher than in 2006, the year was relatively benign when considering insured losses. Our strong balance sheet has yielded significant investment returns which, together with prior year releases, have made a substantial contribution to these results.

Over the years, Lloyd's has shown that it can evolve to meet the changing risk environment. We have continued to pioneer new risk solutions and expand into new markets. At the same time, we have generated ideas closer to home – the programme of business process reform is well underway.

From this secure position, we can take a confident and considered approach to future challenges.

WE KEEP OUR EYES ON THE FUTURE AND OUR FEET ON THE GROUND.

The pro forma financial statements (PFFS) are prepared so that the financial results of Lloyd's and its members taken together and their net assets can be compared with general insurance companies. The PFFS include the aggregate of syndicate annual accounts (Aggregate Accounts), members' funds at Lloyd's (FAL) and the Society of Lloyd's financial statements. The Aggregate Accounts are reported as a separate document and can be found at www. lloyds.com/financialreports.

This report includes the consolidated financial statements of the Society of Lloyd's and all of its subsidiary undertakings, the Central Fund and the group's interest in associates.

*Based on combined ratios calculated from published industry aggregates and reported 2007 financials of our peers.

CONTENTS

OVERVIEW AND HIGHLIGHTS

2007 BUSINESS HIGHLIGHTS

Standard & Poor's and Fitch Ratings upgraded Lloyd's financial strength to A+, A.M. Best affirmed its rating of A.

£500m of Tier 1* subordinated debt was raised successfully, allowing greater flexibility and liquidity.

The China Insurance Regulatory Commission approved Lloyd's Reinsurance Company (China) Limited to begin operations in Shanghai.

Good progress continued to be made on key business reform initiatives:

- → Contract certainty consistently exceeded 90% during 2007.
- → Electronic repositories for claims and back office processing were put in place.

The first phase of the Equitas and Berkshire Hathaway transaction was completed.

The Lloyd's Asia Platform in Singapore expanded to 13 syndicates.

Lloyd's launched its graduate programme to increase talent in the industry.

*See Glossary on page 152.

2007 FINANCIAL HIGHLIGHTS

STRATEGY

→ Lloyd's achieved a profit before tax of £3,846m (2006: £3,662m) and a combined ratio of 84.0% (2006: 83.1%) reflecting continued strong performance.

→ Return on investments of 5.6% (2006: 4.7%) the highest for five years.

→ Overall surplus on prior years of £856m (2006: £270m) as claims develop within projections for the third successive year.

→ Pre-tax return on capital of 29.3% (2006: 31.4%) reflecting a second successive year of excellent results.

→ Central assets increased by 34% to £1,951m (2006: £1,454m).

Gross written premium £16,366m

2003	£16,422m
2004	£14,614m
2005	£14,982m
2006	£16,414m
2007	**£16,366m**

Profit/(loss) before tax £3,846m

2003	£1,892m
2004	£1,367m
2005	£(103)m
2006	£3,662m
2007	**£3,846m**

Capital, reserves and subordinated debt and securities £14,461m

2003	£10,145m
2004	£12,169m
2005	£10,992m
2006	£13,333m
2007	**£14,461m**

Central assets £1,951m

2003	£781m
2004	£1,196m
2005	£1,266m
2006	£1,454m
2007	**£1,951m**

Return on capital 29.3%

2003	21.4%
2004	12.5%
2005	(0.9)%
2006	31.4%
2007	**29.3%**

Combined ratio 84.0%

2003	90.7%
2004	96.6%
2005	111.8%
2006	83.1%
2007	**84.0%**

VISION: OUR VISION IS TO BE THE PLATFORM OF CHOICE

For more information see page 30.

WE HAVE A CLEAR STRATEGY TO ACHIEVE OUR VISION

Lloyd's has set out its vision to be the platform of choice for insurance and reinsurance buyers and sellers to access and trade specialist property and casualty risks.

1 PERFORMANCE FRAMEWORK →
An overarching, consistent performance management framework across all key aspects of a managing agent's business, that supports the achievement of superior operating returns as part of an effective enterprise risk model.

2 CAPITAL ADVANTAGES →
A capital framework in which the benefits of mutuality demonstrably outweigh the costs and which cannot readily be duplicated outside Lloyd's.

3 SECURITY AND RATINGS →
Stable insurer financial strength ratings (currently at least 'A') necessary to attract specialist property and casualty business.

4 MARKET ACCESS →
Cost-effective, easy access to the major markets supported by a global brand and licence network.

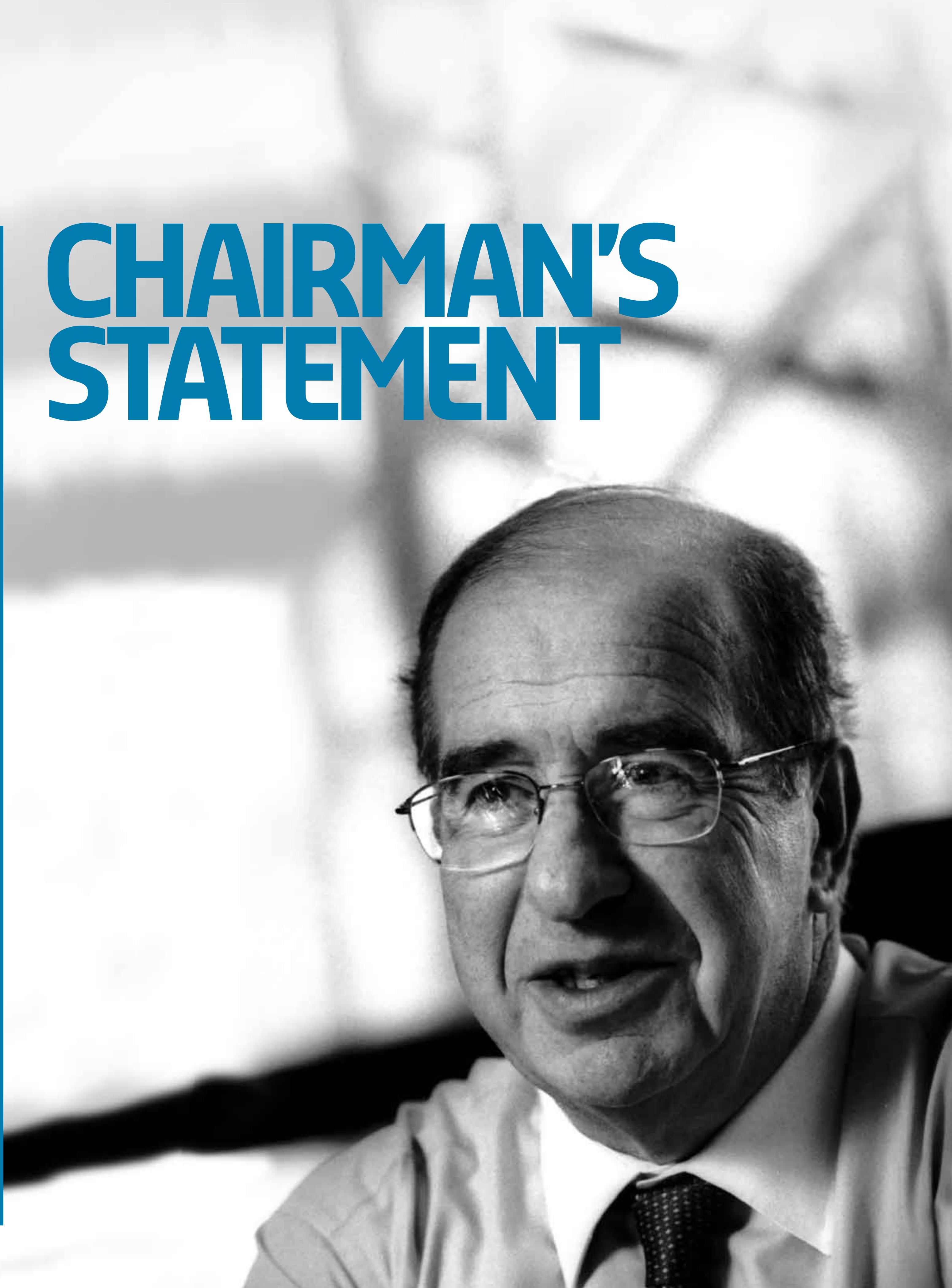
5 OPERATING ENVIRONMENT →
An efficient, cost-effective operating environment that allows managing agents and brokers, irrespective of their location, to deliver excellent service to customers.

STRATEGIC PRIORITIES:

→ **MANAGING THE CYCLE**
→ **MARKET ACCESS**
→ **OPERATING ENVIRONMENT**

WELCOME TO LLOYD'S

CHAIRMAN'S STATEMENT



2007 was a profitable year for Lloyd's with the market reporting a £3,846m profit. With a combined ratio of 84.0%, Lloyd's continues to outperform its international peers.

The market has benefited from a low level of catastrophe and claims activity; however this has led to increased pressure on rates and a softening of rates, terms and conditions across all lines of business.

The need to exercise underwriting discipline and maintain a focus on underwriting for profit rather than market share remains essential. I am encouraged by the number of businesses who have recently announced they are reducing the amount of business they plan to write this year, in line with changing market conditions, and have shown a more robust approach to capital management – increasing dividends and returning capital to shareholders.

Within Lloyd's we have sought to strengthen our capital resources with a £500m debt issue. It has enabled us to repay over £300m of loans from our syndicates and to further reinforce the Central Fund.

Dealing with the realities of the insurance cycle does not mean inertia or preclude growth in areas where a sound commercial business case exists. We will continue to welcome new syndicates that add to the skill base of the market and bring in new and profitable business.

Over the course of the cycle, it is essential that Lloyd's remains a dynamic and attractive marketplace. We need to be establishing the foundations for future growth now, so that we are in the best possible position to take advantage of opportunities when market conditions improve.

The imperatives to evolve and reform remain as strong as ever. The commercial environment is fiercely competitive and we must continue to work with the market to deliver the changes needed to realise our vision of being the platform of choice.

During 2007, the market made significant progress in reforming its processes. Businesses at Lloyd's have embraced the use of technology and now over 70% of all claims and original premium transactions are processed electronically.

We also further broadened our global footprint in Asia and began moves to expand our presence in Latin America, the Middle East and Continental Europe.

Two key appointments to the Executive Team reflected these priorities. Sue Langley joined us as Director, Market Operations and North America to drive our work enhancing the market's operational competitiveness and to focus on North American business. Sue was joined by Jose Ribeiro as Director, International Markets and Business Development with responsibility for promoting the market across the globe, seeking new business opportunities and monitoring the development of emerging markets.

I believe that 2007 has proved to be a year of real progress for Lloyd's. This was only made possible, however, through the hard and devoted work of all of those who work here, to whom I am most grateful. We are also very well served by a first class Council and Franchise Board and, again, I would like to thank all of the members of both bodies for their hard work. This is especially so in respect of those whose terms of office have come to an end and who can look back with satisfaction at their significant contribution to the development of Lloyd's.

PETER LEVENE
Chairman
2 April 2008

ABOUT LLOYD'S

AS THE WORLD'S LEADING SPECIALIST INSURANCE MARKET, WE ARE OFTEN THE FIRST TO INSURE NEW, UNUSUAL AND COMPLEX RISKS.

From oil rigs, man-made structures and major sporting events, to new areas such as cyber-liability and terrorism, Lloyd's conducts business in over 200 countries and territories worldwide. Our clients include 90% of FTSE 100 companies and 93% of Dow Jones companies.

Over 300 years ago Lloyd's began in Edward Lloyd's coffee house as a place where ship-owners could meet people with capital to insure them. Since then, Lloyd's has grown from its marine insurance base to become the world's leading market for specialist property and casualty insurance, covering some of the world's largest, most complicated and unique risks.

Today, Lloyd's remains a face-to-face market, with all the dynamism and innovation that a market generates. Like any market, it enables those with something to sell – underwriters providing insurance coverage – to make contact with those who want to buy – brokers, working on behalf of their clients who are seeking insurance. We gain our strength from the diversity of managing agents who choose to operate here, backed by capital from diverse sources around the world.

The Underwriting Room is central to the smooth running of the Lloyd's subscription market, where large and complex risks can be shared between market participants. We offer a range of distribution channels that allow managing agents to access specialist businesses.

We continue to introduce ways to make Lloyd's an easier place to do business, increasing efficiency and standards of service. Our processes may change, but mutuality of capital will remain central to Lloyd's. It helps us to be more competitive and underpins our licences and ratings.

Lloyd's continues its steady expansion into overseas markets to build the platform for the future. A major priority will be managing performance through the downcycle. We will continue to strengthen our competitive position and improve our processes, taking account of industry trends, in readiness for more favourable market conditions.

Why Lloyd's is a leader in the global insurance market

Developing Lloyd's future leaders

Lloyd's future success clearly depends on the quality of its leaders. Looking ahead, London Business School – one of the world's top ranked business schools – and Lloyd's have developed a leadership course, with content aligned to the challenges and issues facing leaders operating in the market and the Corporation.

The Leadership Development Programme provides existing and aspiring Lloyd's leaders with the skills to respond to the changing nature of the global insurance industry, so they can drive their own businesses forward in positive and creative ways. The programme consists of three modules spread over a nine-month period and focuses on the behavioural aspects of leadership as well as strategic challenges. In this way, it provides a practical toolbox to use in the workplace.

Core strengths

→ Solid financial performance
Lloyd's reported £3.8bn profit in 2007.

→ Global leadership
The Lloyd's market provides specialist underwriting expertise in over 200 countries and territories and we are looking to expand our presence further.

→ Sound management
The Corporation has an experienced management team that is committed to improving the Lloyd's market.

→ Capital strengths
Lloyd's has a unique capital structure that provides excellent financial security to customers and capital efficiency to members.

→ Clear strategy
Lloyd's has a clear vision – to be the platform of choice – and a clear strategy to achieve it.

→ Appetite for risk
Lloyd's underwriters will consider risks that others can't or won't.

→ Innovative risk solutions
Lloyd's underwriters have an entrepreneurial approach to risk, relying on their expertise and common sense.

→ Strong heritage 1688-2008
Over 300 years ago merchants first met to insure their ships at Edward Lloyd's coffee house. Since then, Lloyd's has become the world's leading specialist insurance market.

STABILISING...

MANAGING THE UNDERWRITING CYCLE

Managing the underwriting cycle remains a priority at Lloyd's. Responding to changing market conditions, managing agents are taking a more robust approach to underwriting management. They are focused on reinforcing their strong reputation by proving that they can manage their underwriting through a downturn, while remaining ready to take advantage of improved conditions when the market turns. By analysing actual risk exposure, rather than merely following market trends, they are well positioned to ride the cycle.

BY STANDING FIRM

THE RIGHT RATE FOR GRIDIRON RISKS

As international interest in American football continues to grow, the insurance market for the sport has been booming. “Premiums have risen in the last few years…” says one of Lloyd’s underwriters involved in the sport. “But it’s not a rate we should look to be cutting.”

Top players are insured for upwards of £1m, with the game’s most prized assets – the quarterbacks – commanding cover of as much as £30m. The quarterbacks may be the stars, but it’s the solidity of the offensive line that gives them space to play. Like a strong offensive line, the Lloyd’s market is concentrating on managing the downturn by standing firm.

HOW WE WORK
MARKET STRUCTURE

THE LLOYD'S MARKET BRINGS TOGETHER AN OUTSTANDING CONCENTRATION OF SPECIALIST EXPERTISE AND TALENT.

Lloyd's is not an insurance company, it is a partially mutualised market where members of Lloyd's join together as syndicates to insure risks. Much of Lloyd's business is written on a subscription basis, with more than one syndicate taking a share of the same risk.

How we work

Corporation of Lloyd's

Policyholders	Lloyd's brokers Service companies	Syndicates	Managing agents	Members
Business flow →				← Capital provision
Risk	**Distribution**	**Underwriting**	**Management**	**Capital provision**
Clients have risks that need to be insured or reinsured. They will discuss their needs with a broker.	Brokers: facilitate the risk transfer process between clients and underwriters. Depending on the complexity or size of the risk, there may be more than one broker in the distribution chain. Service companies: some risks are placed directly with managing agent-owned service companies.	Syndicates have specialist underwriters who price, underwrite and handle any claims in relation to the risk. Large, or specialist risks, are often written on a subscription basis across several participating syndicates.	Managing agents provide management and other services to syndicates. They employ underwriting and support staff and provide the business infrastructure.	Capital providers, called members, are the risk carriers. They support one, or a number of, syndicates.

SYNDICATES
WRITING THE INSURANCE

As at 31 December 2007, there were 72 syndicates at Lloyd's. Syndicates operate on an ongoing basis, although they are technically a series of annual ventures. Members have the right, but not the obligation, to participate in syndicates for the following year.

In practice, most syndicates are supported by the same capital providers for several years. The stability of the core capital base enables syndicates to function like permanent insurance operations under the Lloyd's umbrella.

A large proportion of Lloyd's business is conducted in the Underwriting Room at Lloyd's, where most of the syndicates have a presence. Here, detailed negotiations take place regarding the risks brokers wish to place at Lloyd's. Most of these placements involve face-to-face negotiations with much work underway to improve the supporting business processes and to develop an electronic infrastructure (see case study on page 27). Some syndicates specialise in underwriting a certain type of insurance, whereas others write a range of classes. Having direct access to this concentration of underwriting skill gives Lloyd's its excellent reputation for expertise, innovation and quick decision-making.

MANAGING AGENTS
MANAGING THE SYNDICATES

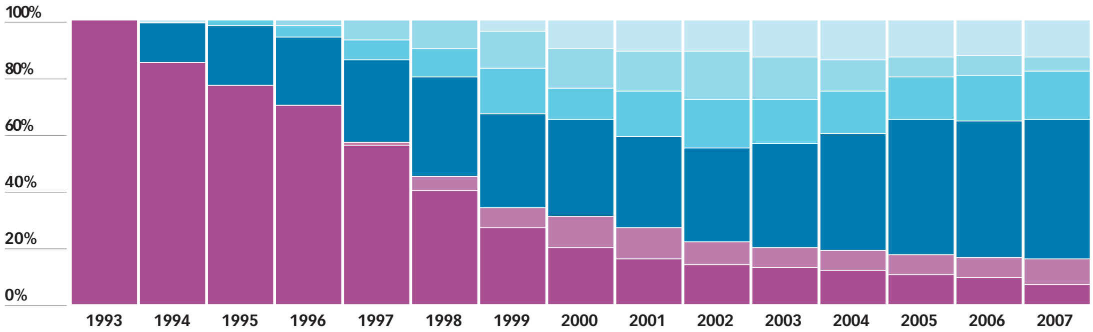
As at 31 December 2007, there were 46 managing agents at Lloyd's. A managing agent is a company set up to manage one or more syndicates on behalf of the members who are the providers of capital. The managing agent employs the underwriters and handles the day to day running of the syndicate's infrastructure and operations.

A list of managing agents and the syndicates they manage can be found on pages 14 and 15.

Many syndicates are now managed and funded by a single corporate group, integrating the management and capital provision.

In a 'dedicated' model, the syndicate is supported by a single capital provider, ownership of which is not connected to ownership of the managing agent.

Lloyd's members' sources of capital by type and location
%



	2007 %		2007 %
Worldwide insurance industry	13%	UK listed and other corporate	49%
Bermudian insurance industry	5%	Individual members (limited liability)	9%
US insurance industry	17%	Individual members (unlimited liability)	7%

For other syndicates, the capital is provided by a 'spread' of different members, who may include both private individuals and corporate groups, and the managing agent may be separately owned and managed.

MEMBERS
PROVIDING THE CAPITAL

It is the members of Lloyd's who provide the capital to support the syndicates' underwriting. Today, members are drawn from some of the world's major insurance groups and companies listed on the UK stock exchanges as well as individuals and limited partnerships.

Corporate members provide a significant majority of the total capital of the Lloyd's market. Private members typically support a number of syndicates, while a corporate member usually underwrites through a single syndicate. Members' agents provide advisory and administrative services to members. A member is liable only for its share of the risks underwritten and is not responsible for meeting any other member's underwriting liabilities.

The diverse sources of capital in 2007 are shown above.

An outline of capital setting at Lloyd's begins on page 12.

For Information on the value Lloyd's brings to its stakeholders see page 58.

CORPORATION OF LLOYD'S
SUPPORTING THE MARKET

The Corporation of Lloyd's (the 'Corporation') oversees and provides services to support the market and promotes Lloyd's around the world. The senior executives of the Corporation exercise the day-to-day powers and functions of the Council and the Franchise Board

See page 17 for more detail regarding the governance of Lloyd's.

The Corporation (including its subsidiaries) had 798 employees worldwide, as at 31 December 2007.

More information can be found in People Strategy on page 42.

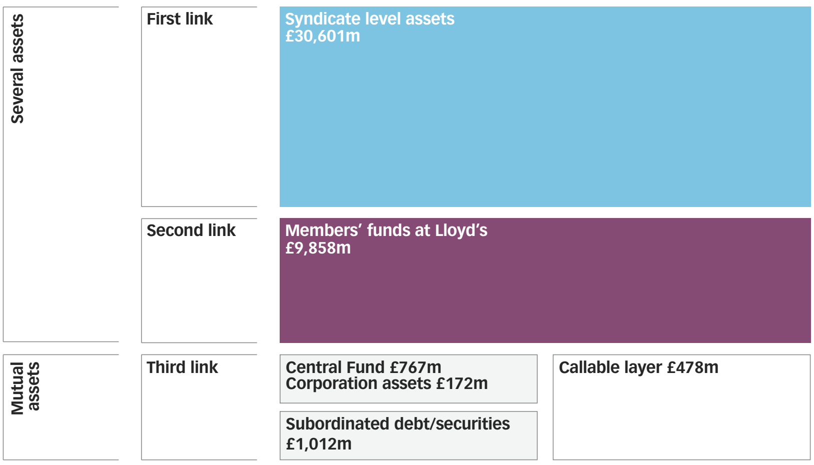
In addition to its objective to provide cost-effective services that are essential to the smooth running of the market, the Corporation strives to raise the standards and improve the performance of the market. The Corporation's work includes:

- Determining the capital that Lloyd's members must provide to support their proposed underwriting.
- Overseeing business activities of the market by operating a minimum standards framework and monitoring the performance of syndicates in areas such as exposure management, cycle management, claims management and operational risk management.
- Working with the management of underperforming syndicates to improve performance and intervening directly if stronger action is required.
- Managing financial and regulatory reporting for the Lloyd's market, including the production of Lloyd's market results and Lloyd's Financial Services Authority (FSA) return.
- Managing and developing Lloyd's global network of licences and the Lloyd's brand.

HOW WE WORK
SECURITY AND RATINGS

LLOYD'S CHAIN OF SECURITY LINKS STRENGTH WITH STABILITY.

Chain of security



All figures as at 31 December 2007.

FINANCIAL STRENGTH
THE CHAIN OF SECURITY

Lloyd's unique capital structure, often referred to as the 'chain of security', provides excellent financial security to policyholders and capital efficiency to members. The Corporation is responsible for setting both member and central capital to achieve a level of capitalisation that is robust and allows members the potential to earn superior returns. There are three 'links' in the chain: the funds in the first and second links are held in trust, primarily for the benefit of policyholders whose contracts are underwritten by that member. Members underwrite for their own account and are not liable for other members' losses.

The third link contains mutual assets held by the Corporation which are, subject to the approval of the Council, available to meet the insurance liabilities of any member. Further information regarding the security underlying policies at Lloyd's can be found on page 80.

FIRST LINK
SYNDICATE LEVEL ASSETS

All premiums received by a syndicate are held in its premiums trust funds, and are the first resource for paying policyholder claims of that syndicate. Funds are generally held in liquid assets to ensure that liabilities can be met as they fall due.

Profits are not released until full provision has been made for future liabilities. The reserves of each syndicate are subject to annual independent audit and actuarial review.

SECOND LINK
MEMBERS' FUNDS AT LLOYD'S

Each member, either corporate or individual, must provide capital to support its underwriting at Lloyd's. In accordance with the FSA regime, each syndicate produces an 'Individual Capital Assessment' (ICA) stating how much capital it requires to cover its underlying business risks.

The Corporation reviews each syndicate's ICA, to assess the adequacy of the capital level proposed. When agreed, each ICA is then 'uplifted' (by 35% for 2007) to ensure extra capital is in place to support Lloyd's ratings and financial strength. This uplifted ICA (known as the Economic Capital Assessment or ECA) for the syndicate is used to determine the capital that the syndicate's members must provide to support their underwriting. This capital is held in trust as readily realisable assets and can be used to meet any Lloyd's insurance liabilities of that member but not the liabilities of other members.

THIRD LINK
CENTRAL ASSETS

The Corporation's central assets are the third level of security.

The Central Fund is funded by members' annual contributions and subordinated debt, issued by the Corporation in 2004 and 2007. In addition to the Central Fund and assets of the Corporation, central assets may be supplemented by a 'callable layer' of up to 3% of members' overall premium limits.

Through detailed analysis, the Corporation determines the optimum level of central assets, seeking to balance the need for robust financial security against the members' desire for cost-effective mutuality of capital. In particular, the Corporation's sophisticated modelling stress tests each member's underwriting portfolio against a number of scenarios and a range of forecasts of market conditions. The Corporation's current target for unencumbered central assets is a minimum of £1.7bn.

Members' contributions to the Central Fund are set at 0.5% of gross written premiums for 2008. The Council of Lloyd's regularly reviews the central assets target and the level of contributions in light of the current financial position and forecasted needs, and will adjust the contribution levels as required.

LLOYD'S ICA AND SOLVENCY

The Corporation also prepares an ICA for Lloyd's overall, using the FSA's six risk categories to examine the risks that are not captured in each syndicate's ICA. The Corporation, for example, must consider the risks posed by a global pandemic or damage to the Lloyd's building.

In addition, the Corporation calculates and reports on the statutory solvency position of the Society of Lloyd's to the FSA. As at 31 December 2007, the Society had an estimated solvency surplus of £2, 289m.

LLOYD'S RATINGS

The world's leading insurance rating agencies recognise Lloyd's strengths and robust capitalisation and rate Lloyd's as follows:

A.M. Best: A (Excellent), Stable Outlook
Fitch Ratings: A+ (Strong), Stable Outlook
Standard & Poor's: A+ (Strong), Stable Outlook

The Lloyd's financial strength ratings apply to every policy issued by every syndicate at Lloyd's since 1993. In recent years our ratings have been resilient – with upgrades from Fitch Ratings and Standard & Poor's during 2007 – reflecting our financial and competitive strength.

"The insurer financial strength rating on the Lloyd's insurance market reflects Lloyd's strong competitive position, strong operating performance, strong capitalization, and strong financial flexibility."
Standard & Poor's, December 2007

Investing in strength – subordinated debt issue

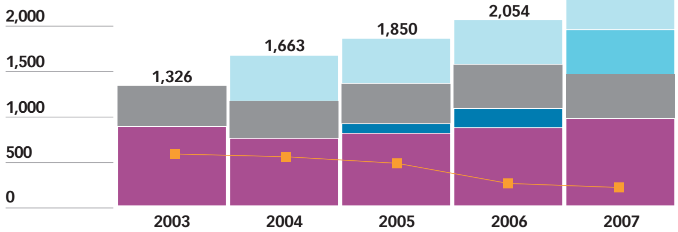
A key advantage of the Lloyd's platform is our mutual capital framework, enabling businesses to potentially generate superior returns on capital. In early 2007, the Corporation looked to identify opportunities to further improve capital efficiency and flexibility and concluded that a new tier 1* debt issue would bring a significant and stable component to our structure. It would also enable repayment of syndicate loans, which carry a significant opportunity cost to members.

With record profits reported for 2006 and rating upgrades from Standard & Poor's and Fitch Ratings, moving swiftly to bring the deal to market would maximise the opportunity to obtain favourable terms. Teams were set up to structure the deal with the joint book-runners, Citi and HSBC, and obtain the necessary tax and regulatory clearances.

Following a positive response from a wide range of quality institutional investors, the terms were set for a £500m tier 1 issue in June 2007. The success of the deal is further recognition of the strength and efficiency of Lloyd's. It has enhanced the ability of the Lloyd's platform to potentially deliver superior returns to members.

*See Glossary on page 152.

Central solvency assets†
£m



- Corporation & Central Fund assets
- Syndicate loans
- Callable layer
- Subordinated debt issued 2004
- Subordinated perpetual securities issued 2007
- Solvency deficit

† The aggregate value of central assets of the Corporation for solvency purposes at 31 December, excluding the subordinated debt liabilities, including the callable layer.

HOW WE WORK
MANAGING AGENTS AND SYNDICATES

The table shows the key characteristics for managing agents and syndicates active as at 31 December 2007. In 2007, Lloyd's wrote gross premiums of £16,366m.

MANAGING AGENT	MANAGED SYNDICATE(S)	SYNDICATE TYPE*	2006 GWP* £M	2007 GWP* £M	OWNED SHARE OF SYNDICATE %
ACE Underwriting Agencies Limited	2488	Traditional	435	393	100%
Advent Underwriting Limited	0780	Traditional	146	137	84%
Aegis Managing Agency Limited	1225	Traditional	268	240	100%
Amlin Underwriting Limited	2001	Traditional	991	901	100%
Argenta Syndicate Management Limited	1965	Traditional	9	8	100%
	2121	Traditional	99	95	54%
	3334	Traditional	1	13	33%
	6101	SPS	–	77	0%
	6102	SPS	–	42	0%
Ark Syndicate Management Limited	4020	Traditional	–	89	100%
Ascot Underwriting Limited	1414	Traditional	541	538	100%
Atrium Underwriters Limited	0570	Traditional	127	117	25%
	0609	Traditional	178	173	26%
Beaufort Underwriting Agency Limited	0318	Traditional	137	130	47%
Beazley Furlonge Limited	0623	Traditional	213	179	4%
	2623	Traditional	726	753	100%
Brit Syndicates Limited	2987	Traditional	643	647	100%
Canopius Managing Agents Limited	0044	Traditional	3	2	100%
	4444	Traditional	464	469	93%
Cathedral Underwriting Limited	2010	Traditional	226	212	56%
	3010	Traditional	–	4	100%
Catlin Underwriting Agencies Limited	2003	Traditional	598	1215	100%
Chaucer Syndicates Limited	1084	Traditional	525	526	100%
	1176	Traditional	24	22	54%
	1301	Traditional	63	69	0%
	4242	Traditional	–	38	14%
CMGL Syndicate Management Limited	5500	RITC	–	21	88%
Diagonal Underwriting Agency Limited	4455	Traditional	5	12	95%
Equity Syndicate Management Limited	0218	Traditional	552	569	64%
	1208	RITC	0	0	100%
Faraday Underwriting Limited	0435	Traditional	332	258	100%
Hardy (Underwriting Agencies) Limited	0382	Traditional	117	108	100%
	3820	Traditional	–	41	100%
HCC Underwriting Agency Limited	4040	Traditional	51	51	80%
Heritage Managing Agency Limited	1200	Traditional	290	325	81%
	3245	Traditional	58	55	61%
Hiscox Syndicates Limited	0033	Traditional	1029	996	73%
Imagine Syndicate Management Limited	1400	Traditional	58	64	100%
	2525	Traditional	46	42	2%
	2526	Traditional	30	30	36%
Jubilee Managing Agency Limited	0779	Traditional	33	29	14%
	1231	Traditional	58	51	100%
	5820	Traditional	55	64	14%

MANAGING AGENT	MANAGED SYNDICATE(S)	SYNDICATE TYPE*	2006 GWP* £M	2007 GWP* £M	OWNED SHARE OF SYNDICATE %
KGM Underwriting Agencies Limited	0260	Traditional	42	49	60%
Liberty Syndicate Management Limited	4472	Traditional	898	1045	100%
Managing Agency Partners Limited	2791	Traditional	450	342	0%
	6103	SPS	–	18	0%
Markel Syndicate Management Limited	3000	Traditional	210	197	100%
Marketform Managing Agency Limited	2468	Traditional	100	110	61%
Marlborough Underwriting Agency Limited	1861	Traditional	101	97	100%
	1919	Traditional	17	91	0%
	2243	Traditional	–	2	0%
Mitsui Sumitomo Insurance Underwriting at Lloyd's Limited	3210	Traditional	296	360	100%
Munich Re Underwriting Limited	0457	Traditional	323	309	100%
Navigators Underwriting Agency Limited	1221	Traditional	151	149	100%
Newline Underwriting Management Limited	1218	Traditional	108	90	100%
Novae Syndicates Limited†	2007	Traditional	286	274	94%
Omega Underwriting Agents Limited	0958	Traditional	251	282	16%
Pembroke Managing Agency Limited	4000	Traditional	65	59	0%
QBE Underwriting Limited	0386	Traditional	440	436	70%
	2999	Traditional	799	978	100%
RJ Kiln & Co. Limited	0308	Traditional	11	14	50%
	0510	Traditional	777	678	53%
	0557	Traditional	27	35	0%
	0807	Traditional	130	145	51%
S. A. Meacock & Company Limited	0727	Traditional	81	63	8%
Sagicor at Lloyd's Limited	1206	Traditional	46	56	100%
Spectrum Syndicate Management Limited	2112	Traditional	–	12	0%
	5151	Traditional	–	8	0%
Talbot Underwriting Limited	1183	Traditional	353	344	100%
Travelers Syndicate Management Limited	5000	Traditional	295	295	100%
XL London Market Limited	1209	Traditional	232	210	100%
All other syndicates and inter-syndicate RITC adjustment			794	(187)	
Total			16,414	**16,366**	

As at 31 December 2007.

As at 31 March 2008:

The following syndicates had commenced trading:
Traditional: s1274 – Chaucer Syndicates Ltd (Antares), s1910 – Whittington Capital Management Ltd (Goldman Sachs), s1955 – Whittington Capital Management Ltd (Barbican), s4141 – HCC Underwriting Agency Ltd.

SPS: s6104 – Hiscox Syndicates Limited, s6105 – Ark Syndicate Management Limited.

RITC: s839 – Canopius Managing Agents Limited, s2008 – Shelbourne Syndicate Services Limited, s5678 – RITC Syndicate Management Limited.

The following syndicates ceased trading:
Traditional: s3245 merged into s1200 – Heritage Managing Agency Limited.

RITC: s1208 – Equity Syndicate Management Limited.

The following syndicates changed managing agent:
Traditional: s1919 and s2243 transferred to Starr Managing Agents Ltd from Marlborough Underwriting Agency Ltd.

† 2006 comparative includes S1007 and S2147.
* See Glossary on page 152, for definitions of traditional, SPS and RITC syndicates and GWP.

HOW WE WORK
MANAGING INSURANCE RISK

WIDE-RANGING EXPERTISE IN EXISTING AND EMERGING RISKS.

MANAGING INSURANCE RISK AT LLOYD'S

As with all insurers, the largest risk facing Lloyd's is insurance risk: the inherent uncertainty of the size and timing of insurance liabilities. At Lloyd's, each syndicate sets its own risk appetite, develops a business plan, plans its reinsurance protection and manages its exposures and claims. Through the Franchise Performance Directorate, the Corporation regularly reviews the performance of the syndicates in each of these activities to ensure that it is satisfied with the level of risk posed to the overall market and its mutual assets.

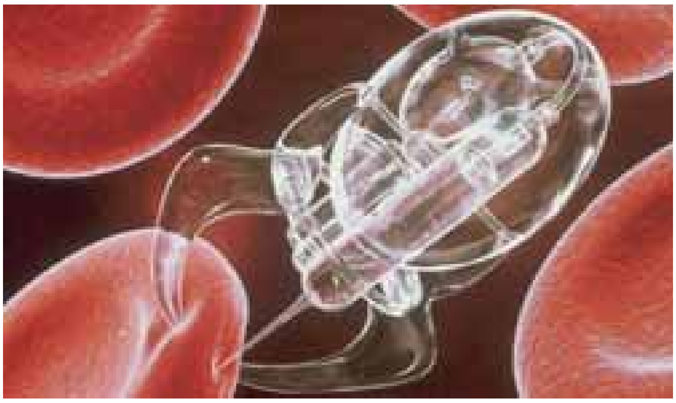
The Corporation uses various tools to control and monitor insurance risk, including:

- Setting guidelines for catastrophe exposure and reinsurance usage.
- Setting realistic disaster scenarios to assist in the measurement and management of catastrophe exposures at a syndicate and market level.
- Reviewing business plans and determining appropriate capital requirements.
- Establishing and monitoring underwriting standards, including claims and exposure management principles.

Each area of potential risk is considered by expert teams within the Corporation. If a syndicate's operations pose an unacceptable risk, the Corporation will work with that syndicate to make appropriate changes. If the syndicate does not respond to this facilitative approach, the Corporation can also withhold or withdraw approval of a business plan and in extreme cases can terminate the right of a managing agent and its syndicate to trade in the market.

The process of setting required capital for syndicates and members also begins with the syndicate's assessment of its own risks.

For more detailed information on capital setting see page 12.



Emerging risks – nanotechnology

The Emerging Risks team was set up in 2006 to identify new risks and feed back knowledge on existing risks. In 2007, the team worked with the Lloyd's Market Association to create a special interests group of experts from managing agents.

The team's latest research on the subject of nanotechnology culminated in a report ('Nanotechnology – recent developments, risks and opportunities') that can be found at www.lloyds.com/emergingrisks. Key findings of the report were that substances operating at the tiny scales of nanotechnology are often highly chemically reactive and have different properties to their larger scale versions, and this may lead to confusion among consumers and an understatement of the risks.

There is little detailed regulation at the moment, leaving more room for liability claims. A number of insurance classes could be affected, though it's too early to be sure. The technologies may be profoundly positive for society as a whole. However, while providing enormous opportunities, the potential risks should not be overlooked.

The Emerging Risks Team will continue to follow this subject closely, producing further reports on similar topics during 2008.

HOW WE WORK
GOVERNANCE

A STRUCTURED APPROACH TO CORPORATE GOVERNANCE.

THE COUNCIL AND FRANCHISE BOARD

The Council of Lloyd's is the governing body of the Society of Lloyd's, with ultimate responsibility for the management of Lloyd's. For many of its functions, the Council now acts through the Franchise Board, whose members are appointed by the Council and are drawn from inside and outside the Lloyd's market.

Further detail regarding the roles of the Council, Franchise Board and their respective committees can be found on pages 87 to 90.

The day-to-day powers and functions of the Council and Franchise Board are exercised by the executive of the Corporation. The members of the Executive Team are the CEO and the Directors of the Corporation.

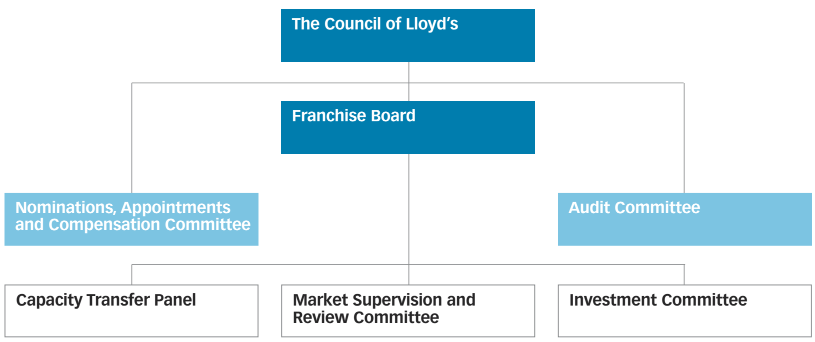
Details of the Executive Team can be found at: www.lloyds.com/managementteam

The members of the Council and the Franchise Board are listed on pages 18 and 19.

The FSA is responsible for regulating Lloyd's, including direct supervision of managing agents and monitoring capital and solvency. The Corporation plays an active role in managing risk within the market to ensure that Lloyd's central assets, brand and reputation are protected.

For more information on corporate governance see pages 87 to 90.

Principal committees of Lloyd's



MANAGEMENT
THE COUNCIL OF LLOYD'S

Council as at 2 April 2008

* Member of Audit Committee.
† Member of Nominations, Appointments and Compensation Committee.

01 **Lord Levene of Portsoken KBE**
Chairman of Lloyd's (Working member)
Peter Levene was elected as Lloyd's Chairman in November 2002. He is the Chairman of General Dynamics UK Limited and a member of the Board of TOTAL SA, China Construction Bank and Haymarket Group. He is an Alderman of the City of London and served as Lord Mayor for the year 1998/99.

02 **Dr Richard Ward**
Chief Executive Officer (Nominated member)
Richard Ward joined Lloyd's as Chief Executive Officer in April 2006. Previously he worked as both CEO and Vice-Chairman at the International Petroleum Exchange (IPE), re-branded ICE Futures. Prior to this, he held a range of senior positions at British Petroleum and Tradition Financial Services.

03 **Ewen Gilmour***†
Deputy Chairman of Lloyd's (Working member)
Ewen Gilmour is a chartered accountant and the Chief Executive of Chaucer Holdings plc. Formerly a corporate financier with Charterhouse Bank, he joined the Corporation to help facilitate the introduction of corporate capital to the Lloyd's market in 1993. He is the Chairman of the Lloyd's Market Association Market Process Committee.

04 **Graham White**†
Deputy Chairman of Lloyd's (Working member)
Graham White is Deputy Chairman of Argenta Syndicate Management Ltd and has worked in the Lloyd's market since 1968 as a reinsurance broker, company secretary and members' and managing agent.

05 **Bill Knight***†
Deputy Chairman of the Council
(Nominated member)
Bill Knight is the Chairman of the Financial Reporting Review Panel and a Gambling Commissioner. He is a solicitor and was formerly the Senior Partner of Simmons & Simmons.

06 **Rupert Atkin**†
(Working member)
Rupert Atkin is the Chief Executive of Talbot Underwriting Ltd and was the active underwriter for syndicate 1183 from 1991 until last year. He is a director of all Talbot Group companies. He has served on various market bodies, including the Lloyd's Regulatory Board and has chaired both the Lloyd's Underwriters Association and the Joint War Risk Committee.

07 **Celia Denton***
(Nominated member)
Celia Denton, a chartered accountant, was a senior audit partner at Deloitte & Touche and Head of its General Insurance Practice for 10 years. She was responsible for risk management in the assurance and advisory practice, prior to her retirement in 2003.

08 **Christopher Harman**
(Working member)
Christopher Harman is the founder member and Deputy Chairman of Harman Wicks & Swayne Ltd, a Lloyd's broker. He has worked in the Lloyd's market as a reinsurance broker since 1971, specialising in reinsurances of Lloyd's syndicates and companies writing global business. He has been an unlimited Name since 1979.

09 **Dr Reg Hinkley**
(Nominated member)
Dr Reg Hinkley is Bursar, at Christ's College Cambridge. Until July 2007 he was Chief Executive Officer of BP's UK pension fund. He joined BP in 1981, and worked in finance, planning and risk management roles. Previously he worked at HM Treasury.

10 **Paul Jardine**†
Representative of Catlin Syndicate Limited
(External member)
Paul Jardine, a qualified actuary, is Deputy Chairman of Catlin Underwriting Agencies Limited and Chief Operating Officer of Catlin Group Limited. He has over 25 years of insurance industry experience and was appointed Chairman of the Lloyd's Market Association in May 2007.

11 **The Honorable Philip Lader**†
(Nominated member)
Philip Lader, former US Ambassador to the Court of St. James's and member of President Clinton's Cabinet, is Chairman of WPP Group plc, a Senior Adviser to Morgan Stanley, and serves on the boards of Marathon Oil, AES, RAND, Rusal, Songbird Estates, and the Smithsonian Museum of American History.

12 **Alan Lovell**
(External member)
Alan Lovell is Chief Executive of Infinis Limited and Chairman of the Mary Rose Trust Appeal Committee. He has held senior positions at Costain Group plc, Dunlop Slazenger and Jarvis plc. He is a director of the Association of Lloyd's Members and of Alpha Insurance Analysts Ltd (a members' agent).

13 **Nicholas Marsh**
(Working member)
Nicholas Marsh is Director of Corporate Underwriting at Atrium Underwriting plc, having been Chief Executive from 2000 to 2005. His Lloyd's career started in 1973, when he joined Syndicate 570 and was Active Underwriter from 1989 to 2005. He is a member of the Lloyd's Market Association Board.

14 **Barbara Merry**
Representative of Hardy Underwriting Limited
(External member)
Barbara Merry is CEO of the Hardy Group. She has worked in the Lloyd's community since 1985, spending 14 years in the Corporation of Lloyd's, then as MD of Omega Underwriting Agents Ltd, before taking on her current role at Hardy. She is a member of the Lloyd's Market Association Board.

15 **Peter Morgan MBE**†
Representative of AJSLP09 (External member)
Peter Morgan, a director of the Association of Lloyd's Members, has been an underwriting member of Lloyd's since 1987. He is a director of Oxford Instruments and Hyder Consulting, and Chairman of Strategic Thought, Technetix and IXICO. He is also a UK delegate to the European Economic and Social Committee in Brussels.

16 **Dermot O'Donohoe**
Representative of Dornoch Limited
(External member)
Dermot O'Donohoe is the Chief Executive Officer of XL London Market and Chief Underwriting Officer for XL's Global Speciality business. He is Active Underwriter of syndicate 1209 and a director of several group companies in the UK and Ireland.

17 **Dr Andreas Prindl CBE***†
(Nominated member)
Andreas Prindl worked for Morgan Guaranty in New York, London and as General Manager in Tokyo and then set up Nomura Bank International, which he chaired. He was appointed a CBE for his contributions to financial services education in Britain and Eastern Europe.

18 **David Shipley***
Representative of MAP Capital Limited
(External member)
David Shipley was named underwriter for MAP Syndicate 2791 from its formation in 2000 until 2007, and is now non-executive Chairman of MAP, having worked as a Lloyd's underwriter since 1976. He has underwritten since 1984, first as a Name and subsequently with limited liability.

MANAGEMENT
THE FRANCHISE BOARD

01 **Lord Levene of Portsoken KBE**
Chairman of Lloyd's
Biography on previous page.

02 **Dr Richard Ward**
Chief Executive Officer
Biography on previous page.

03 **Roy Brown**
Roy Brown is Chairman of GKN plc, Deputy Chairman of Alliance & Leicester plc and a Director of HMV Group plc. He is a Chartered Engineer and has a Harvard MBA. He was formerly an Executive Director of Unilever.

04 **Edward Creasy**
Edward Creasy is Chief Executive Officer of the Kiln Group and Chairman of R.J. Kiln & Co Ltd. He has worked in Lloyd's since 1978 as a broker, underwriter and manager. He is a founding director of the Lloyd's Market Association.

05 **Nick Furlonge**
Nick Furlonge is the Director of Risk Management at Beazley plc. He has worked in the Lloyd's market since 1972 and was co-founder of Beazley. He is currently a Director of the Lloyd's Market Association and Chairman of the Lloyd's Community Programme Management Board.

06 **Stephen Hodge***
Deputy Chairman of the Franchise Board
Stephen Hodge is Chairman of Shell Pensions Trust Ltd. He worked until 2001 for the Shell Group as Treasurer and Finance Director with responsibility for insurance matters. He was Audit Committee Chairman for O2 plc until January 2006.

07 **Claire Ighodaro CBE***
Claire Ighodaro is a Board member of the British Council, the Banking Code Standards Board, UK Trade & Investment (UKTI), the Learning and Skills Council, the Open University and BERR. Claire also chairs three Audit Committees and was the first female President of the Chartered Institute of Management Accountants (CIMA).

08 **Andrew Kendrick***
Andrew Kendrick is Chairman and Chief Executive Officer of ACE European Group Limited. Prior to this, he served as President and Chief Executive Officer, ACE Bermuda. He has over 25 years of insurance industry experience. He was Chairman of the Lloyd's Market Association from January 2006 to June 2007.

09 **Luke Savage**
Director, Finance, Risk Management and Operations
Luke Savage, a chartered accountant, joined Lloyd's in 2004. He has over 20 years' experience in financial services, spent mostly supporting sales and trading in investment banks including Morgan Stanley and Deutsche Bank.

10 **Jim Stretton***
Jim Stretton is Chairman of the Wise Group. He was formerly UK Chief Executive of The Standard Life Assurance Company and a member of the Court of the Bank of England.

11 **Rolf Tolle**
Director, Franchise Performance
Rolf Tolle joined Lloyd's in March 2003. Previously, he was Chief Underwriting Officer of Faraday Group and has held senior positions within various insurance companies operating in Germany, Norway and the US. He is a non-executive director of Xchanging Claims Services Board.

Franchise Board as at 2 April 2008
* Member of Audit Committee.

STRATEGIC REVIEW

CHIEF EXECUTIVE OFFICER'S STRATEGIC REVIEW

The softening market conditions in 2007 reinforced, once again, the need for a clear strategy to enable the market to maintain discipline and strength in the face of increasing competition.

The Three-Year Plan 2007-2009 and the updated 2008-2010 Plan, published in December, clearly outlined the challenges and opportunities that we as a marketplace face, and the steps that we need to take to meet them and capitalise on them.

The decisions and actions we take in the next few years will ultimately determine our future. As a market, we have a responsibility to our policyholders and to ourselves to ensure that we maintain our financial strength and security throughout the course of a cycle. We also have a responsibility to continue to improve Lloyd's long-term position whether through improving our processes, attracting and retaining talent or building our global capabilities so we can grow when the time is right. Only by working together with the market to deliver the Three-Year Plan will we be able to do this.

For the first time, this year we have clearly identified key performance indicators (KPIs) in our Annual Report. These will enable us to track our performance, year on year, against a range of measures that best illustrate Lloyd's financial performance and progress in delivering our strategic objectives.

This section outlines in more detail what these KPIs are, the key features of our strategy, our progress to date and our priorities going forward.

RICHARD WARD
Chief Executive Officer
2 April 2008

EMERGING...

EMERGING MARKETS

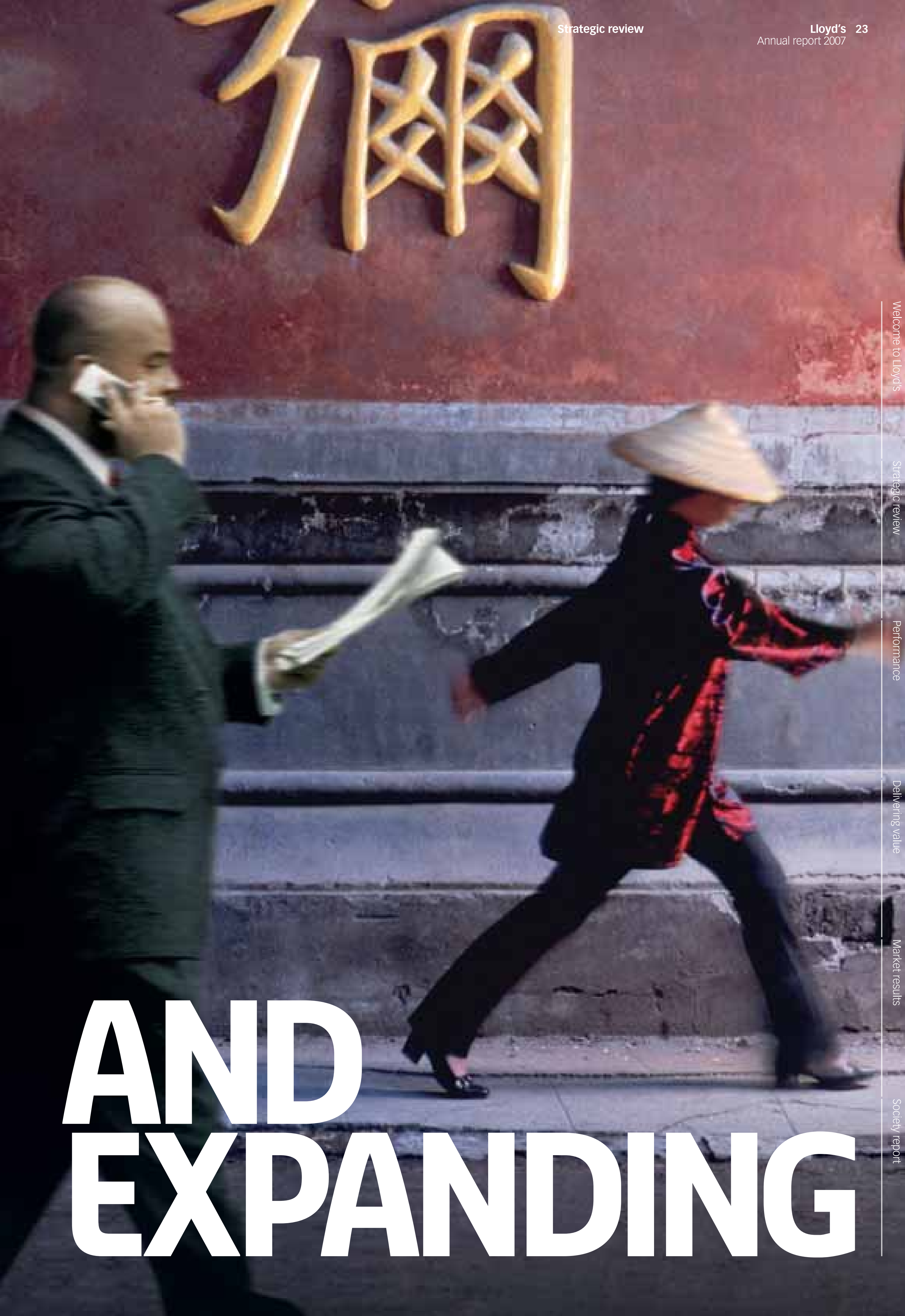
As the world economy's centre of gravity shifts, we too are moving rapidly. We are enthusiastically supporting economic growth in emerging markets. With 300 years' experience of global insurance, we know that fast growing economies need the support of growth and innovation within the insurance sector. Our onshore reinsurance operation in Shanghai is now functioning, we are working to support the liberalising reinsurance sector in Brazil and we are pursuing opportunities in India and the Middle East.

CHINA AND LATIN AMERICA

In April 2007, Lloyd's Reinsurance Company (China) Limited was established in the People's Republic of China. This growing market has shown consistent GDP growth of over 10% per annum, rapid economic development and a burgeoning consumer class.

Lloyd's has also been developing its presence in Latin America. In November 2007, Lloyd's was approved to transact direct marine, aviation and transportation business in Chile – the first foreign reinsurer to register and take advantage of this shift in regulation.

The largest economy in Latin America, Brazil, has also recently liberalised. New reinsurance regulations were approved in December 2007 and will be effective from April 2008. Lloyd's is moving fast to make sure we're ready to take on whatever new and diverse risks this exciting market provides.



AND EXPANDING

MARKETPLACE OVERVIEW
INSURANCE TRENDS

MAINTAINING COMPETITIVE STRENGTH IN AN INCREASINGLY RISKY WORLD.

The Lloyd's market remains in a strong competitive position. Interest from new sectors, record financial strength, rating agency affirmations and a number of new syndicate applicants confirm that Lloyd's is an attractive place to do business.

For more information on global insurance trends visit:
www.lloyds.com/publicmarketintelligence

THE INSURANCE CYCLE

With the insurance industry reporting excellent results for a second successive year, capacity will inevitably remain in both the direct and reinsurance markets. As a significant element of Lloyd's business is from mature markets, such as the US and the UK, the level of competition is even more intense.

As evidenced by the January 2008 renewal season, this increased competition has led to further rate reductions in most lines. We have seen some softening of terms and conditions and the re-emergence of multi-year policies in certain areas. In the absence of major adverse claims development or catastrophes, this trend is likely to continue.

While some lines of business, particularly those exposed to North Atlantic windstorms, are seeing rates soften from a relatively hard position achieved in recent years, there is concern that rates in other lines are approaching their break-even price, with minimal underwriting margins available. Some may already be below this level.

Although the length and severity of the downcycle cannot be predicted with certainty, Lloyd's recognises that a major priority for the medium term is to ensure prudent underwriting discipline is maintained. Emphasis will continue to be placed on working with managing agents to improve performance although, ultimately, the Corporation has other powers at its disposal to help prevent or mitigate significant underperformance.

AN INCREASINGLY RISKY WORLD

Despite the low level of insured losses, the number of catastrophe events during 2007 was above average. The hurricane season saw 15 named storms, with two category five hurricanes making landfall. A high pressure system off Florida helped steer the hurricanes away from the US coastline. If this high-pressure system had been further north, in its more usual position near Bermuda, the hurricanes could have made landfall in the US, potentially causing significant damage.

The recent trend in weather extremes shows that climate change is already taking effect and an increase in severe windstorm events is expected in the future. The consensus view, including the opinions of scientists at Colorado State University, continues to be that we remain in a cycle of above average North Atlantic windstorm activity.

However, it is not just that windstorm events are becoming more frequent. Their economic impact is also on an upward trend, reflecting an increasing concentration of property values in highly exposed areas. Large-scale migration to coastal areas, particularly in Florida, is a cause for concern and we expect this trend will continue.

The recent UK floods show that the insurance market is susceptible to major natural catastrophes that are not just hurricane related. The increasing frequency of flooding events, and associated losses, in the UK has illustrated the potential benefit of enhanced flood risk assessment capabilities within the Lloyd's market.

During the last decade flood losses have been the largest natural peril affecting the UK insurance industry, with large discrete events in 1998, 2000, 2002, 2004, 2005 and most recently in June and July 2007. Climate change modelling indicates a potential for more frequent and more severe future flooding, due to increases in sea level or changes in the frequency, duration, and intensity of storms.

Lloyd's has developed a flood risk assessment tool. A sophisticated web-based application, it combines flood risk assessment with additional mapping functionality and will improve managing agents' understanding and management of their flood risk exposures over time.

These exposure snapshots will be available quarterly, although the new application will also permit flood risk assessments for individual risk queries in real time.

In other parts of the world, there has been significant typhoon activity in Asia and the Far East, four earthquakes of magnitude 8 or greater, windstorm Kyrill in Northern Europe, storms in Australia and wildfires in California.

CAPITAL MANAGEMENT

It is generally acknowledged that the insurance industry is in a period of downturn in the cycle with diminishing margins. This leads to a risk of the industry seeking to underwrite greater volumes of business in order to meet the return on capital demands of investors.

However, this risk has been partly mitigated by a more robust approach to capital management within the insurance industry; for example, by returning surplus capital through share buybacks or the payment of special dividends. Lloyd's has also responded through recognising and releasing profits as they are earned to avoid surplus or trapped capital and by its adoption of the FSA's Individual Capital Adequacy Standards to ensure capital reflects current market conditions.

MARKETPLACE OVERVIEW
INSURANCE TRENDS CONTINUED

GROWTH IN COMPETITION FROM INTERNATIONAL AND REGIONAL TRADING HUBS

More locations are establishing themselves as centres for the transaction of specialist (re)insurance business. The growth of these hubs is driven by a combination of insurers and brokers seeking both to diversify and to lower their costs, and by favourable local government policy.

While London continues to strengthen its relative competitive position through the reform of market processes, the UK tax regime does not compare favourably with those prevailing elsewhere. This has been cited as one of the reasons why some insurance businesses have sought to relocate or redomicile to low tax insurance centres. The London Insurance Market Review Group, chaired by Lord Levene, has been established to contribute to the work of the Government's High Level Review Group looking at overall City competitiveness. Through this group, Lloyd's will continue to lobby HM Treasury to help create a more level playing field.

LOCALISATION OF BUSINESS FLOWS

As local insurance markets develop and cost pressures drive brokers and insurers to seek more cost-effective distribution channels, the transaction of 'less complex' commercial insurance increasingly remains in local markets.

This, along with the development of specialty insurance hubs, means that efforts must continue to be made to maintain the flow of insurance business into the Lloyd's market. The aim is to make it as easy and cost-effective as possible to bring business to London. The Corporation will also develop options to help market participants to access business closer to its source.

BROKER BUSINESS MODELS

Increasing cost pressures, the demand for transparency and the localisation of business flows are driving brokers to change their business models. In seeking to access local markets more easily and cost effectively, brokers' strategies have implications for the flow of certain types of business into London. Lloyd's will seek to understand these strategies and requirements, which will inform our business development and process reform agenda.

ONGOING REGULATORY CHANGE

The insurance industry will experience significant regulatory change in the coming years, following the introduction of new regimes such as Solvency 2 and amendments to existing legislative frameworks. Lloyd's will continue to lobby local and overseas market regulators to influence these developments.

Through the implementation of the Solvency 2 Directive, the EU will establish a common approach to capitalisation in the insurance industry, based on the alignment of capital with risk. Although implementation has been delayed until 2012, Solvency 2 is welcomed by Lloyd's. The current proposals will allow the continuing use of letters of credit and bank guarantees as admissible assets in order to meet the proposed solvency capital requirements.

CONVERGENCE OF CAPITAL MARKETS AND INSURANCE MARKETS

Capital market interaction with insurance markets is being seen in the form of new product types and new capital providers. Lloyd's needs to consider both the threats and opportunities of this convergence and test potential responses with market participants.

Increasing risk, driven by the rising frequency and severity of natural and man-made events, highlights the importance of the insurance industry and reinforces Lloyd's role as a provider of specialist insurance.

For an overview of developments within each class of business see page 48.

THE LLOYD'S AND LONDON MARKETS' OPERATING ENVIRONMENT

The Lloyd's and London markets continue to face operational challenges. The Lloyd's subscription market and distribution chain bring real benefits, but can also drive a higher perceived administrative burden than other platforms. The costs of operating at Lloyd's are also often perceived to be higher than those elsewhere. While significant progress is being made to address these issues, more needs to be done to ensure Lloyd's ongoing success. Market participants recognise that they must take ownership of this issue and jointly develop solutions to maintain the Lloyd's and London markets' competitive position.

As in all previous cycles, in a phase of downturn, margins in the business are further reduced by increasing acquisition costs. In some lines of business Lloyd's is beginning to see pressure to increase the level of brokerage. This risk could potentially increase if there is further consolidation within the broking community.

Business process reform

2007 saw good progress in making the market a more efficient place to do business. In all three key workstreams – Accounting and Settlement, Electronic Claims Files and Contract Certainty – the market has embraced new systems and shown a determination to change the way it does business.

Challenging targets were set and the market, as it has done many times in the past, rose to the challenge.

By the end of 2007 over 80 brokers were using electronic claims, accounting for approximately 92% of claims by volume. Approximately 88% of in-scope claims and 75% of all claims were being handled electronically. A reduction in settlement time has been reported, improving our service to customers.

After a measured start, use of Accounting and Settlement increased rapidly with 65% of original premium related transactions being processed using the system as at the end of 2007. There is marketwide agreement to the paper service ending in April 2008 for original premium submissions and Xchanging is already reporting a big reduction in the volume of paper transported to and from Chatham for processing.

Progress on contract certainty continued throughout 2007, remaining consistently over 90% and becoming embedded as a 'business as usual' process. The old ways of checking policies have now ceased and a condensed version has been introduced. If a Lloyd's jacketed policy is still required, it can be produced electronically rather than on paper.

For more information on the Three-Year Plan visit:
www.lloyds.com/threeyearplan

THIS YEAR...

PLATFORM OF CHOICE

Lloyd's vision is to be the platform of choice. Our role is to offer the best possible platform for placing specialist insurance and reinsurance risks. The Corporation is working with the businesses in the market to ensure that Lloyd's remains easy to access at competitive cost and that capital providers achieve attractive returns and stable financial performance.

AND NEXT

SPACE INSURANCE

This sector is not only receiving orders for the replacement of existing satellites but is also seeing a lot of interesting new satellite applications. Satellite manufacturers and launch providers are enjoying full order books and the Lloyd's market is well placed to absorb these new risks.

Looking forward, it is projected that approximately 25 new satellites will be launched each year. The number of satellites operating in geostationary orbit has also increased – with the total now standing at around 140 and growing.

Welcome to Lloyd's
Strategic review
Performance
Delivering value
Market results
Society report

STRATEGY
PLATFORM OF CHOICE

LLOYD'S VISION IS TO BE THE PLATFORM OF CHOICE AND WE HAVE A CLEAR STRATEGY TO ACHIEVE THIS.

VISION
TO BE THE PLATFORM OF CHOICE

Lloyd's vision is to be the platform of choice for insurance and reinsurance buyers and sellers to access and trade specialist property and casualty risks.

The publication of the vision in January 2006 signalled the intent to provide a more compelling offer in the face of increasing competition from the global insurance industry, the changing wider external environment and the trends within the Lloyd's market itself.

The starting point for building the optimal platform began with:

- → Assessing the strengths and weaknesses of Lloyd's.
- → Identifying the principal benefits that Lloyd's could offer businesses operating at Lloyd's.
- → Establishing what needed to be done to deliver the benefits set out in a Three-Year Plan.

CHARACTERISTICS
DEFINING LLOYD'S

We have set out certain characteristics that define Lloyd's and how it operates, and help define how the vision is to be achieved. During the current Three-Year Plan period (2008-2010) these include:

- → Lloyd's is a specialist property and casualty subscription market, of which the Underwriting Room is an important element.
- → Mutuality of capital is central to Lloyd's.
- → Lloyd's derives strength from, and continues to welcome, a diversity of businesses and capital providers who wish to participate at Lloyd's.
- → Lloyd's is centred in London, although aims to be open to all specialist insurance brokers, underwriters and providers of capital, irrespective of their physical location.
- → Lloyd's offers a range of distribution channels which allow managing agents to access specialist business.
- → The not-for-profit business model of the Corporation will remain.

BENEFITS
DEFINING THE PLATFORM OF CHOICE

The principal benefits of operating at Lloyd's can be summarised under the following headings. Each of the five benefits has a set of key features, which can be found on page 32.

1 PERFORMANCE FRAMEWORK	An overarching, consistent performance management framework across all key aspects of a managing agent's business, that supports the achievement of superior operating returns as part of an effective enterprise risk model.
2 CAPITAL ADVANTAGES	A capital framework in which the benefits of mutuality demonstrably outweigh the costs and which cannot readily be duplicated outside Lloyd's.
3 SECURITY AND RATINGS	Stable insurer financial strength ratings (currently at least 'A') necessary to attract specialist property and casualty business.
4 MARKET ACCESS	Cost-effective, easy access to the major markets supported by a global brand and licence network.
5 OPERATING ENVIRONMENT	An efficient, cost-effective operating environment that allows managing agents and brokers, irrespective of their location, to deliver excellent service to customers.

THREE-YEAR PLAN
DELIVERING THE BENEFITS

The rolling Three-Year Plan sets out the objectives that we need to meet in order to to deliver the benefits and achieve our vision of becoming the platform of choice.

The first three benefits – Performance Framework, Capital Advantages and Security and Ratings – have broadly been delivered. However, there is still much to do in the areas of Market Access and the Operating Environment.

Success in achieving our goals will be seen in profitable cross-cycle growth. This does not necessarily translate into year on year growth as it may be necessary to contract at certain points in the underwriting cycle.

TESTING AND UPDATING THE PLAN

The Three-Year Plan is reviewed and tested annually against trends and developments affecting the insurance industry and the Lloyd's market. The current Three-Year Plan (2008-2010) continues to work towards the delivery of the five benefits and improving Lloyd's competitive position in the global insurance market.

MANAGING THE CYCLE

A major driver behind our strategy for the 2008-2010 plan period is the current phase in the insurance cycle where we have recently been witnessing softening market conditions.

A strategic priority throughout 2008 and beyond, therefore, is working with managing agents to maintain prudent underwriting discipline. The current Three-Year Plan (2008-2010) sets out the main aspects of the role the Corporation will play in this regard, specifically:

- The provision of services to managing agents to help them carry out their responsibilities.
- Engaging with managing agents as a challenging business partner to help them improve their performance.
- If necessary, where significant underperformance has been identified, applying sanctions to protect the interests of the Lloyd's franchise, policyholders and market participants.

OTHER PRIORITIES
IMPROVING SKILLS AND TALENT

Improving the level of skills to protect and enhance the Lloyd's market talent base is a major priority. A number of initiatives have been put in place, including our new leadership programme developed in conjunction with the London Business School.

For more information on people strategy see page 42.

WORKING CLOSELY WITH THE MARKET

Delivering the strategy involves the Corporation working closely with the businesses operating in the market. We continue to engage with the relevant representative bodies regularly to share plans and build consensus for the best approach to meet the challenges that face us.

A full version of the Lloyd's Three-Year Plan 2008-2010 is available at: www.lloyds.com/threeyearplan

Welcome to Lloyd's
Strategic review
Performance
Delivering value
Market results
Society report

STRATEGY
OUR PROGRESS

FEATURES

1 PERFORMANCE FRAMEWORK

- A performance framework that recognises, reacts to and rewards the relative performance of individual managing agents and raises standards across the market.
- The provision of differentiated levels of support and intervention by the Corporation, depending on the capabilities of each managing agent.
- Business planning tools that enable managing agents, their capital providers and the Corporation to better understand the risks and performance potential of individual businesses.
- The provision of appropriate data and analysis which allows managing agents to benchmark, plan, measure and manage their business.
- A framework for the expert management of complex and subscription claims in order to further enhance the claims handling capability of the market.

2 CAPITAL ADVANTAGES

- A risk-adjusted capital-setting process, based on the FSA's ICAS regime, that reflects the level of exposure of the mutual assets to an individual business and 'commercially prices' this accordingly, taking into account the market's ratings requirements and each managing agent's enterprise risk management capability.
- Capital structures, including mutual assets, that can be tailored and give managing agents the opportunity to benefit from strong ratings and obtain increased returns for their capital providers, compared to trading on a stand-alone basis.
- The cost of maintaining Lloyd's mutual assets targeted to be on average less than 1% of gross written premiums across the insurance cycle.
- A capital framework that actively assists managing agents in accessing flexible sources of capital at a competitive cost.
- Managing agents able to increase their capital resources expeditiously to take advantage of business opportunities as they arise.
- Managing agents able to pay out excess funds through biannual release of profit from their syndicates and capital providers able to reduce their commitment where surplus capital exists.
- Asset admissibility criteria that allow flexibility in how capital is provided, which enhances potential investment returns.

3 SECURITY AND RATINGS

- Within reasonable bounds of expectation, Lloyd's maintains its necessary ratings across the insurance cycle.
- Lloyd's has the capability to survive a '1 in 200' industry-level event and enable managing agents to trade forward with a secure rating.

4 MARKET ACCESS

Trading rights

- A turnkey licence structure that offers access to the major markets in specialist property and casualty risks.
- Co-ordinated relationship management and reporting by the Corporation to regulatory and tax authorities, and proactive government relations, to protect the licences and reduce the burden on individual managing agents.
- Access to world class information and expertise on trading in international markets.

Brand

- A leading global brand and reputation, which helps managing agents to win and retain preferred business.

Market support

- Proactive business development in partnership with managing agents, and a network of international offices that provide support services.
- Access, through the Lloyd's network, to a pool of insurance talent and a choice of service providers and professional firms with insurance knowledge and expertise.

Access

- Managing agents have access to a variety of distribution channels, and brokers are able to place risks with Lloyd's in a simple, cost-effective manner.
- Local underwriting operations in worldwide markets open to local capital providers as well as existing capital providers.

5 OPERATING ENVIRONMENT

Service and cost

- Fast, expert service from quotation through to claims settlement.
- Brokers and other producers are able to deal easily with Lloyd's underwriters, using simple, streamlined processes with costs comparable to other markets.

Distribution

- Flexible operational support underpinning the range of distribution channels.
- Easy access to Lloyd's underwriting expertise and range of insurance products irrespective of location.

Standards and tools

- Operational and data standards that ensure the efficient conduct of business in the market.
- Centrally sponsored, value-added services and tools which support high quality, efficient transaction of business.

PROGRESS	PRIORITIES
→ The standards framework has been completed, covering six key business areas: corporate governance, underwriting, claims, risk management, operational processes and protecting Lloyd's brand and reputation. → Standards are being monitored using managing agent self-assessments and performance reviews. → Gaps in performance are being addressed in partnership with managing agents. → Enhancements are being made to business information tools to improve the Corporation's review of syndicate business plans and performance. → Quarterly reports to managing agents have been upgraded and enable agents to measure syndicate performance against market benchmarks.	→ Ongoing refinement of the standards framework to ensure it remains relevant and adds value. → Complete enhancements to business information tools and their migration to a more robust IT platform. → Commence building a price monitoring tool to improve understanding of underwriting conditions.
→ A more flexible ICA review process and timetable has been introduced for managing agents. → Changes have been made to allow syndicates broadly the same level of flexibility as insurance companies over the investment of premiums. → A 'best practice' Central Fund investment strategy has been implemented. → An additional £500m of subordinated debt has been successfully raised as part of the resources of the Central Fund. → The Central Fund contribution rate has been reduced to 0.5% of written premiums for 2008.	→ Further improvements to be made, where feasible, to the ICA review process. → Regular review of key aspects of the capital framework, with further enhancements to be made where demand exists, taking into account prevailing market conditions. → Review and update the medium-term strategy for the size and composition of the Central Fund.
→ Lloyd's achieved ratings upgrades to 'A+' from Standard & Poor's and Fitch Ratings in 2007. → A.M. Best affirmed its 'A' excellent rating, citing the market's improved central solvency capital, declining exposure to reinsurance credit risk and enhanced risk management.	→ Maintain ratings at the desired level, further enhancing Lloyd's reputation as a secure and stable market to place (re)insurance business. → Test current ratings levels with stakeholders to ensure they continue to meet the market's needs.
→ Lloyd's Reinsurance Company (China) Limited opened and is supported by 11 managing agents as at the end of 2007. → Significant growth in the Lloyd's Asia platform (in Singapore). → Appointment of a country manager for India. → Upgrading of Lloyd's online global trading, regulatory and taxation advice. → New York and Florida are responding to Lloyd's lobbying calls to remove discriminatory reinsurance collateral rules. → Streamlining of Lloyd's broker accreditation and coverholder approval processes. → Thought leadership programme in place. Reports published on climate change, terrorism and political risk.	→ Develop, maintain and exploit Lloyd's trading rights, eg: – Develop Lloyd's trading position and local presence in key territories such as India, Brazil and Middle East. → Offer market support to exploit business opportunities, eg: – Lloyd's overseas office network to be aligned to support business development. → Continue to promote Lloyd's brand and reputation, eg: – A targeted marketing programme that supports Lloyd's business development. → Develop access routes, eg: – Deliver improvements in service company and coverholder distribution channels.
→ Electronic claims file (ECF) repository has been put in place to speed up the processing of claims. Good progress has been made with its take up by the market with 88% of in-scope claims being handled electronically as at the year end. → An accounting and settlement (A&S) repository has been developed that enables documents relating to premium transactions to be transferred between market participants more swiftly and with greater control than the current paper based processes. As at the year end, 65% of original premium related transactions were processed using the repository. → Lloyd's has met the challenge of embedding contract certainty as business as usual and throughout 2007 met the target of 90% set by the Market Reform Group. The rate achieved at the end of 2007 was 95%. → Lloyd's online Quality Assurance Tool has been designed to assist managing agents with the accuracy and consistency of risk placement information. → Lloyd's wordings repository has been made available for use by market participants.	→ Promoting excellent service and reducing costs, eg: – Work with the market to ensure 100% usage of ECF and A&S repositories. – Develop further solutions to simplifying the processes involved in conducting business at Lloyd's. – Work with the market to prioritise areas of potential for improving the placing process. → Improve distribution channels, eg: – Improve central support to distribution channels in key territories such as Lloyd's Asia platform. → Deliver standards and value added business tools to the market, eg: – Work with ACORD to develop further information standards.

Welcome to Lloyd's
Strategic review
Performance
Delivering value
Market results
Society report

KEY PERFORMANCE INDICATORS

MEASURING OUR YEAR-ON-YEAR PERFORMANCE: SOME POSITIVE TRENDS.

Key performance indicators (KPIs) are important measures used by the management team for evaluating both the market and the Corporation's performance. Lloyd's has a range of metrics used internally for tracking and performance management. Those shown here best illustrate Lloyd's financial performance and progress in delivering its strategy. Some of the measures may become more sophisticated and change over time as more comparative information becomes available. Directional trends are important, even in a market made up of independent businesses.

MARKET PERFORMANCE

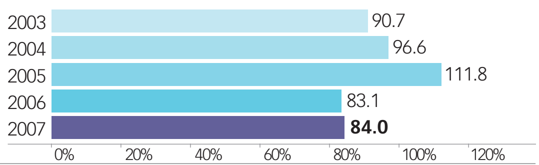
To find out more about the market's performance see page 48.

Combined ratio

Definition The combined ratio is the ratio of net incurred claims and expenses to net earned premium. Any figure that is less than 100% signifies a technical underwriting profit.

Rationale Headline financial indicator for measuring underwriting performance.

Progress A combined ratio of 84.0% reflects a small increase on 2006. However, underlying performance across all major classes of business remains strong (see page 49). 2007 benefited from strong prior year reserve releases.

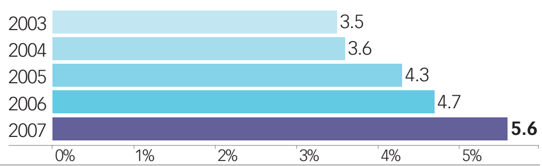


Investment return

Definition Realised and unrealised return on investments as a percentage of total investments.

Rationale Investment return can have a significant impact on overall profitability for insurers/reinsurers.

Progress Return on investments of 5.6% reflects the highest return for five years. Having largely avoided sub prime losses, bond investments generally benefited from falling yields (see page 50).



STRATEGIC PERFORMANCE

To find out more about our strategy see page 30.

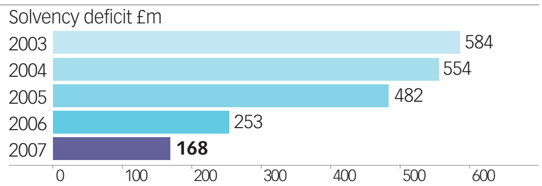
1 PERFORMANCE FRAMEWORK

Solvency deficit

Definition The aggregate shortfalls for all members where the member's assets are insufficient to cover its underwriting liabilities and member capital requirement.

Rationale Indication of success at mitigating Central Fund exposure.

Progress The fall in solvency deficits reflects improved underwriting results for insolvent members and no failures since 2003.

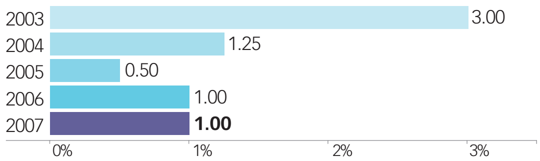


Cost of mutuality

Definition Central Fund contribution rate charged to members. This excludes the syndicate loans charged in 2005 and 2006, and subsequently repaid in 2007.

Rationale Medium term cost indicator for the operational efficiency of mutually available assets.

Progress The 2008 contribution has been reduced to 0.50% following a review of capital requirements leading to a decrease in the cost of mutuality for members.



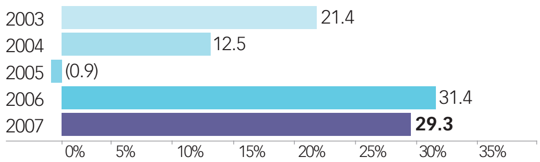
2 CAPITAL ADVANTAGES

Pre-tax return on capital

Definition Result on ordinary activities before tax as a ratio of average capital and reserves held.

Rationale Indicates the capital efficiency of Lloyd's and the potential to achieve higher returns in comparison to other insurance markets. The goal of the Franchise Board and Council is to support the market in monitoring cross-cycle returns to all capital providers.

Progress 29.3% reflects a second successive year of excellent results.



3 SECURITY AND RATINGS

Financial Strength Rating

Definition Lloyd's strengths and robust capitalisation evaluated by the world's leading insurance rating agencies.

Rationale Indicates the strength of Lloyd's rating offering.

Progress Ratings targets for 2007, initially set in 2003, were met during the year with upgrades from S&P and Fitch.

	Actual	Target
Standard & Poor's	A+	✓
Fitch Ratings	A+	✓
A.M. Best	A	✓

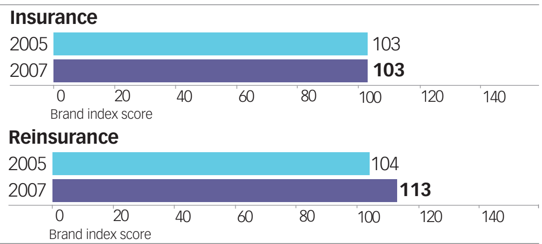
4 MARKET ACCESS

Brand strength

Definition Non-financial indicator – Independent survey of brokers and policyholders run biennially. The brand 'health score' is a combination of scores for awareness, familiarity, favourability, trust and endorsement. The measure is an index and tracks relative changes in perception over time.

Rationale A leading global brand and reputation helps managing agents win and retain preferred business.

Progress Lloyd's has maintained strong brand health in the insurance sector (ranked 2nd out of the brands monitored). In the reinsurance sector the Lloyd's brand has grown in strength since 2005, particularly in relation to awareness, favourability and endorsement.



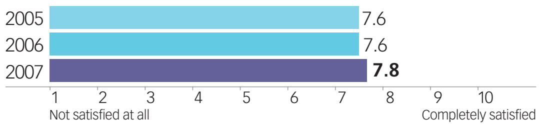
5 OPERATING ENVIRONMENT

Customer satisfaction levels

Definition Non-financial indicator measuring satisfaction levels of brokers, coverholders, insurance and reinsurance policyholders with Lloyd's overall service, taken from an independent survey.

Rationale Recognition of business process reform and its importance to the end customer.

Progress Satisfaction with service from the Lloyd's market has increased from 7.6 in 2005 and 2006 to 7.8 in 2007. The increase is driven predominantly by improvements in satisfaction with speed of contract documentation, speed of quotation, processes to notify of a claim and speed of claims payment.

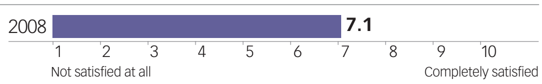


Managing agent satisfaction levels

Definition Non-financial indicator measuring Lloyd's managing agents' overall satisfaction levels with Lloyd's service taken from an independent survey.

Rationale Recognition of managing agents as customers of the Lloyd's platform and the importance of tracking their satisfaction.

Progress The score of 7.1 is viewed favourably. This is the first time this particular indicator has been tracked and it will provide a benchmark for future years.



For more information on Lloyd's 360 Risk Project
visit: www.lloyds.com/360

ALERT...

EMERGING RISKS

As a market with an appetite for risk, we are well aware that the risk landscape is changing. Terrorism, political violence, climate change and liability issues such as nanotechnology, are the more obvious emerging risks. Acting on these global developments, we have established the 360 Risk Project, created an Emerging Risks Team and taken a leading role in the industry body Climate Wise. We are also running a programme to consolidate diverse risk data using Google Earth to map global risks.

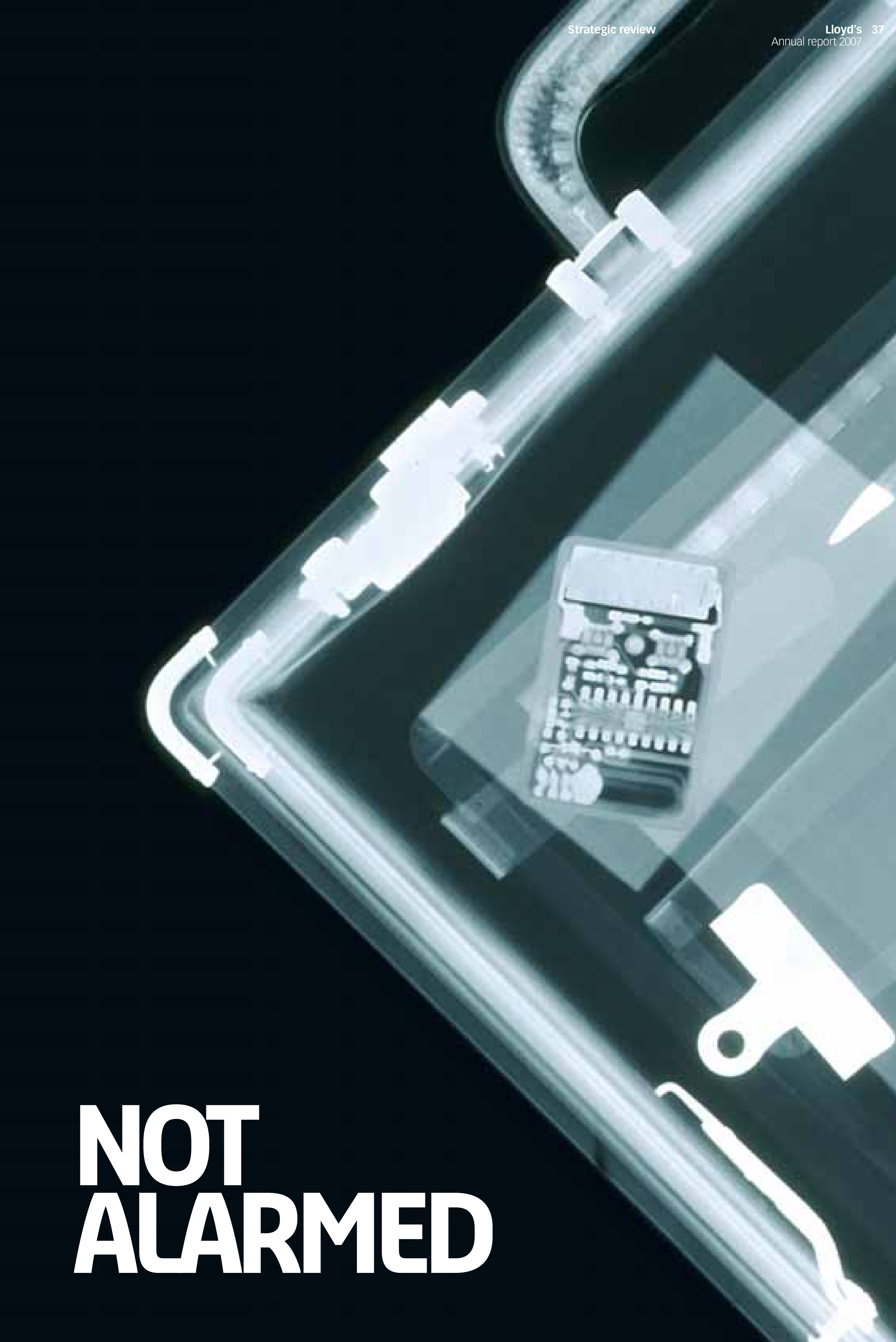
360 RISK PROJECT – DRIVING THE DEBATE ON EMERGING RISK

Lloyd's 360 Risk Project is driving the debate on emerging risk. Drawing on the knowledge of experts from the market and around the world, we're working to help professionals – whether CEO's and risk managers or their insurance intermediaries and consultants – to keep on top of the emerging issues.

Working closely with specialist teams across the Lloyd's business, the project focuses on the three core subjects of climate change, terrorism and political violence and corporate liability risk.

Through a programme of research and analysis on specific risk issues, we have investigated issues such as the impact of home-grown terrorism for companies in the UK and Asia. And by developing an online information and news resource, we have unlocked discussion on global stability and global warming with the world's business and political leaders.

Welcome to Lloyd's
Strategic review
Performance
Delivering value
Market results
Society report



NOT ALARMED

RISK MANAGEMENT

WHILE HELPING OTHERS MITIGATE THEIR RISKS, WE EFFECTIVELY MANAGE OUR OWN.

Risk is managed at Lloyd's via a comprehensive risk management framework. For the Corporation, the assurance processes of Internal Audit, Compliance and Financial Control play an important role.

Managing risk is considered to be a responsibility for all Lloyd's employees within the Corporation and the market. For Corporation employees, this is included as a key capability within the employee performance management framework. Employees are assessed against this capability in their annual performance appraisals.

The risk management framework aims to pull together the key risks facing the market and the Corporation and allows these risks to be assessed on a common basis. It seeks to provide assurance to the Executive Team and Franchise Board that key risks are being identified and managed effectively. The risk management framework has a dual focus – syndicate and managing agent level risks are monitored through the 'Syndicate Risk Matrix', so that key issues are analysed and considered by senior Lloyd's managers; and Corporation specific and overall Lloyd's market level risks are addressed through the 'Lloyd's Risk Framework', which is subject to oversight by the Lloyd's Risk Committee. These channels for managing risk are discussed in detail in the following pages.

For information on financial risk management and treasury policies see page 110.

THE SYNDICATE RISK MATRIX (SRM)

The SRM is a tool used to bring together syndicate level risk and performance issues and enable coordinated decision making and action planning. Syndicates are assessed against a number of key risk and performance indicators gathered from across the Corporation. This information is gathered in the SRM and discussed on a structured basis at monthly meetings of key senior Lloyd's managers which focus on individual syndicates or issues of concern, and on determining and monitoring appropriate actions.

Key areas monitored include compliance with underwriting standards, adequacy of the control environment, regulatory compliance and capital adequacy. Relevant issues identified at the monthly meetings are shared with the Executive Team and also with the FSA, in order to avoid unnecessary duplication of supervisory activities. These issues are also fed into the Franchise Risk and Control Assessment (discussed in the following pages). The key aim is to obtain a wider understanding of syndicate and market wide risk and performance issues, resulting in coordinated management, decision making and action planning.

For information on insurance risk see page 16.

KEY RISKS AND UNCERTAINTIES

RISK	IMPACT	MITIGATION
Failure to manage Lloyd's response to the insurance cycle.	→ Lloyd's insurers suffer losses and erode their capital base through inadequate pricing.	→ Agreement of Business Plans and Individual Capital Assessments. → Close interaction with managing agents to ensure prudent selection and pricing risks in accordance with Business Plans. → Implementation of enhanced performance management information tools.
Failure of Business Process Reform (BPR) initiatives to deliver desired level of change to the Lloyd's market.	→ Lloyd's is unable to maintain its competitive position and deliver process improvements that create a more efficient marketplace.	→ Franchise Board oversight and sponsorship of BPR initiatives to drive and ultimately mandate the adoption of key processes in the market. → Barriers to uptake of reform initiatives identified and overcome. → Articulation of the end vision under development to generate momentum in the market.
Failure to adequately manage levels of underwriting exposure.	→ Losses incurred are outside expected thresholds, resulting in potential failure of members and subsequent Central Fund exposures.	→ Widely acclaimed approach to catastrophe exposure management through Realistic Disaster Scenario framework. → Review of managing agent compliance with exposure management standards and support provided to the market. → Lloyd's Emerging Risk team working closely with the market, wider insurance industry and academia to examine emerging risks and take steps to mitigate risk.
Failure to set and implement appropriate distribution strategy.	→ Lloyd's fails to attract and/or retain appropriate business.	→ Working with brokers to ensure that the ease of placing business though Lloyd's international platforms is equivalent to its competitors by 2010. → Use of international platforms as distribution channels for Lloyd's products and solutions. → Strengthening presence in high growth emerging markets like Latin America, Middle East and Asia.
Failure to respond effectively to major financial systemic failure (eg the 'Credit Crisis').	→ Lloyd's suffers increased insurance liabilities, decreased asset values and/or capital constraints.	→ Underwriting Guidelines in place to control exposure to insurance liabilities. → Asset eligibility rules in place to control exposure to capital losses or asset value fluctuations. → Close liaison with the market to identify and control insurance liabilities and exposure to asset fluctuations arising from major financial events.
Failure to respond effectively to major operational disruption.	→ The Lloyd's market is unable to recover and operate following a significant external event resulting in loss of market share or the development of alternative methods of placement that undermine future viability of Lloyd's.	→ Detailed business continuity plans maintained and regularly tested. → Emergency Response Team convened on regular basis for scenario based rehearsals. → Annual market-wide business continuity exercise and crisis management tests undertaken. → Regular review of information technology environment against best practice to ensure high levels of stability and security.
Failure to attract, develop and retain appropriate people.	→ Lloyd's is unable to deliver on its strategic objectives, operate in an efficient manner or optimise its competitive position.	→ Leadership development programme established to support the development of high potential individuals. → Corporation wide programme in place to support individuals in developing skills in leadership, decision making and response to organisational change. → Graduate scheme established to attract appropriate talent to Lloyd's.
Failure to maintain information technology infrastructure at a level that enables delivery of Lloyd's objectives.	→ Lloyd's is unable to perform operational functions or provide effective market oversight.	→ Regular review of information technology environment against best practice to ensure high levels of stability and security. → Formal IT prioritisation exercise and review of governance undertaken. → All material projects reviewed by cross-directorate committee.

RISK MANAGEMENT CONTINUED

THE LLOYD'S RISK FRAMEWORK

The Lloyd's Risk Framework is managed by the Risk Analysis team and overseen by the Risk Committee, which was established during 2006 as a sub-committee of the Executive Team. The function of the Risk Committee is to provide assurance to the Executive Team and the Franchise Board that Corporation and Lloyd's market level risks are identified and managed in accordance with approved risk policy and appetite. Although the Risk Committee is not intended to consider risks within individual syndicates or managing agents, any risks identified that are relevant at Lloyd's market level are discussed by the Risk Committee.

The Risk Committee oversees the identification, assessment and management of risk process, as follows:

RISK IDENTIFICATION

Risks are identified through a number of risk information channels including the Franchise Risk and Control Assessment (FRCA) process, environment scanning, the Emerging Risk team and the Executive Team/Franchise Board risk assessments. The risks are documented and managed using the Lloyd's Risk Register.

The FRCA is a continuous self-assessment process, which is embedded within the business and is subject to three or four formal updates each year. This process is coordinated and facilitated by the Risk Analysis team and is the main channel for the identification of new risks, or changes to the profile of known risks.

Environment scanning for significant risk issues is conducted on an ongoing basis by the Risk Analysis team and is included as a standing agenda item for all Risk Committee meetings. This process includes a systematic review of press publications (provided by an external media company), websites and internal communications. It also includes ongoing liaison with internal and external stakeholders.

The Emerging Risk team forms part of the Franchise Performance Directorate. The remit of the team is to consider new risks (for example, nanotechnology) and existing risks where new information suggests the level of risk is changing unexpectedly (for example, the impact of climate change on flood risk). The Emerging Risk team aims to ensure such early warning information is captured and effectively utilised going forward. As the nature of the risks facing Lloyd's is dominated by insurance risk, this is the primary focus of the Emerging Risk team. However, where emerging risks impact other risk categories, the team also considers the wider implications of these risk events.

The annual Executive Team and Franchise Board Risk Assessments were conducted on 25 September 2007 and 29 October 2007 respectively. The primary purpose of these exercises was to identify the key risks facing Lloyd's and ensure that these risks and associated controls/actions were adequately articulated in the Risk Register. In order to drive additional value from the sessions, the format for the 2007 exercises was amended to provide the Executive Team and Franchise Board with the specific opportunity to consider new mitigating actions for the reduction of residual risk in key areas.

A description of the current 'key risks and uncertainties' to Lloyd's, their potential impact and a summary of mitigation activities can be found in the table on page 39.

RISK ASSESSMENT

All risks identified by the processes outlined previously are monitored using the FRCA process. Each risk is allocated an appropriate owner, who is the key contact for the management of that particular risk, with the support of a network of control and action owners across the Corporation. Risk is assessed by the risk owner, under scrutiny by the Risk Committee, in terms of the potential impact on Lloyd's should it occur, and the perceived probability of occurrence within a 12 month time horizon.

Risk assessment and control measurement is independently verified and challenged using a number of risk information flows. This not only establishes a robust challenge to the self-assessment process, but assists in ensuring a 'coordinated view' of risk and an integrated approach to risk management. The key risk information channels are as follows:

→ **Internal Audit:** The Internal Audit team utilises the Risk Register content to plan and conduct audits throughout the year. The Risk Analysis team uses audit output to challenge risk and control self-assessments.

→ **Compliance and Financial Control:** The Compliance and Financial Control departments jointly conduct a monthly process to capture internal control failures and any breach of compliance with legislation or regulation across the Corporation.

→ **The Syndicate Risk Matrix:** Although the matrix is designed to support the monitoring of risk at syndicate level, the risk data captured may be relevant at Lloyd's market level. As such, the data is analysed and fed into the Risk Committee reporting process to ensure consistency between the two key risk reporting channels.

RISK MANAGEMENT AND MITIGATION

The risk is assessed on a 'residual' (after controls) basis in terms of impact and probability. A risk appetite is determined for each risk, which is articulated as 'target' risk and probability scores in the Risk Register. Where residual risk exceeds target, actions are generated and recorded in the Risk Register. The FRCA process then tracks actions by key milestones or deliverables to ensure residual/target gaps are reduced within desired time frames.

The results of the formal FRCA updates are reported to, and agreed by, the Risk Committee on behalf of the Executive Team. The Risk Committee uses these results to maintain oversight of the risks in order to provide assurance to the Franchise Board about the effective management of risk and the maintenance of a robust system of internal control.

INDIVIDUAL CAPITAL ASSESSMENT (ICA)

The risk management framework is also used in the calculation of the Lloyd's ICA, which is the level of capital resources required to withstand a 1-in-200-year event over a three-year time frame. Each risk within the risk framework is assessed to ensure it is treated appropriately from a capital perspective; as part of the stochastic model, as part of the stress and scenario testing or by being controlled by alternative methods.

While there is considerable stochastic modelling of insurance risk, and some other elements of risk such as credit risk, the risk framework was used to identify relevant stress and scenario tests for risks that were outside the stochastic model. The scenario tests that followed were based on potential events where one or more of the risks in the framework could occur, and assessed the potential loss from a significant event. The results were fed into the calculation of the Lloyd's ICA.

PEOPLE STRATEGY

WE ARE WORKING HARD TO ATTRACT TALENT AND RELEASE POTENTIAL.

2008 INITIATIVES

Attracting talent, releasing potential and rewarding performance are central to the Corporation's people strategy. The Corporation also works with market firms on a number of people strategy initiatives. The major ingredients of the 2008 programme will be:

Raising Lloyd's profile in the 'quest for talent' by vigorously promoting Lloyd's employment brand.

Continuing to improve leadership skills in partnership with the market and London Business School.

Realising potential by promoting career ownership and improving career development within the Corporation.

Supporting the programme of organisational development and culture change within the Corporation.

Introducing a new Lloyd's Performance Plan to align the interests of all Corporation employees with capital providers by linking an element of reward to market profitability.

Graduate scheme

Following research that showed almost 90% of graduates would not consider a career in insurance and a perceived skills shortage in the industry, Lloyd's re-entered the graduate market after an 11 year absence. After a successful recruitment campaign in 2007, and a rigorous selection process, ten highly talented graduates will join the Corporation in September 2008. During the 18-month programme, they will develop a holistic understanding of how the Lloyd's market and the Corporation operate. They will also study for the Lloyd's and London Market Introductory Test (LLMIT) and Certificate in Risk Management.

Recruitment began in October 2007, with a new brochure and website coinciding with the start of the university recruitment season. Much work was also carried out to establish Lloyd's on campus, ranging from attendance at careers fairs and a presentation to careers advisers from top-tier universities.

The Lloyd's graduate campaign was awarded three RAD (Recruitment Advertising) awards – Best Employer Website, Best Graduate Campaign, Best Work of the Year.

For more information on Lloyd's Graduate Scheme visit: www.lloyds.com/graduates

In an increasingly competitive world, it is the quality of thinking that gives an edge, an idea that creates advantage and a new technique that solves a problem. The nature of Lloyd's business means that success rests on intellectual capital. People are the ultimate source of value and strategy is no more than a good intention until turned into reality by people.

A CONTINUING PROGRAMME OF CHANGE

During 2006, the Corporation embarked on a substantial programme of change to improve leadership, raise standards, identify talent, nurture potential and release ability. The programme aimed to reinforce the cultural shift required by the Corporation as the Lloyd's market's strategic business partner.

2007 PROGRESS

IMPROVING LEADERSHIP SKILLS

The Corporation of Lloyd's management team was formed to support the CEO and Executive Team in providing leadership across the Corporation and several events were held to help them assume this role.

A cutting-edge leadership programme was designed in partnership with the London Business School for participants from the market and Corporation. Based on three intensive modules, it takes participants from the personal dimensions of their own leadership style and capability through to the organisational dimensions of leading change and shaping corporate culture. The first cohort of 18 started the programme in November and further cohorts are planned for 2008.

ALIGNING RESOURCES WITH PRIORITIES

Significant restructuring during the year helped to align resources with changing priorities and create greater organisational flexibility. This included the creation of two new directorates in the Corporation with new directors to lead them. Sue Langley became Director, Market Operations and North America and Jose Ribeiro joined as Director, International Markets and Business Development. Major restructuring and recruitment was carried out within and across directorates to bring functions more closely into line with business requirements, raise standards and improve co-ordination and collaboration.

IMPROVING COMMUNICATION

Regular staff forums took place throughout 2007 at which the CEO and Executive Team briefed Corporation staff and answered questions on business progress and other issues. These were supplemented by CEO lunches where small groups of Corporation employees spoke directly with the CEO.

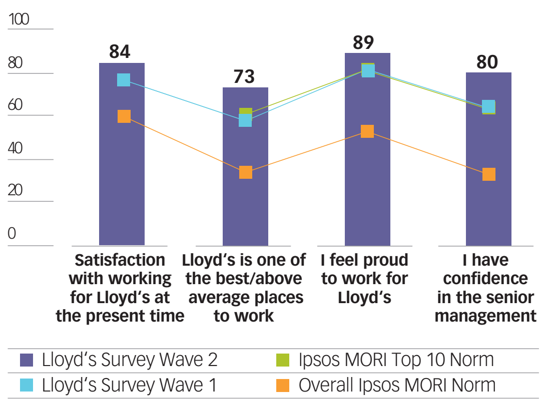
Regular team meetings were conducted at every level of the Corporation, ranging from large 'town hall' meetings for upwards of 100 people to small 'work in progress' sessions of a dozen or less.

The intranet (C-net) was further developed during the year to provide information rapidly to employees.

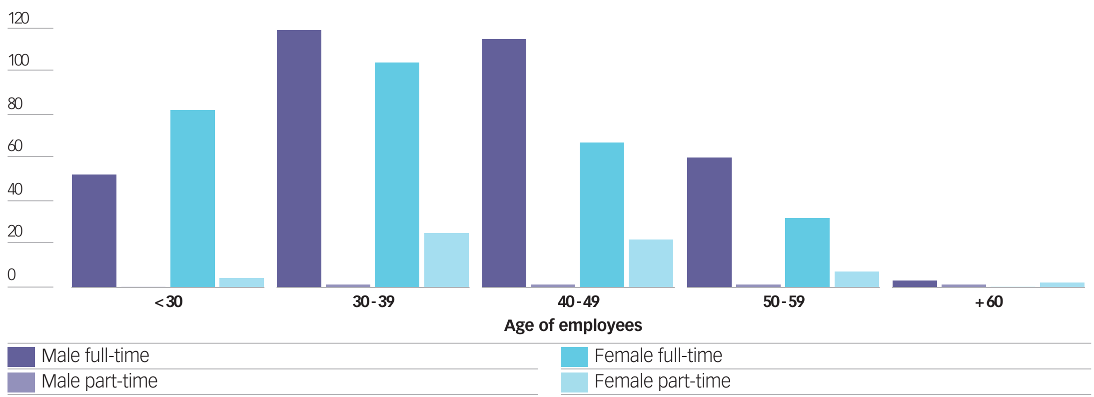
EMPLOYEE OPINION SURVEY

The Corporation undertakes an annual staff opinion survey in conjunction with Ipsos-MORI. The most recent survey achieved a high response rate of 88% (in comparison to 83% the previous year). Staff satisfaction and engagement has improved over the two surveys, the positive results surpass the Ipsos-MORI norms and are in line with the top 10 companies Ipsos-MORI monitor. The survey also identifies areas for continued improvement and will be repeated on an annual basis to monitor performance and progress.

Employee opinion survey



UK employee profile (number of employees)



PEOPLE STRATEGY CONTINUED

PROMOTING DIVERSITY

Complementing formal policies, the Corporation has an active diversity group, sponsored by Jose Ribeiro, Director, International Markets and Business Development. The group promotes an environment of inclusion where all people are valued and respected for their individual abilities, skills and experience and where difference is respected as a potential asset. During 2007, the group continued its agenda of encouraging discussion on diversity issues, communicating latest initiatives and research results through the diversity website and sharing ideas and best practice across the Lloyd's market. Drama based training was trialled at the end of the year with senior managers and is being extended to the whole organisation in 2008.

A NEW GRADUATE SCHEME

In October 2007, the Corporation launched Lloyd's recruitment campaign to attract ten graduates. The scheme, starting in September 2008, is designed to develop a talent pipeline of the brightest graduates, increase awareness of Lloyd's as an attractive place to work and build stronger networks between the market and Corporation.

EXPANDING THE PACESETTERS PROGRAMME

Launched in 2006, and continued throughout 2007, this programme is aimed at Corporation employees. Its objectives are to contribute to organisational change by breaking down cultural barriers, developing networks and challenging people to think and act in new and different ways. At the end of 2007 over 50% of employees had attended and 80% of those attending said it exceeded or fully met their expectations. A small working group has now been formed to take forward the ideas generated by the programme and ensure that momentum is not lost.

LEARNING AND DEVELOPMENT

The Corporation continues its strong commitment to learning and development. This aims to make sure we have the skills, values and capabilities to achieve business objectives, meet FSA requirements and improve individual performance. Employees are actively encouraged to obtain relevant qualifications and financial and other support is available. A system of internal job advertising is in place so that as many vacancies as possible are filled internally.

A NEW PERFORMANCE MANAGEMENT SYSTEM

At the start of 2007 a more rigorous approach to objective setting and evaluation was introduced for Corporation employees. Bonus ratings are now used to measure performance in two dimensions: performance against objectives and performance against the behaviour required to deliver success (values and capabilities). The new bonus approach increased the proportion of variable pay available and enabled top performing employees to increase their bonus.

WORKING ENVIRONMENT

The project aimed at redesigning the working environment, announced in 2006, is on-target. By the end of 2007, 41% of the Corporation was in redesigned space. By the end of 2008, all Corporation staff will be in a bright, modern, open-plan environment that supports and encourages collaborative ways of working.

PaceSetter programe

The PaceSetter programme gives everyone in the Corporation the opportunity to learn about leadership and the part they can play in improving the way Lloyd's works. From an initial 20, the number of participants at the end of 2007 had grown to over 400, with registrations still being received.

Individuals and teams are adopting the principles and applying them across the organisation. New initiatives have also been introduced by staff, building on the PaceSetter message that everyone can make a difference.

The programme has unearthed a new level of creativity and desire for involvement in the changes taking place at Lloyd's. With support from senior management and the Executive Team, the momentum and benefits should continue to grow.

CORPORATION EMPLOYEE DEMOGRAPHICS

Employees are employed by the Corporation in the UK and by overseas subsidiaries. The demographic profile for all employees, which includes both permanent and contracted staff, is shown below:

	2007 Number	2006 Number
UK	**694**	668
USA	**30**	29
Canada	**3**	3
Asia	**31**	25
Europe	**33**	31
Africa, Australasia, Central and South America	**7**	7
	798	763

UK permanent employee turnover and absence	2007 Number	2006 Number
Total employees as at 1 January	**668**	669
Number of joiners (hires, rehires and insourced)	**130**	136
Number of voluntary leavers	**(64)**	(45)
Number of involuntary leavers (redundancies, retirements) – Kinnect Limited	**–**	(42)
– Other	**(40)**	(50)
Total UK employees as at 31 December	**694**	668

	%	%
Total turnover	**15.0**	20.5
Turnover excluding Kinnect Limited	**15.0**	14.2
Industry average turnover	**14.5**	16.1
Voluntary turnover	**9.2**	6.7
Industry average voluntary turnover	**9.9**	10.3
Absence	**2.1**	1.9
Industry average absence	**3.2**	2.4

The Corporation regularly monitors the level of staff turnover and absence against suitable industry benchmarks and corrective action is taken if required. During 2007, UK voluntary staff turnover, excluding retirements and redundancies, continued to be below the industry average at 9.2%, as did the sickness absence record at 2.1%. The Corporation considers the performance against these benchmarks in a fast-moving environment to be very positive.

The Corporation's UK employee segmentation and profile as at 31 December 2007 is shown below:

UK employee segmentation	Executive		Head of Function		Manager		Professional/ Technical		Admin		Total	
Figures in numbers	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006
Male	**6**	7	**29**	31	**131**	119	**147**	131	**35**	39	**348**	327
Female	**1**	–	**7**	8	**69**	65	**147**	136	**122**	132	**346**	341
Total employees	**7**	7	**36**	39	**200**	184	**294**	267	**157**	171	**694**	668
Figures in years	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006	**2007**	2006
Average age	**50**	49	**46**	45	**42**	42	**38**	38	**37**	37	**39**	39
Average service	**4**	5	**8**	8	**9**	9	**8**	9	**6**	6	**8**	8

The segmentation as shown above includes 4 male and 60 female part time employees as at 31 December 2007 (31 December 2006: 4 male; 56 female).

ON PAPER...

IMPROVING BUSINESS PROCESSES

One of Lloyd's goals is to remove the vast majority of paper from the back office and we are making good progress in achieving this objective. The Lloyd's market must be easy to do business with and among the benefits outlined in the Three-Year Plan is the development of processes to support the cost-effective, efficient transaction of business.

ONLINE

CRYSTAL

Crystal is Lloyd's online business tool that provides Lloyd's brokers and underwriters with quick and easy access to the information they need to manage their international regulatory and tax requirements. Users can access an overview of the international requirements or tailor searches to find the specific information they require. Crystal also provides the market with high level trading information via an interactive map and guidance on risk location and multi-jurisdictional policies.

PERFORMANCE

HOW THE MARKET PERFORMED IN 2007

2007 PERFORMANCE REVIEW

2007 highlights

- Lloyd's achieved a profit before tax of £3,846m (2006: £3,662m) and a combined ratio of 84.0% (2006: 83.1%) reflecting continued strong performance.
- Return on syndicate investments at 5.2% (2006: 4.2%) the highest for five years.
- Overall surplus on prior years of £856m (2006: £270m) as claims develop within projections for the third successive year.
- Pre-tax return on capital of 29.3% (2006: 31.4%) reflecting a second successive year of excellent results.

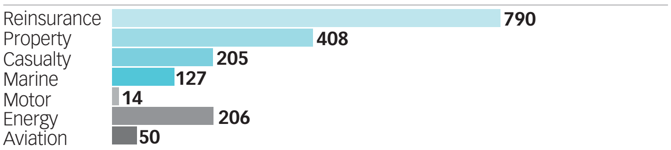
2007 combined ratio*

90.5% Accident year

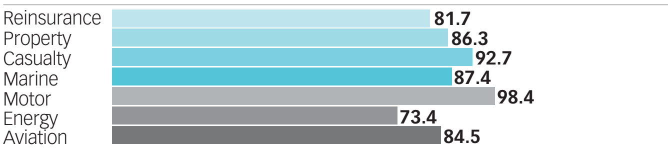
(6.5%) Prior year reserve movement

84.0% Calendar year

Underwriting results by class
£m



Combined ratio by class
%



The Lloyd's market reported a second successive year of excellent results. The underlying performance across all major classes of business in the Lloyd's market remains strong, with the level of catastrophe losses below the long-term average. The strength of the balance sheet also contributed to the results through surpluses arising on established claims reserves and an improved investment performance.

*See Glossary on page 152.

The overall combined ratio includes central adjustments in the technical account in respect of transactions between syndicates and the Society as described in notes 2 and 8 to the PFFS (pages 73 and 77). The combined ratios and results for individual classes of business do not include these adjustments as the market commentary for each class reflects trading conditions at syndicate level as reported in syndicate annual accounts.

2007 PERFORMANCE

Gross written premium for the year was £16,366m (2006: £16,414m), a decrease of 0.3%. While 2006 was a tale of two markets, the hardening in wind-exposed catastrophe business in the US has largely ceased and in 2007 Lloyd's saw evidence of concessions on rates across all major classes of business.

The US is the single largest market for Lloyd's and the weaker US dollar during the year means that lower written premiums are reported in converted sterling compared to 2006.

ACCIDENT YEAR PERFORMANCE

Lloyd's achieved an accident year combined ratio of 90.5% (2006: 85.2%).

The underlying combined ratio, excluding catastrophes, of 86.7% (2006: 84.8%) has benefited from the strong underwriting conditions experienced in 2006, with premiums continuing to be earned throughout 2007. This is an impressive result considering the softening market conditions that were experienced in 2007.

Underlying performance excluding catastrophes
%

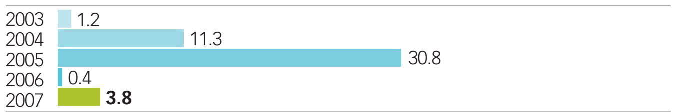
Combined ratio

The turmoil from the US sub-prime crisis has dominated headlines and the impact on the insurance industry as a whole continues to provoke significant debate, with a wide range of estimates being quoted, although the full effect is unlikely to be felt until at least the latter stage of 2008.

So far Lloyd's has received a small number of claims notifications and the restrictions on the level of financial guarantee business that may be written are likely to limit the potential exposure to credit insurance and the reinsurance of bond insurers to negligible levels. Lloyd's continues to monitor the situation as it develops but does not expect to have a significant sub-prime exposure.

However, with the variety of class actions that could be triggered and the potential for repercussions beyond the US, this is clearly an area of great uncertainty and Lloyd's expects to have a clearer picture of potential exposures as the issue develops. The Franchise Performance Directorate will continue to work closely with the market to identify and manage potential exposures.

Catastrophes
%



Combined ratio

The accident year performance also benefited from a relatively low level of catastrophe losses during the year, with the most significant to the market as a whole being the UK floods and the European Windstorm Kyrill.

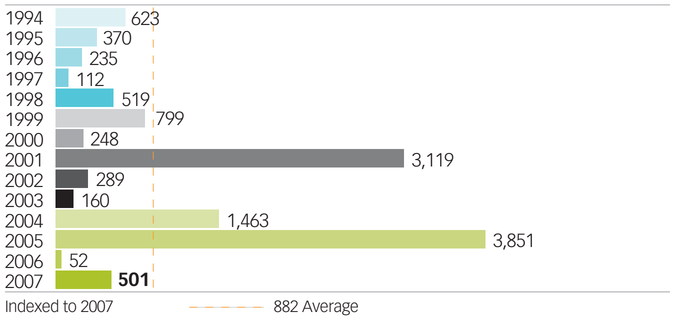
The severe flooding in the UK in June and July has resulted in industry loss estimates at around £2.2bn. However, Lloyd's has a relatively small proportion of the overall market for direct UK property business and as a result of retention levels, the main impact of this loss will be borne by the primary insurers. The current estimate of the impact to the Lloyd's market is a net loss of £215m, including provision for claims incurred but not reported.

2007 PERFORMANCE REVIEW CONTINUED

Industry estimates for Windstorm Kyrill, which swept across northern Europe on 18 January, are around £3.0bn. The current estimate of the impact to the Lloyd's market is £85m.

While the impact of catastrophes on the combined ratio of 3.8% (2006: 0.4%) is greater than the previous year, the level of catastrophes was below the long-term average for the Lloyd's market, as can be seen in the chart below.

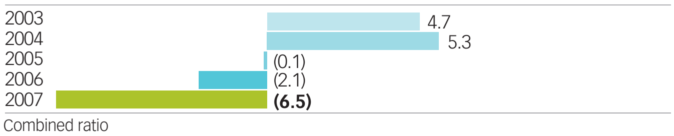
Lloyd's catastrophes: net ultimate claims
£m



PRIOR YEAR RESERVE MOVEMENT

Prior year reserve movement has improved the combined ratio by 6.5% (2006: 2.1%). This is the third successive year of prior year surpluses and encouragingly releases are being seen across all major classes.

Prior year reserve movement
%



The emerging surpluses arise mainly on claims reserves established for business written during 2002-2006, where claims development remains benign and well within expectations.

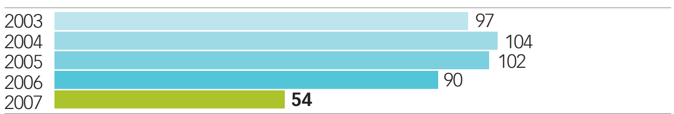
Claims estimates for the 2005 US hurricanes are showing signs of stabilisation and development on the longer-tail business written in the soft market conditions of 1997–2001 continues to be within expectations.

Despite ultimate net claims estimates for the 2005 US hurricanes being £3,802m (2006: £3,724m) the 2005 underwriting year of account closed at a profit of £340m, benefiting from surpluses on the 2004 and prior RITC received at December 2006.

In aggregate, run-off years reported an overall profit of £75m including investment income (2006: £125m) and syndicates backed by insolvent members supported by the Central Fund reported a small overall surplus.

2007 also saw an increase in the market's appetite to accept the reinsurance to close of orphan syndicates with the number of underwriting years of account in run-off significantly decreased by the year end.

Years of account in run-off



The results of the major classes of business are discussed in detail on pages 51 to 57.

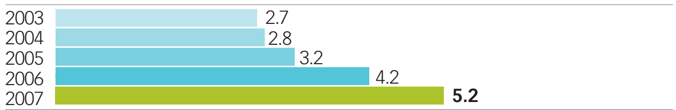
INVESTMENT REVIEW

Managing agents are responsible for investment of syndicate premium assets. Whilst the trend towards asset class diversification continues, with growing exposure to equities and hedge funds, the overwhelming majority of syndicate assets continue to be invested in fixed-interest securities of high credit quality. Currency dispositions of investments broadly reflect the currency of syndicates' insurance exposures. The average term of fixed-interest investments tends to be relatively short, limiting the volatility of such exposures. This is appropriate in view of the requirement that syndicate assets be available to meet claims as they fall due.

Fixed-interest markets experienced a turbulent year in 2007. Emerging concerns about the creditworthiness of sub-prime mortgage borrowers in the US caused the value of structured securities backed by such obligations to fall significantly. Such falls quickly spread to other securities having exposure to corporate credit risk, as investors reassessed the level of risk inherent in such investments. As borrowing in financial markets became more expensive, fears grew that this 'credit crunch' may lead to recession. This had the effect of further eroding confidence in corporate borrowers and with growing expectations that interest rates would fall to protect economic growth, led to a significant reduction in the general level of yields.

Even AAA rated structured securities were not immune to sub-prime related losses, so that the high credit quality of most syndicate investments was not a guaranteed protection against the adverse market developments. In fact, only a limited number of syndicates had any significant exposure to the worst affected securities and these exposures were insignificant across the market as a whole. Having largely avoided sub-prime related losses, syndicate bond investments instead benefited from falling yields. Overall syndicate investments returned £1,226m, or 5.2% in 2007 (2006: £957m, 4.2%). This is the highest return from syndicate investments for the last five years, and represents a significant element of Lloyd's total profit.

Syndicate investment return
%



Members' capital is generally held centrally at Lloyd's. A proportion of this capital is maintained in investment assets and managed at members' direction. A notional investment return of £653m or 6.0% (2006: £651m, 5.9%), based on the disposition of invested capital and market indices, has been included in the Pro Forma Financial Statements (PFFS).

Investment performance of Lloyd's central assets is discussed on page 108.

RESULTS SUMMARY

Lloyd's achieved a profit for the financial year before tax of £3,846m (2006: profit of £3,662m) and a combined ratio of 84.0% (2006: 83.1%). The PFFS aggregates the results of the syndicate annual accounts, notional investment return on funds at Lloyd's (FAL) and the Society of Lloyd's financial statements. The basis of preparation of the PFFS is set out in note 2 on page 73. The syndicate annual accounts reported an aggregate profit of £3,029m (2006: profit of £2,826m). These results are reported in a separate document (the Aggregate Accounts) and can be viewed on www.lloyds.com/financialreports. During 2007, certain syndicates changed their accounting policies resulting in a restatement of the comparative figures for 2006 within their annual accounts and the Aggregate Accounts have been restated accordingly. The restatements are not material and therefore the comparative figures within the PFFS have not been restated.

REINSURANCE
SECOND YEAR OF STRONG EARNINGS

2007 highlights

- → Low catastrophe loss experience worldwide.
- → Prior year releases of £198m.

2007 combined ratio

86.3%	Accident year
(4.6%)	Prior year reserve movement
81.7%	Calendar year

The reinsurance sector covers a wide range of classes and types, both short and long tail and uses a variety of placement types including facultative ie individual risk placements; proportional treaties; and non-proportional treaties such as excess of loss placements.

The largest classes of business within this sector are property facultative, catastrophe excess of loss and property non-proportional risk excess. In addition, there is a limited amount of retrocessional business. A large proportion of this business provides protection for US insurance and reinsurance companies and includes a small amount of casualty treaty business. The sector also includes class specific reinsurance, including energy and aviation.

2007 PERFORMANCE

Lloyd's reported gross written premium for 2007 of £5,453m (2006: £5,557), a decrease of 1.9%.

Following last year's strong trading conditions in US wind-exposed business, combined with a benign catastrophe season, 2007 saw an increase in the available capacity for this class of business, as well as alternative forms of capacity, leading to rate reductions during the last three-quarters of the year.

Last year we highlighted the political risk faced by insurers in the US, where state-led oversight can affect regional market conditions. The legislative changes in Florida, concerning the Florida Hurricane Catastrophe Fund (FHCF), did not have a significant direct impact on premium income for Lloyd's in 2007 with savings made by primary companies often being used to buy more coverage. While this model has not been adopted in other states, it remains to be seen whether the FHCF will give rise to further changes in the US.

Other markets remained extremely competitive with rates flat or continuing to soften, showing little reaction to events such as windstorm Kyrill or the UK floods.

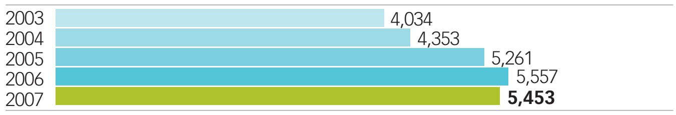
Class specific coverage, particularly aviation, experienced accelerated rate reductions in line with the direct market.

ACCIDENT YEAR PERFORMANCE

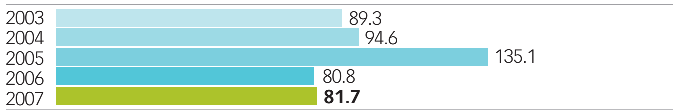
The accident year combined ratio for 2007 was 86.3% (2006: 77.0%). The level of losses has increased compared to the prior year due to events such as windstorm Kyrill and the UK floods, although 2007 was still a benign year with incurred loss incidence below long-term averages.

Combined with the loss experience, the softening market conditions discussed above have caused the slight deterioration in the accident year combined ratio, although it remains significantly below 100%.

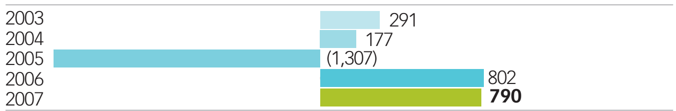
Gross written premium
£m



Combined ratio
%



Underwriting result
£m



PRIOR YEAR RESERVE MOVEMENT

The prior year reserve movement was a surplus of 4.6% (2006: deterioration of 3.8%). The improvement, compared to 2006, is a result of the stabilisation in the loss estimates for the 2005 US hurricanes combined with releases from other areas of the account.

LOOKING AHEAD

The traditional reinsurance market and the capital markets are converging. Insurance linked securities are becoming more accessible, affordable and accepted by rating agencies, with a number of new trading exchanges established during the last year. The popularity of these products, due to the attraction of insurance linked securities as an uncorrelated risk, does not appear to be waning, despite the issues facing the wider credit markets.

The reinsurance sector is also affected by the increase in self-insurance. Modelling techniques have become more sophisticated and readily available to all parties in the risk transfer chain. This is driven by new technologies and a greater understanding and availability of data on the risk environment. Tolerable remaining risk is increasingly being self-insured with only the higher-risk, more volatile elements being passed to the insurance industry.

Competition within the reinsurance sector is further intensified by entities operating out of lower tax jurisdictions or those that benefit from a tax deduction for a portion of their capital in excess of technical reserves, ie claims equalisation reserves, as they are able to operate with lower technical prices.

The non-US reinsurance sector is facing additional pressure from entities, particularly recent start-ups operating out of Bermuda, with large capital levels and a desire to diversify their portfolio.

This increased competition has led to another late renewal season, with a range of rate reductions. Extreme movements were less evident than in the insurance sector. Concessions were mainly on pricing with no significant changes in coverage.

Managing the cycle remains of paramount importance, as the level of alternative risk transfer mechanisms could significantly impact the ability of traditional reinsurers to take advantage of the upturn in the insurance cycle.

PROPERTY
DECLINING RATES FROM HIGH POINT IN CYCLE

2007 highlights

- Benign US windstorm season.
- Limited impact from worldwide catastrophe losses.

2007 combined ratio

92.3%	Accident year
(6.0%)	Prior year reserve movement
86.3%	Calendar year

The Lloyd's property sector covers both commercial and private property. Business is written via insurance agents or the broker distribution chain. The US is the largest geographical segment within the property sector.

2007 PERFORMANCE

Gross written premium for the Lloyd's property sector in 2007 was £3,809m (2006: £3,638m), an increase of 4.7%.

For US catastrophe exposed business, competition increased during 2007, particularly from the US domestic and Bermudian markets. This has resulted in softening rates, albeit from the highs of 2006.

Elsewhere, other lines of business continued to face increased competition, particularly as some insurers seek to diversify their portfolios away from catastrophe exposed risks. As a result the softening market conditions experienced in recent years have continued.

ACCIDENT YEAR PERFORMANCE

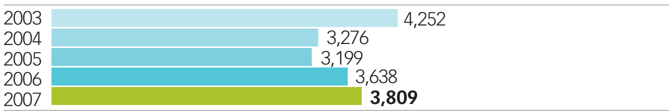
Windstorm Kyrill in Northern Europe, the California wildfires, hurricane Dean, and the record floods in the UK all impacted the property sector during 2007. While Lloyd's share of the industry losses for these events was not significant, they did contribute to an increase in the level of accident year losses when compared to the exceptionally low loss incidence experienced during 2006.

The increases in the level of losses, allied with the softening market conditions, caused the accident year loss ratio to rise to 92.3% (2006: 86.2%).

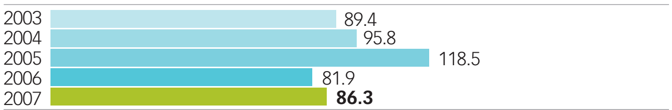
PRIOR YEAR RESERVE MOVEMENT

The stabilisation in the 2005 US hurricanes losses, and the continued releases from reserves established in 2002 to 2006, have generated further surpluses and improved the combined ratio by 6.0% (2006: 4.3%).

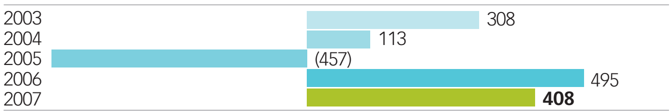
Gross written premium
£m



Combined ratio
%



Underwriting result
£m



LOOKING AHEAD

Along with the reinsurance and energy sectors, the Lloyd's property sector is heavily impacted by US windstorms. As such the view that we are in a cycle of above average North Atlantic hurricane activity continues to dominate the outlook for the sector.

Despite these predictions, competition within US catastrophe exposed lines is intensifying. This has resulted in further softening of rates during the 2008 January renewal season.

Furthermore, within other lines of business, the level of competition shows no signs of dissipating. This competitive pressure is beginning to spread to deductibles and coverage, which have broadly held since 2001, without a commensurate increase in pricing. There is a risk that these concessions will lead to rising attritional losses and further erode margins.

CASUALTY
CHANGING ECONOMIC ENVIRONMENT THREATENS RETURNS

2007 highlights

- Third successive year of prior year surpluses.
- Excellent performance must be balanced against increasingly fragile global economy.

2007 combined ratio

101.8%	Accident year
(9.1%)	Prior year reserve movement
92.7%	Calendar year

Lloyd's casualty sector covers professional indemnity, medical malpractice, accident and health, directors' and officers' liability, financial institutions, general and employers' liability. A large proportion of casualty business is within the US, UK and European markets.

2007 PERFORMANCE

2007 saw gross written premium of £3,364m (2006: £3,572m), a decrease of 5.8%.

Within the US, rates came increasingly under pressure and began to fall, albeit from relatively high levels, following the sharp rises in 2002 and 2003 and the more stable environment from 2004 to 2006.

Outside of the US the picture is very different with competition intense and rates continuing to fall.

ACCIDENT YEAR PERFORMANCE

The casualty sector achieved an accident year combined ratio of 101.8% (2006: 96.3%).

To date the US sub-prime crisis has resulted in few claims notifications being received by the Lloyd's market. Elsewhere, there has been limited major loss activity, reflecting the continued favourable economic conditions experienced during much of 2007.

For casualty business, profits emerge over time due to the longer tail for claims development. Consequently, the prior year reserve movement has a significant bearing on the overall combined ratio. The recent adverse history of this sector, particularly on business written in 1997–2001, has led to higher accident year combined ratios.

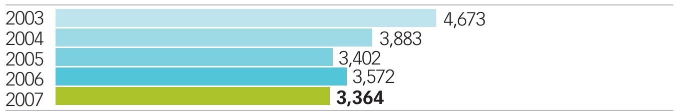
While performance varies between the different products and geographical segments, in aggregate the softening conditions and the changing economic environment have eroded what was a small margin. Should these conditions continue, the Lloyd's casualty sector runs the risk of becoming reliant on uncertain prior year reserve movements to achieve an underwriting profit on a calendar year basis.

PRIOR YEAR RESERVE MOVEMENT

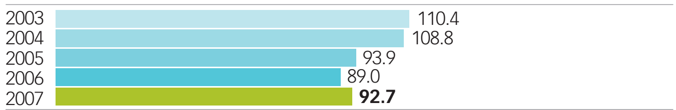
Prior year reserve movement improved the combined ratio by 9.1% (2006: 7.3%). For the third successive year underlying claims development has led to a surplus, a trend which confirms that Lloyd's businesses have now addressed the legacy issues arising on business written in soft market conditions in 1997–2001.

Overall results for casualty syndicates benefited from investment returns earned on assets held to meet the longer tail claims for this class.

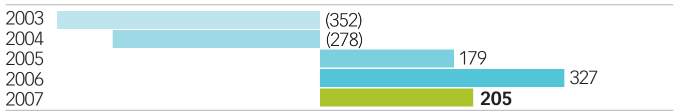
Gross written premium
£m



Combined ratio
%



Underwriting result
£m



LOOKING AHEAD

While the January renewal season has seen some stabilisation of rates in those lines of business most closely linked to the US sub-prime crisis, the general rating trend in the sector as a whole continues downwards, albeit in the case of the US from a hard market position.

The US sub-prime crisis is a significant issue for the insurance industry and the global casualty sector in particular with professional indemnity and D&O among the classes that could be affected. Several class actions have already been instigated in the US and, irrespective of the indemnity potential, the costs of defending these claims will be significant.

Lessons have been learned from the previous underwriting cycle and a more specialised mix of business is being written within Lloyd's. Wall Street exposure is no longer as significant as previously, and Lloyd's is not expected to incur substantial direct sub-prime losses.

However, the sub-prime crisis and the global 'credit crunch', combined with the turmoil in the US real estate market, has caused more and more economists to predict that the US economy is heading for a recession, if not already there, with likely knock-on impacts to other economies around the world.

This possible downturn in the global economy is likely to widen the potential for more varied losses, particularly within the casualty arena.

The various tort systems and legal processes around the world are a significant factor in dealing with long-term liability claims. Recent tort reforms in some countries are partially addressing this risk, resulting in reduced claim frequency and reduced costs.

The extent to which these reforms are apolitical and neutral to the changing economic landscape will have a significant impact on the future profitability of the casualty sector.

MARINE
LLOYD'S MARKET AVOIDS LARGE INDUSTRY LOSSES

2007 highlights

- Competition remains intense.
- Fifth consecutive year of prior year releases.

2007 combined ratio

95.0%	Accident year
(7.6%)	Prior year reserve movement
87.4%	Calendar year

The most significant classes of business within the Lloyd's marine sector are hull, cargo, marine liability and specie.

2007 PERFORMANCE

The marine sector achieved gross written premium of £1,226m (2006: £1,153m), an increase of 6.3%.

The two largest marine classes, hull and cargo, remain highly competitive. As a consequence, rates remain under pressure with reductions experienced during the year.

By contrast, the value of risks has increased, as the booming growth in world trade leads to a demand for bigger and faster ships to transport goods.

This has led to increased exposures and higher premiums, despite lower rates; ie a masking of the softening conditions.

Overall, rates in the marine liability account reduced during the year. The International Group of P&I Clubs programme constitutes a major part of this class of business.

Specie, the insurance of highly valued items such as fine art, remains a very competitive market, with rate reductions experienced during the year.

ACCIDENT YEAR PERFORMANCE

In 2007, the global marine market saw major hull losses running at levels not experienced since the 1980s, when there were structural failures amongst the ageing bulk carrier fleet. In recent years, Lloyd's syndicates have exercised caution in this market, particularly in relation to blue water fleets where the impact of a single loss can be severe. The benefit of this caution has been that Lloyd's syndicates have been able to avoid several of these losses.

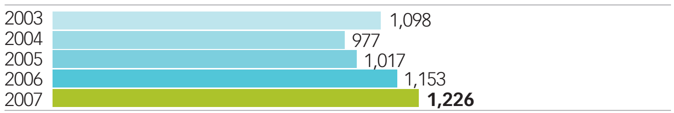
Within the rest of this sector, the International Group of P&I Clubs programme and specie also experienced notable losses, while the cargo account experienced a second year of favourable claims activity.

Whilst market conditions have softened, the overall decrease in the level of claims has resulted in an improvement in the accident year combined ratio to 95.0% (2006: 99.0%).

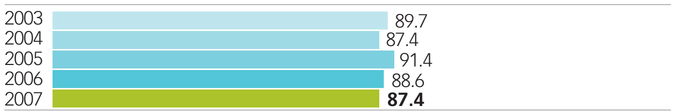
PRIOR YEAR RESERVE MOVEMENT

An overall release from prior years' reserves reduced the combined ratio by 7.6% for the year (2006: release of 10.4%). This has continued the trend for prior years to develop within expectation with a surplus arising for the fifth consecutive year.

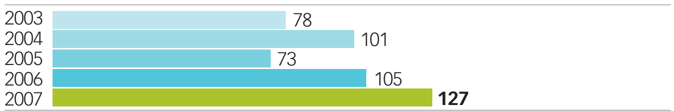
Gross written premium
£m



Combined ratio
%



Underwriting result
£m



LOOKING AHEAD

Following the loss experience during 2007, the 2008 January renewal season for the hull class was flat, and rate increases were experienced in the International Group of P&I Clubs programme. However, other classes of business within the marine sector continue to experience softening market conditions.

The size and number of blue water fleets have increased over recent years to meet the demand from the growth in world trade. A collision involving one of these vessels would be a major catastrophe and the current rating environment is marginal.

With shipyards around the world operating at full capacity to meet the demand for new vessels, repair facilities and trained engineers are at a premium. This, allied to the continuing rise in the price of commodities, has resulted in an increase in the costs of the vessels, their repair and the cargoes they are transporting.

The shortage of experienced officers and crew together with new regulations aimed at improving crew members' hours and working conditions, whilst laudable, unfortunately coincides with the launch of an increasing number of ships. As a result the number of adequately experienced mariners will be spread ever more thinly.

P&I clubs are also affected by new legislation and changes to existing laws, which may give rise to additional liabilities, as well as having to prepare for a more demanding regulatory environment.

This potential for increased loss frequency and severity heightens the continued need for underwriting discipline on both rates and terms and conditions.

MOTOR
SPECIALIST MIX HELPS PERFORMANCE IN TOUGH MARKET CONDITIONS

2007 highlights

- Soft market conditions continue pushing current trading further into loss.
- Reliance on positive prior year reserve movement for overall underwriting profit.

2007 combined ratio

104.8%	Accident year
(6.4%)	Prior year reserve movement
98.4%	Calendar year

In recent years this class has become less prominent in the market as a whole but remains an important part of our overall diversified business. In the face of intense competition within the private car market, from large consumer-facing organisations such as supermarkets, the mix of motor business written within Lloyd's has changed.

There has been a move to underwrite company fleet business and non-standard risks such as high value vehicles, vintage or collectors' vehicles, high risk drivers and affinity groups; to the extent that less than half the current premium income derives from private car insurance.

The bespoke nature of these risks plays to Lloyd's traditional strengths, as the exposures are more complex and require a higher level of skill and experience to underwrite effectively.

The overseas market continues to be an important part of Lloyd's portfolio, with around 16% now originating outside of the UK.

2007 PERFORMANCE

Gross written premium in 2007 for the Lloyd's motor sector was £983m (2006: £923m), an increase of 6.5%.

In the UK, while conditions vary across the different lines of business, overall the softening rates experienced since 2003 continued into 2007, although there were signs of rates flattening in the final quarter of the year.

The overseas motor market continued to experience softening conditions throughout the year, although performance varies between territories.

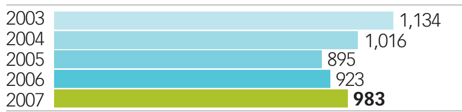
ACCIDENT YEAR PERFORMANCE

The trend for claims costs to outstrip inflation continues. This combined with the ongoing soft market conditions has resulted in a further increase in the accident year combined ratio to 104.8% (2006: 101.7%).

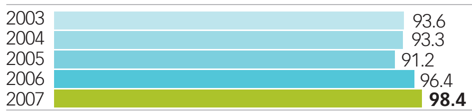
PRIOR YEAR RESERVE MOVEMENT

Prior year reserve movement improved the combined ratio by 6.4% (2006: 5.3%) as claims continue to develop within expectations.

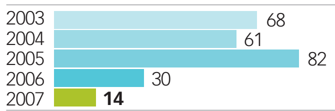
Gross written premium
£m



Combined ratio
%



Underwriting result
£m



LOOKING AHEAD

In the face of continued soft market conditions, the Lloyd's motor sector has become dependent on reserve releases to turn accident year losses into profitable results. This is not a sustainable strategy and the motor market must look to underwrite for profit.

While some analysts predict that the UK motor market is at the bottom of the cycle, with a general upturn forecast for the next few years, momentum is likely to be slow as the market remains extremely competitive. The growing popularity of the aggregators offering price comparison sites, means that consumers are increasingly focusing on price rather than other factors such as brand, claims service or coverage.

The Lloyd's market offering of niche products is key if it is to avoid the most intense areas of competition.

ENERGY
CONTINUING STRONG CONDITIONS AND A BENIGN LOSS EXPERIENCE

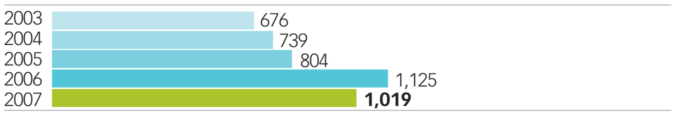
2007 highlights

- Increase in asset values.
- Aggregate prior year release following stabilisation of 2005 US hurricane claims estimates.

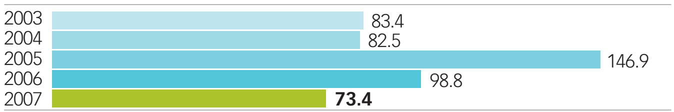
2007 combined ratio

77.3%	Accident year
(3.9%)	Prior year reserve movement
73.4%	Calendar year

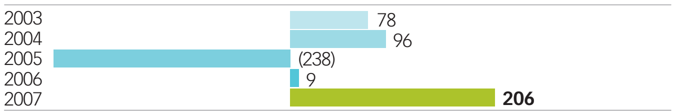
Gross written premium
£m



Combined ratio
%



Underwriting result
£m



The Lloyd's energy sector includes a variety of onshore and offshore property and liability classes, ranging from construction to exploration and production, refinery and distribution.

A significant part of the portfolio is offshore energy business and a large proportion of this is located in the Gulf of Mexico.

2007 PERFORMANCE

The Lloyd's energy sector achieved gross written premium of £1,019m (2006: £1,125m), a decrease of 9.4%.

Following the significant rate increases experienced in the aftermath of the 2005 hurricanes and the benign loss experience in 2006, competition intensified during the year, with softening market conditions being experienced in both the offshore and onshore markets. Significant increases in asset values, however, are partially masking the impact of soft market conditions on premium volumes.

ACCIDENT YEAR PERFORMANCE

The accident year combined ratio for 2007 was 77.3% (2006: 83.7%). The improvement in the ratio is being driven by the strong underwriting conditions experienced in 2006, with premiums continuing to be earned throughout 2007, as loss experience was once again benign.

PRIOR YEAR RESERVE MOVEMENT

2007 saw a significant improvement in the prior year reserve movement as the loss estimates for the 2005 hurricanes stabilised, resulting in a surplus on prior years of 3.9% (2006: deficit of 15.1%).

LOOKING AHEAD

The future performance of the energy sector for Lloyd's is intrinsically linked to the hurricane season in the Gulf of Mexico. Following a second year of low loss levels and strong accident year performance, industry capacity for most lines of business is expected to increase again in 2008, despite predictions that we are in a cycle of above average North Atlantic hurricane activity.

The increase in competition is already being seen in the recent renewals. These show a continuation of the softening conditions, although rates are still relatively high by historical standards. Other signs of the softening market are now being seen with concessions being given on terms and conditions such as increased wind limits for Gulf of Mexico risks, expansion or deletion of sub-limits and attempts to place multi-year policies.

The price of crude oil continues to rise, recently exceeding US$100 per barrel, as supply struggles to cope with the high demand from emerging countries. This has led to existing facilities operating at or near capacity, with the price per barrel increasingly sensitive to any small production disruptions and a significant increase in the number of new projects worldwide.

These projects are looking more and more at fields that had previously been considered marginal or inaccessible, requiring innovative technology and increased exploration, drilling and construction at a time when resources are scarce and commodities such as steel, concrete and cement are already in high demand.

This has led to further increases in contractor rates and rises in commodity prices driving up project costs and a knock-on increase in the valuation of existing facilities.

As a result of the ageing existing facilities and rising valuations, business interruption remains a key concern, particularly with regard to the values presented truly reflecting the risk that underwriters are being asked to assume. In addition, the shortage in skilled resources is likely to cause further delays to the time required to restore facilities to operational status following physical damage. Estimates have risen from 24 months to between 36 and 48 months and in a few cases up to 60 months.

The rising asset values are resulting in increased premium levels and a rise in the number of projects which offer business opportunities for the energy insurance sector. However, this will be tempered by the likelihood of an increase in loss frequency and severity.

Maintaining discipline on terms and conditions as well as pricing and aggregate exposure is critical to the ongoing profitability of this sector.

AVIATION
PRESSURE ON RATES REACHES CRITICAL POINT

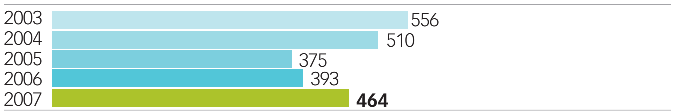
2007 highlights

- Sixth consecutive year of rate softening.
- Increased loss incidence during the year.
- Continuing prior year releases a key component of the strong combined ratio.

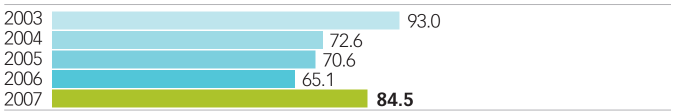
2007 combined ratio

102.8%	Accident year
(18.3%)	Prior year reserve movement
84.5%	Calendar year

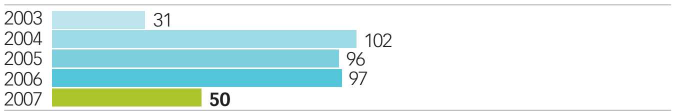
Gross written premium
£m



Combined ratio
%



Underwriting result
£m



Lloyd's is an industry leader within the global aviation market and has a balanced portfolio across all sectors of this specialist class, including airline, aerospace, general aviation and space business.

2007 PERFORMANCE

Aviation business is written as both direct and reinsurance acceptances, on an excess of loss, proportional or facultative basis. On a direct basis gross written premium was £464m (2006: £393m), an increase of 18.1%. This increase is driven by a reclassification from reinsurance to direct aviation to more appropriately reflect the underlying nature of the business written; the prior year analysis has not been restated. Overall, direct and reinsurance aviation business combined has seen an increase of less than 4% in gross written premium.

While rates in the aviation market improved significantly immediately after the heavy losses of 2001, namely 9/11 and Queens, subsequent years have seen persistent falls in airline rates. This trend continued throughout 2007.

As margins diminished further within the airline sector, capacity has continued to move into other aviation classes, with the result that rates in these classes also softened further in 2007.

ACCIDENT YEAR PERFORMANCE

The accident year combined ratio for 2007 was 102.8% (2006: 87.4%). While the increase in the ratio is in part due to the continuing softening market conditions, the main driver has been the increase in the level of loss incidence during the year, which is higher than the average over the last ten years.

PRIOR YEAR RESERVE MOVEMENT

Surpluses on prior years' claims reserves improved the combined ratio by 18.3% (2006: 22.3%), continuing the trend for benign claims development across the entire portfolio.

LOOKING AHEAD

The global airline market invests heavily in technology and training to improve safety and security. Nevertheless, pilot error remains the main cause of airline losses and this, allied with the continued increase in the number of flights, means there is potential for a rise in loss frequency.

During 2007, we continued to see an increase in exposure with fleet values and passenger numbers over 10% higher than 2006. Furthermore, the introduction of two new super-jumbos means that there is also potential for a rise in loss severity.

Following a sixth consecutive year of falling rates, there is a risk that the current level of premium is insufficient to cover these potential increases in loss frequency and severity, let alone any major catastrophe.

In light of the loss experience in 2007 and with margins diminishing, capacity may leave the airline sector, which would cause a hardening of rates. This will be largely dependent on the performance of the sector leading up to the main renewal season in the fourth quarter of 2008. There is also likely to be pressure to underwrite multi-year policies as airlines will seek to take advantage of the current rating environment.

With the increasing popularity of corporate and private jets, particularly under shared ownership schemes, the general aviation sector is growing. Also safety features and technology, such as ground proximity warnings, are filtering down from airlines into the general aviation market, improving the overall risk management of the sector.

This creates opportunities for existing insurers but will also attract additional capacity to the sector, putting further pressure on what is already a soft rate environment.

The space sector did experience significant losses during 2007, which could have an impact on the rates in 2008. However, there have also been improvements in reliability and a maturing of the satellite and launch vehicle technology. Allied to new satellite applications this has led to an increase in the number of satellites being launched each year. This, combined with the prospect of space tourism in the near future, means that there continue to be opportunities within the space insurance sector.

DELIVERING VALUE

DELIVERING VALUE TO OUR STAKEHOLDERS

THE PRINCIPAL BENEFITS OF LLOYD'S OFFER

LLOYD'S OFFERS CLEAR BENEFITS TO MARKET PARTICIPANTS – AND THE WIDER COMMUNITY.

MARKET PARTICIPANTS

Lloyd's principal stakeholders are its market participants including managing agents, brokers and capital providers. The value each can derive from participating at Lloyd's is described below.

CAPITAL PROVIDERS

An opportunity to participate, within a capital efficient framework, in businesses with the ability to maximise their performance in the specialist insurance and reinsurance markets.

MANAGING AGENTS

A core central offer of security, market access and standards, plus the provision of flexible tools and services which can be used as appropriate to execute individual strategies.

BROKERS AND POLICYHOLDERS

A secure market with diverse participants, differing strategies and risk appetites, with the benefit of Lloyd's reputation and service quality.

The attractions of Lloyd's to each stakeholder group can also be summarised by reference to the five benefits, see pages 60 to 61.

COMMUNITY AND ENVIRONMENT

Lloyd's also has wider social responsibilities. These include supporting the local community, co-ordinating a range of charitable initiatives both in the UK and overseas, and responding to the environmental challenges of climate change.

For more details on Community and Lloyd's Charities Trust, see pages 62 to 65.
For more details on Environment, see pages 66 to 67.

MARKET PARTICIPANTS

	BENEFITS	CAPITAL PROVIDERS
1 PERFORMANCE FRAMEWORK	An overarching, consistent performance management framework across all key aspects of a managing agent's business, that supports the achievement of superior operating returns as part of an effective enterprise risk model.	→ The confidence that managing agents are meeting minimum standards and consequently reducing the volatility of their performance.
2 CAPITAL ADVANTAGES	A capital framework in which the benefits of mutuality demonstrably outweigh the costs and which cannot readily be duplicated outside Lloyd's.	→ The ability to achieve higher returns compared to those in other insurance markets through the exploitation of an efficient mutual layer of capital that supports the business of the whole market, yielding a diversification credit to capital providers. Greater choice available to capital providers in how they provide capital to support their underwriting.
3 SECURITY AND RATINGS	Stable insurer financial strength ratings (currently at least 'A') necessary to attract specialist property and casualty business.	→ The ability to earn improved returns on capital as a result of the ratings and the better quality business that they attract.
4 MARKET ACCESS	Cost-effective, easy access to the major markets supported by a global brand and licence network.	→ The opportunity to obtain attractive returns from an investment in a bespoke portfolio of global insurance risks.
5 OPERATING ENVIRONMENT	An efficient, cost-effective operating environment that allows managing agents and brokers, irrespective of their location, to deliver excellent service to customers.	→ More transparent, automated processes, supported by improved management information will reduce managing agents' operational risk, making Lloyd's more attractive.

MANAGING AGENTS	BROKERS AND POLICYHOLDERS
→ A framework of minimum standards which makes clear what is required of businesses operating at Lloyd's. The framework is differential in its application, rewarding better performing businesses (eg with lower capital, more flexibility in the application of the Franchise Guidelines and a generally lighter touch from the Corporation) and taking action against underperforming businesses or those which pose a threat to the interests of policyholders and other market participants.	→ More efficient, transparent and consistent market performance which strengthens Lloyd's attractiveness as a place for brokers to bring business. → Policyholders have their insurance placed with businesses that are subject to underwriting management and claims management standards.
→ The ability to respond quickly and flexibly to changing market conditions, attracting capital for both new and existing businesses with the prospect of producing higher returns than could be achieved elsewhere.	→ The ability for brokers to offer risks to a number of diverse businesses with different risk : reward appetites that share a common rating. → Policyholders derive comfort from Lloyd's financial strength.
→ Access to the security ratings necessary to attract specialist insurance and reinsurance business. → A more stable rating than could be achieved individually due to the benefits of market diversification. → No need to commit the substantial human and financial resources necessary to obtain a rating in their own right.	→ Brokers have access to significant capacity with the rating required by policyholders. → Brokers can place risks with many businesses without having to put each through a separate due diligence process.
→ The ability to utilise Lloyd's trading rights, allowing access to a broad range of business from the world's major markets, with the majority of the compliance burden being met by the Corporation. Access is possible through a variety of distribution channels. Managing agents can use, as required, one of the most recognised and renowned global insurance brands. The Corporation provides lobbying services on the market's behalf and ready access to advice and expertise on international compliance and the regulatory environment.	→ Brokers have easy access to, and speed of decision making by, underwriters who are able to provide global insurance coverage for policyholders.
→ Strengthening the competitive position of all managing agents by minimising any burden associated with the processes and operation of a subscription market. Information will be sourced once and used many times to support managing agents in planning, measuring and managing their business. Managing agents (and brokers) may need to modify systems, processes and behaviours to benefit fully from the planned changes.	→ An interface with the Lloyd's market that will be comparable to other markets in terms of time and cost to conduct business. Brokers will be able to use simple processes when dealing with Lloyd's, while continuing to derive the benefit from a subscription market. They will be able to carry out some activities without the need for face-to-face interaction.

COMMUNITY

WE SUPPORT OUR LOCAL COMMUNITY BY VOLUNTEERING TIME, TALENT AND EXPERIENCE.

LLOYD'S COMMUNITY PROGRAMME

The award-winning Lloyd's Community Programme gives people in the Corporation and the market the opportunity to 'put something back' into the community on their doorstep.

This long-running community involvement scheme provides volunteering opportunities for individuals and companies from Lloyd's.

In 2007, 900 volunteers from the Corporation and the market took part in opportunities in the East London community through Lloyd's Community Programme. Volunteering ranged from working with children in Tower Hamlets and Hackney to improve literacy and numeracy skills, to helping regenerate the local community through team challenges such as renovating local parks.

Volunteers taking part in the Lloyd's Community Programme have found it gives them a greater understanding of diversity in the local community and adds a further dimension to their work within Lloyd's.

Lloyd's Community Programme is supported by individuals from over 65 managing agents, insurance brokers and other associated companies. The positive impact of these companies was recognised in 2007, with the award of the Business in the Community Power in Partnership Award. A second Corporate Responsibility award – the Silver Jubilee Award – was also presented in recognition of the programme's longevity.

Despite bordering on the City and being home to Canary Wharf, East London is characterised by having some of the country's highest social deprivation statistics. Since Lloyd's Community Programme was established, it has helped address some of the main socio-economic challenges affecting the area. Read on to find out more about the programme's support for the community.

For more information on Lloyd's community programme visit: www.lloyds.com/community

CHILDREN AND BASIC SKILLS
HELPING CHILDREN WITH LITERACY AND NUMERACY SKILLS

During 2007, over 650 children from schools in Tower Hamlets and Hackney benefited from volunteer support to develop basic skills through Reading and Number Partners schemes. Once a week, volunteers from Lloyd's spent half an hour during a lunchtime, in a local primary or secondary school, to work with children to develop and improve their reading or number skills.

YOUNG PEOPLE AND EMPLOYABILITY
HELPING YOUNG PEOPLE DEVELOP SKILLS TO TACKLE THE WORLD OF WORK

Levels of unemployment in East London are among the highest in the UK, with youth unemployment being a particular issue. Lloyd's Community Programme works with young people in local schools and colleges to develop essential skills for future employment.

Over 110 volunteers from Lloyd's have coached young people in the skills required to develop an understanding and awareness of the world of business and develop specific skills such as CV writing, interview techniques and presentation skills.

The annual Tower Hamlets Schools Public Speaking Competition gives students an opportunity to enhance their communication skills, self confidence and ability to construct a reasoned argument. In 2007, nine Year 10 students (14–15 year olds) shared their views on the topic 'What needs to be done about climate change and whose responsibility is it?' in the 12th competition hosted by the Corporation and supported by Lloyd's Community Programme.

Lloyd's Community Programme also encourages companies in the market to provide work experience placements and internships for local students. During summer 2007 the Corporation and four managing agents offered 11 students from inner London the chance to undertake paid work. This will continue in 2008, aiming to foster better links between companies in the Square Mile and young people in the neighbouring boroughs. Apart from helping students who ultimately want to work in the City, the initiative identifies new sources of talent for Lloyd's.

Reading Partners – helping pupils with literacy in Tower Hamlets

East London pupils in Lloyd's football cup tournament

REGENERATING COMMUNITIES
IMPROVING OPPORTUNITIES AND FACILITIES FOR LOCAL PEOPLE

Community based team challenges are increasingly popular team building opportunities for the Corporation and market firms and a great way to support the local community. In 2007, 198 people from six managing agents took part in 11 team challenges in a variety of activities ranging from painting and decorating local school classrooms to clearing a plot of land for a local women's group to use for allotments.

Local employment opportunities are a key issue and Lloyd's Community Programme continues to support the Lloyd's Loan Fund, set up in 1989, to provide financial support to small business start-ups in East London. Further funding for training, both for budding entrepreneurs to help them get off to the best start and for post business start-up training, benefited hundreds of people during 2007.

CHILDREN AND BROADENING HORIZONS: SPORTS
HELPING DEVELOP A LOVE FOR SPORTS

With a renewed understanding of the importance of physical activity for a healthy lifestyle, Lloyd's Community Programme volunteers are encouraging local students to start young by sharing their passion for sports. Individuals from the Corporation and the market continue to support the development of sporting skills with regular lunchtime coaching sessions at primary schools in Tower Hamlets and the annual Lloyd's Cup for cricket and football gives local schools a chance to play in a friendly tournament.

In 2007, over 180 children from eight local schools took part in a cricket coaching day held at the world's oldest test match venue, the Brit Oval. Volunteers supported the day by getting involved in umpiring and coaching sessions.

The Lloyd's Football Cup was made possible with the support of volunteers who provided coaching and refereeing support for over 160 children from ten local schools.

CHILDREN AND BROADENING HORIZONS: ARTS
OPENING UP CULTURAL OPPORTUNITIES AND EXPERIENCES TO CHILDREN

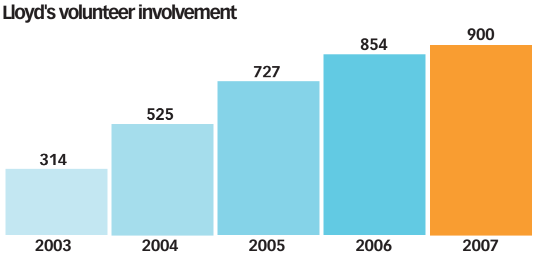
Lloyd's Community Programme continued to support the National Theatre's Word Alive! Storytelling Programme. Word Alive! offers a creative way to learn about language, word play and stories. With support from the Lloyd's Community Programme, over 450 students from Tower Hamlets, Hackney and Newham took part in the programme, which concluded with a visit to the National Theatre to watch a storytelling performance.

Lloyd's Community Programme's travel bursaries provide children from primary schools in Tower Hamlets with the opportunity to experience educational activities outside their immediate environment. Over 790 children from 22 Tower Hamlets schools benefited from the travel bursary scheme during 2007. Children from John Scurr Primary School visited Gorsefield Outdoor Activity Centre in Essex, while another group from St Mary & St Michael Primary School enjoyed a trip to Atherfield Bay on the Isle of Wight.

EFFECTIVE COMMUNITY LEADERS
SHARING PROFESSIONAL SKILLS TO SUPPORT THOSE WITH LEADERSHIP ROLES IN THE COMMUNITY

During 2007, volunteers took part in the Police Mentoring project which matches senior business people from Lloyd's with members of the Senior Management Team at Hackney Police Service to provide mentoring support through regular meetings. Lloyd's Community Programme continues to provide opportunities for people to get involved with local charities and non-governmental organisations, in a leadership capacity, as school governors, trustees or board members.

Lloyd's volunteer involvement



Lloyd's Community Programme members

The Lloyd's Community Programme was able to undertake its work in the East London community due to the support of the following market participants and service providers during 2007:

- Ace European Group
- Advent Underwriting Ltd
- Amlin plc
- Aon Ltd
- Ascot Underwriting Ltd
- Atrium
- BMS Group Ltd
- Barlow Lyde & Gilbert
- Beazley Group plc
- Benfield
- Bowood Partners Ltd
- Brit Insurance Holdings Ltd
- Canopius Managing Agents Ltd
- Capita
- Catlin Underwriting Agencies Ltd
- Chaucer Syndicates Ltd
- Clyde & Co
- Cooper Gay
- Denis M Clayton & Co Ltd
- Dewey & LeBoeuf
- Edwards Angell Palmer & Dodge UK LLP
- Ernst & Young
- Faraday Underwriting Ltd
- Hardy Underwriting Group plc
- Heath Lambert Group
- Hiscox plc
- Holman's
- HSBC Insurance Brokers Ltd
- Ince & Co
- Jardine Lloyd Thompson Group plc
- Kiln plc
- Liberty Syndicates
- Lloyd's
- Lockton
- Marketform Group
- Marsh Ltd
- Mazars
- Miller Insurance Services Ltd
- Munich Re Underwriting Ltd
- Navigators Underwriting Agency Ltd
- Omega Underwriting Agency Ltd
- Pricewaterhouse-Coopers
- QBE Insurance Group
- Reynolds Porter Chamberlain
- Talbot Underwriting Ltd
- Travelers
- Xchanging Claims Services
- Xchanging Ins-sure Services
- XL London Markets Ltd

LLOYD'S CHARITIES TRUST

CHARITY BEGINS AT LLOYD'S AND GOES AS FAR AS AFRICA AND THE ANTARCTIC.

Lloyd's has a history of social responsibility spanning more than two centuries. Our commitment to social responsibility is clearly demonstrated by the range of charitable initiatives we carry out in the UK and internationally. Whether supporting people in Southern Sudan, making an award to the Dorset and Somerset Air Ambulance, or offering a helping hand to ex-service personnel, Lloyd's aims to help people through its charitable support.

LLOYD'S CHARITIES TRUST

Lloyd's demonstrates its charitable support through Lloyd's Charities Trust. Established over 50 years ago, the grant making charity for the Corporation and the market supports a wide range of national and international charities. Donations are made by the Trust to a variety of charities focusing on children and young people, social welfare development and medical health projects.

PARTNER CHARITIES

Lloyd's Charities Trust works with three partner charities over a three-year period. Another milestone for the Trust was marked in 2007 with the announcement of the new partner charities for 2007–2010: Coram, FARM-Africa and the Samaritans. These charities were selected because of the work they do with those most 'at risk' and the Trust will provide grants of £150,000 to each organisation over the next three years to develop a specific project.

For more information on Lloyd's charity work
visit: www.lloyds.com/charity

CORAM
CHILDREN AT RISK

Coram, one of England's oldest charities, works with children who are vulnerable and at risk. Coram runs a unique adoption and fostering project – the Concurrent Planning Adoption Programme, which is being supported by Lloyd's Charities Trust. The programme works with newborn babies in England who are the subject of care proceedings, placing them in families able to adopt them if they're unable to return to their birth parents. This prevents children experiencing significant disruption in their early years.

FARM-AFRICA
COMMUNITIES AT RISK

FARM-Africa works with people at risk across Africa, helping them to effectively manage their natural resources and build sustainable livelihoods for future generations. The support of Lloyd's Charities Trust will enable FARM-Africa to progress the Household Recovery Programme for people in Southern Sudan returning to their land after the civil war. Through the partnership, households will be provided with access to clean water, high yield seed, agricultural tools, livestock and village vet training.

Children at risk
Image courtesy of Coram

Communities at risk
Image courtesy of FARM-Africa

SAMARITANS
LIVES AT RISK

The Samaritans offers 24-hour confidential support to anyone in emotional distress. The charity's 'Skills for Life' project, which is being supported by Lloyd's Charities Trust over the next three years, aims to build emotionally healthier communities for young people at risk of self-harm and suicide. A Suicide and Self Harm Response Toolkit, to support schools in the event of suicides or self-harm cases, will be developed with the Self-Harm and Response Training Bursary to support teachers and others working with young people at risk.

LLOYD'S MARKET CHARITY AWARDS

Another step forward was made in 2007 with the launch of the Lloyd's Market Charity Awards. These awards enable people in the Corporation and the market to give £1,000 to a UK based charity, including local charities that might otherwise struggle for funding, that they actively support or are involved in. Thirty awards of £1,000 were made to charities including Cystic Fibrosis Trust, Epilepsy Action UK, Tower Hamlets Gateway Club, Dorset and Somerset Air Ambulance and Chingford Air Cadets.

SPECIAL AWARD

A new Special Award was launched by Lloyd's Charities Trust in 2007 with the support of Lloyd's Council. This annual award is a one-off donation of £50,000 to a charity making a positive contribution to an issue or subject of interest to Lloyd's.

The first recipient of this award was International Alert, an independent peace building organisation that works to lay the foundations for lasting peace and security in communities affected by violent conflict.

Lloyd's Charities Trust donation is being used to help establish a new Business and Peace Fund, which will work with businesses operating in conflict prone areas to help them contribute to the creation of a stable political climate.

LLOYD'S TERCENTENARY FOUNDATION

Lloyd's Tercentenary Foundation was established in 1988 to commemorate Lloyd's 300th anniversary, to support medical, scientific, technical and business related education and research.

The Foundation provides essential financial support to a small number of top-flight research students at the immediate post-doctoral stage of their careers. In 2007, two Lloyd's fellowships were awarded for research into the Earth's core where the magnetic field is generated and for the study of Antarctic fossils to determine the effects of climate change.

LLOYD'S PATRIOTIC FUND

Lloyd's Patriotic Fund is the oldest naval and military charity of its kind, established in 1803 to raise funds for victims of the Napoleonic War.

With increased global conflict and UK military personnel serving overseas, the Fund's support is as vital now as ever, and today financial assistance is available for ex-servicemen and women, their widows and dependants.

The fund pays particular attention to cases of real need, especially those with chronic ailments or who live in poverty. Through its working relationship with SSAFA Forces Help, grants are made for exceptional expenses, essential domestic items, utility bills and home adaptations for those who are disabled.

Assistance is also given to Gurkha pensioners and children of service personnel at nominated schools.

Facts – Lloyd's partner charities

Coram
- → Less than 1% of young people who have been taken into the care system go to university.
- → There are currently approximately 4,000 children waiting to be adopted in the UK.

FARM-Africa
- → 90% of the population in the South of Sudan live below the poverty line of less than US$1 a day.
- → In Southern Sudan less than a third of the population has access to a safe source of clean water.

Samaritans
- → 1 in 10 young people self-harm in the UK.
- → Suicide remains the most common cause of death in men under 35.

ENVIRONMENT

FOR US, CLIMATE CHANGE IS NOT ACADEMIC: IT'S A CORE BUSINESS CHALLENGE FOR THE FUTURE.

LLOYD'S AND CLIMATE CHANGE

Our latest research shows that global warming is likely to bring increasingly dramatic, and possibly rapid, climate change. Business, along with all sections of society, shares responsibility to address the risks and consider the implications of climate change, including preparation for its effects.

Given the nature and extent of the weather risks insured in the Lloyd's market, climate change is at the top of our environmental agenda.

HOW IS LLOYD'S RESPONDING?

Lloyd's is actively engaging with various audiences on the impact of climate change, through the ongoing work of the Emerging Risks team and through Lloyd's 360 Risk Project.

In March 2007, Lloyd's launched its third climate change report, 'Rapid Climate Change', in response to the latest scientific consensus that climate change is likely to bring increasingly dramatic, and possibly rapid, effects at a local level. The report highlighted a number of key issues:

- The possibility of a rapid rise in sea levels over the coming decades putting coastal communities, including key urban conurbations in the developed world, at risk.
- The increase in instability of ice sheets and the potentially damaging impact their destruction could have on ocean circulation, sea levels and global climate.
- The frequency and magnitude of flooding which is set to increase, with resulting impact on lives and homes and businesses.
- Changing patterns of drought with greater vulnerability in certain regions, such as southern Africa.

Apart from the possibly devastating impacts on the communities affected, these issues are also important to Lloyd's given the nature and locations of the risks the market insures.

Lloyd's has made a series of expert views available on www.lloyds.com/360, as part of its programme of drawing on the expertise of leading thinkers from the insurance industry and the worlds of business, politics and academia. In October 2007, Lloyd's Emerging Risk team helped to bring together a number of international organisations for the first Catastrophe Modelling Forum (see case study, far right).

The Emerging Risks team has continued to work closely with academia on developing new and focused climate change related research and this has resulted in Lloyd's being awarded a second CASE studentship by the Engineering and Physical Sciences Research Council. Under the guidance of Professor David Stainforth at Exeter University, the research will focus on assessing which outputs from climate models can be used by the insurance industry for robust risk management.

The Emerging Risks team has also been active during the year in highlighting the role of insurers in adaptation and mitigation of climate change. This has included the publication of a report in the Geneva Papers on this subject, as well as participation in a round table discussion at the European Commission's 'Green Week'.

Building on feedback from participants in the live debate we hosted in 2006, Lloyd's 360 Risk Project has also been working to raise awareness amongst wider audiences, particularly students, of the significance of climate change (see case study, right).

With 87% of the Corporation's employees based in our two UK offices, the Corporation's direct environmental impact is relatively small. However, we have a role to play in promoting good environmental practice both internally and externally. During 2007, Lloyd's Environmental Working Group, reporting to the Director, Finance, Risk Management and Operations, met regularly to monitor progress against our Environmental Action Plan. Action was taken in 2007 to reduce energy consumption through a number of initiatives including auto switch-off for computer monitors. Work to address other environmental issues such as waste reduction, recycling and more effective use of resources such as water has also continued during the year. We were proud to receive a Platinum Clean City Award from the Corporation of London for our work on recycling and environmental issues during 2007.

Engaging wider audiences

Feedback from Lloyd's 360 Risk Project highlighted the need for businesses to raise awareness about the importance of tackling climate change amongst wider audiences, particularly the next generation.

In 2007, Lloyd's teamed up with charity Poet in the City to encourage individuals to think about the issue in a fresh way through its Trees in the City project. In February 2007, Lloyd's CEO, Richard Ward, officially opened a new outdoor space with trees and seating for City workers at London's Fenchurch Street. The site's design incorporated specially-commissioned poetry on climate change and schoolchildren from nearby Tower Hamlets submitted their 'wishes for the environment' which were attached to the newly-planted trees. The project funded the training of a team of educators who took the new poetry to a number of Tower Hamlets schools to help local students understand the importance of tackling climate change.

In May 2007, nine Year 10 Tower Hamlets students delivered impassioned speeches on the subject of 'Climate Change – what needs to be done and whose responsibility is it?' in the Old Library at Lloyd's. The students were the finalists in the Tower Hamlets Schools' Public Speaking Competition, hosted and supported by Lloyd's. Lloyd's was impressed with the time and effort which many students had spent researching the issues and 15-year-old Eiblin Priestley from Morpeth School won the competition with a strong challenge to the audience to 'Be the change in climate change'.

Lloyd's work to help equip the next generation to deal with emerging risk issues will continue with a further series of schools workshops in 2008.

Bringing scientists and insurers together on climate change

As part of our involvement with ClimateWise, Lloyd's is committed to sharing research with scientists and others in the insurance industry on climate change related issues.

In October 2007, Lloyd's teamed up with American International Group (AIG), the Insurance Information Institute (III) and Harvard Medical School to host the first Catastrophe Modelling Forum event in New York. The Catastrophe Modelling Forum has a current focus on climate change and, with additional support from ACE Ltd, Marsh Inc and Travelers, invited leading scientists for a two-day meeting to discuss how catastrophe models should be updated to reflect the latest climate change risks. The meeting was attended by many leading companies from the global insurance industry including brokers, reinsurers, insurers and catastrophe modelling firms.

Professor Kerry Emanuel, from the Massachusetts Institute of Technology, highlighted the strong correlation between hurricane power and sea surface temperatures. Dr Richard Murnane from the Risk Prediction Initiative called for an open architecture for catastrophe models which would accelerate the development of these models. This would enable findings from academia to be integrated into the models more quickly, thus strengthening risk management within the industry and helping insurers to more accurately quantify risk and, therefore, maintain insurability, as the level of risk changes. He also called for an integration of climate and risk models. The meeting raised a number of interesting questions and proceedings from the meeting will be made publicly available. The next meeting of the forum is scheduled for early summer in 2008 where the debate will continue.

CLIMATEWISE

A major development during the year was Lloyd's agreement to become a founding signatory of the new ClimateWise principles for the insurance industry. The principles provide a framework for insurance companies worldwide to tackle climate change and build solutions into their business operations. They were developed following consultation between The Prince of Wales's Business and the Environment Programme, Lloyd's, the ABI and other insurance market participants.

In September 2007, the principles were officially launched by HRH The Prince of Wales and to date 41 companies have signed up, including the Corporation and 17 managing agents in the Lloyd's market.

In signing up to ClimateWise, Lloyd's committed to take ongoing action under six main themes:

- Lead in risk analysis.
- Inform public policy making.
- Support climate awareness amongst our customers.
- Incorporate climate change into our investment strategies.
- Reduce the environmental impact of our business.
- Report and be accountable.

The ClimateWise principles provide a comprehensive framework for Lloyd's to address the significant social and economic impacts of climate change. The Corporation is working in partnership with the signatories from the market to track how Lloyd's is collectively, not just individually, making progress against the principles.

The primary vehicle for reporting progress will be the Lloyd's website, where up-to-date information will be posted. A summary so far can be found at www.lloyds.com/climatewise.

For more information on ClimateWise
visit: www.lloyds.com/climatewise

For more information on Lloyd's environmental policy
visit: www.lloyds.com/environment

THE MARKET'S FINANCIAL RESULTS

REPORT OF ERNST & YOUNG LLP TO THE COUNCIL OF LLOYD'S ON THE 2007 LLOYD'S PRO FORMA FINANCIAL STATEMENTS

We have examined the Lloyd's pro forma financial statements ('PFFS') for the year ended 31 December 2007, which comprise the pro forma profit and loss account, the pro forma statement of total recognised gains and losses, the pro forma balance sheet and the pro forma cash flow statement and the related notes 1 to 14 which have been prepared on the basis set out in note 2.

This report is made solely to the Council of Lloyd's in accordance with its instructions to us. Our work has been undertaken so that we might state to the Council those matters which we are required to state in this report in accordance with the Council's instructions and for no other purpose. To the fullest extent permitted by law, we do not accept or assume any responsibility to anyone other than the addressee of this report for our work, for this report, or for the conclusions we have formed.

RESPECTIVE RESPONSIBILITIES OF THE COUNCIL OF LLOYD'S AND ERNST & YOUNG LLP

The Council of Lloyd's is responsible for the preparation and approval of the PFFS.

Our responsibility is to examine the PFFS and to report to you whether the PFFS have been properly prepared in accordance with the basis of preparation set out in note 2.

BASIS OF CONCLUSION

The PFFS have been compiled in part from an aggregation of financial information extracted from the balance sheet and profit and loss account included in syndicate annual accounts by the managing agent of each syndicate, which has been submitted to the Council of Lloyd's and on which the auditors of each syndicate have reported. We have relied absolutely on those reports by syndicate auditors. We have not audited those extractions. Our work is solely intended to enable us to make this report.

Our work, which has been carried out in accordance with International Standard on Assurance Engagements, ISAE 3000, 'Assurance Engagements other than audits or reviews of Historical Financial Information', consisted principally of making enquiries of the Council of Lloyd's and applying analytical procedures to the financial information and underlying financial data. It excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions as included in the PFFS. We have also carried out such investigations and examined such evidence, on a test basis, as we considered necessary to form an opinion as to whether the PFFS have been properly prepared in accordance with the basis of preparation note 2.

However, our work provides less assurance than an audit or a review in accordance with International Auditing Standards. We have not performed an audit and, consequently, we do not express an audit opinion on the financial information set out in the PFFS.

CONCLUSION

In our opinion, the PFFS for the financial year ended 31 December 2007 have been properly prepared in accordance with the basis of preparation set out in note 2.

Ernst & Young LLP, London
2 April 2008

PRO FORMA PROFIT AND LOSS ACCOUNT

for the year ended 31 December 2007

Technical account	Note	2007 £m	2007 £m	2006 £m	2006 £m
Gross written premiums – continuing operations			**16,349**		16,390
– discontinued operations	5		**17**		24
	9		**16,366**		16,414
Outward reinsurance premiums			**(3,110)**		(3,213)
Premiums written, net of reinsurance			**13,256**		13,201
Change in the gross provision for unearned premiums		**(237)**		(644)	
Change in provision for unearned premiums, reinsurers' share		**78**		131	
			(159)		(513)
Earned premiums, net of reinsurance			**13,097**		12,688
Allocated investment return transferred from the non-technical account			**1,223**		957
			14,320		13,645
Claims paid					
Gross amount		**8,741**		11,718	
Reinsurers' share		**(2,515)**		(5,120)	
			6,226		6,598
Change in provision for claims					
Gross amount		**(1,278)**		(4,524)	
Reinsurers' share		**1,599**		4,145	
			321		(379)
Claims incurred, net of reinsurance			**6,547**		6,219
Net operating expenses	11		**4,451**		4,327
Balance on the technical account for general business			**3,322**		3,099
Attributable to: – continuing operations			**3,290**		3,032
– discontinued operations	5		**32**		67
Total			**3,322**		3,099
Non-technical account					
Balance on the technical account for general business			**3,322**		3,099
Syndicate investment return		**1,226**		957	
Notional investment return on funds at Lloyd's	6	**653**		651	
Investment return on Society assets		**128**		53	
		2,007		1,661	
Allocated investment return transferred to the technical account		**(1,223)**		(957)	
			784		704
Other income			**89**		68
Contribution to Equitas-Berkshire Hathaway transaction			**(90)**		–
Other expenses			**(259)**		(209)
Profit for the financial year before tax	8		**3,846**		3,662

Statement of total recognised gains and losses	Note	2007 £m	2006 £m
Profit for the financial year		**3,846**	3,662
Other recognised gains and losses		**106**	38
Total recognised gains and losses	8	**3,952**	3,700

PRO FORMA BALANCE SHEET

as at 31 December 2007

	Note	2007 £m	2007 £m	2006 £m	2006 £m
Investments					
Financial investments	12		**29,484**		27,165
Deposits with ceding undertakings			**9**		17
Reinsurers' share of technical provisions					
Claims outstanding		**7,449**		9,259	
Unearned premiums		**841**		771	
			8,290		10,030
Debtors					
Debtors arising out of direct operations		**3,428**		3,520	
Debtors arising out of reinsurance operations		**2,918**		3,190	
Other debtors		**318**		382	
			6,664		7,092
Other assets					
Tangible assets		**26**		22	
Cash at bank and in hand	13	**7,497**		7,926	
Other		**28**		20	
			7,551		7,968
Prepayments and accrued income					
Accrued interest and rent		**144**		98	
Deferred acquisition costs		**1,656**		1,582	
Other prepayments and accrued income		**155**		163	
			1,955		1,843
Total assets			**53,953**		54,115
Capital and reserves					
Members' funds at Lloyd's	6	**9,858**		11,282	
Members' balances	14	**2,652**		597	
Members' assets (held severally)		**12,510**		11,879	
Central reserves (mutual assets)		**939**		957	
	8		**13,449**		12,836
Subordinated debt			**516**		497
Subordinated perpetual capital securities			**496**		–
Capital, reserves and subordinated debt and securities			**14,461**		13,333
Technical provisions					
Provision for unearned premiums		**7,282**		7,024	
Claims outstanding		**28,971**		30,377	
			36,253		37,401
Deposits received from reinsurers			**42**		69
Creditors					
Creditors arising out of direct insurance operations		**697**		831	
Creditors arising out of reinsurance operations		**1,534**		1,643	
Other creditors including taxation		**774**		715	
			3,005		3,189
Accruals and deferred income			**192**		123
Total liabilities			**53,953**		54,115

Approved and authorised for issue by the Council of Lloyd's on 2 April 2008 and signed on their behalf by

Lord Levene of Portsoken, Chairman **Richard Ward, Chief Executive Officer**

PRO FORMA CASH FLOW STATEMENT

for the year ended 31 December 2007

	2007 £m	2006 £m
Profit on ordinary activities before tax	**3,846**	3,662
Depreciation	**3**	2
Realised and unrealised (gains)/losses and foreign exchange	**(157)**	3,466
Net purchase of investments	**(1,576)**	(3,770)
Notional return on funds at Lloyd's	**(653)**	(651)
Increase/(decrease) in technical provisions	**585**	(2,132)
Decrease in debtors	**243**	838
Decrease in creditors	**(15)**	(912)
Cash generated from operations	**2,276**	503
Income taxes (paid)/received	**(20)**	2
Net cash from operating activities	**2,256**	505
Cash flows from financing activities		
Net profits paid to members	**(1,537)**	(1,654)
Net movement in funds at Lloyd's	**(1,424)**	1,076
Capital transferred into syndicate premium trust funds	**322**	–
Interest paid	**(46)**	(46)
Net decrease in cash holdings	**(429)**	(119)
Cash holdings at 1 January	**7,926**	8,045
Cash holdings at 31 December	**7,497**	7,926

NOTES TO THE PRO FORMA FINANCIAL STATEMENTS

as at 31 December 2007

1. INTRODUCTION

Lloyd's is not an insurance company. It is a Society of members which underwrite insurance (each for their own account) as members of syndicates. The pro forma financial statements (PFFS) are prepared so that the financial results of Lloyd's and its members taken together and their net assets can be compared with general insurance companies.

2. BASIS OF PREPARATION

GENERAL

The PFFS include the aggregate of syndicate annual accounts (Aggregate Accounts), members' funds at Lloyd's (FAL) and the financial statements of the Society of Lloyd's (pages 114 to 151).

The aggregate of syndicate annual accounts report the audited results for calendar year 2007 and the financial position at 31 December 2007 for all syndicates which transacted business during the year. They include the syndicate level assets, which represent the first link in the chain of security (see pages 80 to 83). The Aggregate Accounts are reported as a separate document and can be viewed at www.lloyds.com/financialreports. During 2007, certain syndicates changed their accounting policies in relation to foreign exchange resulting in a restatement of the comparative figures for 2006 within their annual accounts and the Aggregate Accounts have been restated accordingly. The restatements are not material and, therefore, the comparative figures within the PFFS have not been restated.

The Aggregate Accounts do not present a consolidated view of the results of Lloyd's business taken as a single entity and, in particular, do not eliminate inter-syndicate reinsurances.

The capital provided by members is generally held centrally as FAL and represents the second link in the chain of security. The non-technical account of the PFFS includes a notional investment return on FAL.

The Society of Lloyd's audited financial statements report the central resources of the Society, which forms the third link in Lloyd's chain of security.

The profit and loss account in the PFFS aggregates the syndicate results, the notional investment return on members' capital and the results of the Society of Lloyd's. The balance sheet in the PFFS aggregates the assets held at syndicate level, members' assets held as FAL and the central resources of the Society. Overall, the PFFS aggregate the results and resources of the Society and its members and reflect all the links in Lloyd's chain of security as described in detail in the 'Security underlying policies issued at Lloyd's' section on pages 80 to 83. The PFFS may, therefore, be used as a reasonable presentation of the results and state of affairs of the Lloyd's market on a basis that is broadly comparable with general insurance companies.

TAXATION

The PFFS report the market's result before tax. Members are directly responsible for tax payable on their syndicate results and investment income on FAL. For consistency the results of the Society are also included pre-tax in the profit and loss account. The balance sheet includes the tax provisions in the Society financial statements.

FUNDS AT LLOYD'S

FAL comprise the capital provided by members to support their underwriting, and are the equivalent of capital shown in insurance companies' accounts. The valuation of FAL has, therefore, been included in the pro forma balance sheet.

FAL are available to meet cash calls made on the member in respect of a syndicate. The assets in FAL must be readily realisable, may include letters of credit and bank and other guarantees, and must be at least equivalent to the aggregate of the member's net economic capital assessment (ECA) requirement and certain liabilities in respect of its underwriting business. Each member's ECA to support its underwriting at Lloyd's is determined using Lloyd's Individual Capital Assessment (ICA) capital setting methodology.

A notional investment return on FAL has been calculated, which is the equivalent of insurance companies generating investment return on the capital that they hold to support their underwriting. The notional investment return is calculated on the average value of FAL during the year, based on indices yields on each type of asset held. The typical investment return on bank deposits has been applied to FAL provided as letters of credit or bank guarantees. The actual return achieved on FAL investments will differ from the notional return due to individual stocks held, daily cash flows and transactional charges.

SOCIETY OF LLOYD'S FINANCIAL STATEMENTS

The PFFS include the results and assets reported in the consolidated financial statements of the Society of Lloyd's, comprising the financial statements of the Society of Lloyd's and all its subsidiary undertakings, the Lloyd's Central Fund and the Society's interest in associates.

NOTES TO THE PRO FORMA FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

2. BASIS OF PREPARATION CONTINUED

TRANSACTIONS BETWEEN SYNDICATES AND THE SOCIETY

(1) Central Fund contributions, members' subscriptions and other market charges levied by the Society are reported as net operating expenses in the syndicate annual accounts and as income in the Society financial statements.

(2) Central Fund claims and provisions to discharge the liability of members where they have unpaid cash calls and do not have the resources to meet those cash calls are reported as a profit and loss charge and balance sheet liability in the Society financial statements. The Central Fund other income includes recoveries from insolvent members. The syndicate annual accounts for calendar year 2007 and earlier years include those members' results and at the balance sheet date will report the outstanding liability within members' balances.

(3) Syndicate loans to the Central Fund (and annual interest payments on the loans) are reported as assets (and accrued income) within the syndicate annual accounts within the comparative figures. The comparative figures of the Society financial statements report the loans as equity and account for interest payable when the Council formally approves interest payments. The loans were repaid during 2007.

(4) Loans funding statutory overseas deposits are reported as assets within the syndicate annual accounts and as liabilities in the Society financial statements.

Transactions between the syndicates and the Society which have been reported within both the syndicate annual accounts and the Society financial statements have been eliminated (note 8).

INTER-SYNDICATE LOANS

The syndicate annual accounts report debtor and creditor balances for inter-syndicate loans totalling £101m (2006: £372m). These amounts have been eliminated from the amounts reported in the balance sheet to provide a more meaningful presentation of the balance sheet for users of the PFFS.

THE SUBORDINATED DEBT AND SECURITIES

In accordance with the terms of the subordinated debt and securities, the capital raised is available for payment to policyholders in advance of repayment to the note holders and is included in 'capital, reserves and subordinated debt and securities' in the pro forma balance sheet.

3. ACCOUNTING POLICIES NOTES

A. AGGREGATE ACCOUNTS

General

Under the Insurance Accounts Directive (Lloyd's Syndicates and Aggregate Accounts) Regulations 2004, managing agents must prepare the syndicate annual accounts under UK GAAP. However, where UK GAAP permits different accounting treatments, each managing agent is able to adopt the accounting policies it considers most appropriate to its syndicate. The following accounting polices are, therefore, generic in nature.

Premiums written

Premiums written represent premiums on business incepting during the year, together with adjustments for premiums written in previous accounting periods. Premiums written are stated before deduction of commissions but net of taxes, duties levied on premiums and other deductions.

Unearned premiums

Written premiums are recognised as earned according to the risk profile of the policy. Unearned premiums represent the proportion of premiums written in the year that relate to unexpired terms of policies in force at the balance sheet date, calculated on the basis of established earnings patterns or time apportioned as appropriate.

Reinsurance premium ceded

Reinsurance premium ceded comprise the cost of reinsurance arrangements placed and are accounted for in the same accounting period as the related insurance contracts. The provision for reinsurers' share of unearned premiums represents that part of reinsurance premium written which is estimated to be earned in following financial years.

Claims provisions and related recoveries

Gross claims incurred comprise the estimated cost of all claims occurring during the year, whether reported or not, including related direct and indirect claims handling costs and adjustments to claims outstanding from previous years.

The provision for claims outstanding is assessed on an individual case basis and is based on the estimated ultimate cost of all claims notified but not settled by the balance sheet date, together with the provision for related claims handling costs. The provision also includes the estimated cost of claims incurred but not reported ('IBNR') at the balance sheet date based on statistical methods.

3. ACCOUNTING POLICIES NOTES CONTINUED

These methods generally involve projecting from past experience of the development of claims over time to form a view of the likely ultimate claims to be experienced for more recent underwriting, having regard to variations in the business accepted and the underlying terms and conditions. For the most recent years, where a high degree of volatility arises from projections, estimates may be based in part on output from rating and other models of the business accepted and assessments of underwriting conditions. The amount of salvage and subrogation recoveries is separately identified and, where material, reported as an asset.

The reinsurers' share of provisions for claims is based on the amounts of outstanding claims and projections for IBNR, net of estimated irrecoverable amounts, having regard to the reinsurance programme in place for the class of business, the claims experience for the year and the current security rating of the reinsurance companies involved. Statistical techniques are used to assist in making these estimates. The two most critical assumptions as regards claims provisions are that the past is a reasonable predictor of the likely level of future claims development and that the rating and other models used for current business are fair reflections of the likely level of ultimate claims to be incurred.

The directors of each syndicate's managing agent consider that the provisions for gross claims and related reinsurance recoveries are fairly stated on the basis of the information currently available to them. However, the ultimate liability will vary as a result of subsequent information and events, which may result in significant adjustments to the amounts provided. Adjustments to the amounts of claims provisions established in prior years are reflected in the financial statements for the period in which the adjustments are made. The methods used, and the estimates made, are reviewed regularly.

Unexpired risks provision

A provision for unexpired risks is made where claims and related expenses arising after the end of the financial period in respect of contracts concluded before that date, are expected to exceed the unearned premiums under these contracts, after the deduction of any acquisition costs deferred.

The provision for unexpired risks is calculated at syndicate level by reference to classes of business which are managed together, and may take into account relevant investment return.

Acquisition costs

Acquisition costs, comprising commission and other costs related to the acquisition of new insurance contracts are deferred to the extent that they are attributable to premiums unearned at the balance sheet date.

Foreign currencies

Income and expenditure in foreign currencies are translated into pound sterling using the exchange rates prevailing at the date of the transactions or, the average rate may be used when this a reasonable approximation.

Where the overseas operations for a syndicate are treated as a branch, its branch assets and liabilities are translated into pound sterling at the rates of exchange ruling at the balance sheet date. The exchange differences arising are normally accounted for through the statement of total recognised gains and losses.

For other overseas operations, monetary assets and liabilities are translated into pound sterling at the rates of exchange ruling at the balance sheet date. Resulting exchange differences on translation may be recorded in the profit and loss account or through the statement of total recognised gains and losses.

Investments

Investments are stated at current value at the balance sheet date. For this purpose listed investments are stated at their bid price market value, and deposits with credit institutions and overseas deposits are stated at cost.

Unlisted investments for which a market exists are stated at the average price at which they are traded on the balance sheet date or the last trading day before that date.

Syndicate Investment return

Syndicate investment return comprises all investment income, realised investment gains and losses and movements in unrealised gains and losses, net of investment expenses, charges and interest.

Realised gains and losses on investments carried at market value are calculated as the difference between sale proceeds and purchase price. Unrealised gains and losses on investments represent the difference between the valuation at the balance sheet date and their valuation at the previous balance sheet date, or purchase price, if acquired during the year, together with the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

Syndicate investment return is initially recorded in the non-technical account. A transfer is made from the non-technical account to the general business technical account where the investments generating the return relate to insurance business.

NOTES TO THE PRO FORMA FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

3. ACCOUNTING POLICIES NOTES CONTINUED

Taxation

Under Schedule 19 of the Finance Act 1993 managing agents are not required to deduct basic rate income tax from trading income. In addition, all UK basic rate income tax deducted from syndicate investment income is recoverable by managing agents and consequently the distribution made to members or their members' agents is gross of tax. Capital appreciation falls within trading income and is also distributed gross of tax.

No provision has been made for any United States Federal Income Tax payable on underwriting results or investment earnings. Any payments on account made by the syndicate during the year are included in the balance sheet under the heading 'other debtors'.

No provision has been made for any overseas tax payable by members on underwriting results.

Operating expenses

Operating expenses (including pension and other staff costs) have been charged to the syndicates in accordance with the policies adopted by the managing agents.

Profit commission

Where profit commission is charged by the managing agent it will normally be fully paid once the appropriate year of account closes, normally at 36 months. The profit commission is accrued in the profit and loss account in accordance with the earned profit.

Managing agents may make payments on account of their anticipated profit commission from the syndicate premiums trust funds prior to the closure of a year of account where they have transferred open year surpluses (interim profits) from the syndicate level premiums trust funds to the members' personal reserve fund. Any payments on account of such commission are restricted to the profit commission expensed in the profit and loss account in striking the level of interim profits declared and subsequently released.

B. FUNDS AT LLOYD'S

FAL are valued in accordance with their market value at the year end, and using year end exchange rates.

Investments are stated at current value at the balance sheet date. For this purpose, listed investments are stated at their bid price market value, and deposits with credit institutions and overseas deposits are stated at cost.

Unlisted investments for which a market exists are stated at the average price at which they are traded on the balance sheet date or the last trading day before that date.

In 2007 a rule change permitted any member that only participates on one syndicate to hold the capital supporting their underwriting in their syndicate's premium trust funds. Where a member takes advantage of this facility, the capital held in the premium trust fund is reported within members' balances and the investment return retained within the non-technical account.

C. SOCIETY OF LLOYD'S

The accounting policies adopted in the Society of Lloyd's financial statements are as set out on pages 117 to 122.

4. VARIABILITY

Calendar year movements in reserves are based upon best estimates as at 31 December 2007 taking into account all available information as at the balance sheet date. These estimates are subject to variability until the date at which the underlying claims are settled. Such changes in best estimate are reflected in the technical account of the year in which they occur.

5. DISCONTINUED OPERATIONS

Continuing/discontinued operations represent the analysis reported in the syndicate annual accounts between business that they are continuing to underwrite and business that they have ceased to underwrite. It is quite possible, however, that business discontinued by one syndicate continues to be written at Lloyd's by one or more other syndicates.

When a syndicate has ceased underwriting, their operations are reported as discontinued within the syndicate's annual accounts. Where the entire book of business continues to be written by another syndicate, however, an adjustment is made in the PFFS to reflect the continuing nature of this business to Lloyd's and its members as a whole.

Where business has been reported as discontinued in 2007, the results for that business have also been reported as discontinued in the 2006 comparative figures.

6. MEMBERS' FUNDS AT LLOYD'S

The valuation of members' FAL in the balance sheet totals £9,858m (2006: £11,282m).

The notional investment return on FAL included in the non-technical profit and loss account totals £653m (2006: £651m).

7. SOCIETY OF LLOYD'S

The results of the group financial statements of the Society included in the profit and loss account are a profit of £296m (2006: £275m) in the technical account and a loss of £132m (2006: £88m) in the non-technical account.

8. AGGREGATION OF RESULTS AND NET ASSETS

A reconciliation between the results, statement of realised gains and losses and net assets reported in the syndicate annual accounts, members' FAL and by the Society is set out below:

Profit and loss account	2007 £m	2006 £m
Result per syndicate annual accounts	3,029	2,826
Result of the Society	164	84
Central Fund claims and provisions (credit)/charge in Society financial statements	(18)	116
Central Fund recoveries from insolvent members	(48)	(20)
Taxation charge in Society financial statements	66	7
Interest receivable on syndicate loans to Central Fund accrued in syndicate annual accounts	–	(1)
Notional investment return on members' funds at Lloyd's	653	651
Elimination of prior year adjustment in syndicate annual accounts	–	(1)
Result on ordinary activities before tax	**3,846**	**3,662**

Statement of total recognised gains and losses	2007 £m	2006 £m
Result for the financial year	3,846	3,662
Other recognised gains and losses per syndicate annual accounts	69	42
Other recognised gains and losses of the Society	37	(1)
Elimination of prior year adjustment in syndicate annual accounts	–	(3)
Total recognised gains and losses	**3,952**	**3,700**

Capital and reserves	2007 £m	2006 £m
Net assets per syndicate annual accounts	2,523	653
Net assets of the Society	939	957
Central Fund claims and provisions	129	159
Members' funds at Lloyd's	9,858	11,282
Syndicate loans to Central Fund in syndicate annual accounts	–	(214)
Interest receivable on syndicate loans to Central Fund accrued in syndicate annual accounts	–	(5)
Elimination of prior year adjustment in syndicate annual accounts	–	4
Total capital and reserves	**13,449**	**12,836**

Transactions between syndicates and the Society which have been reported within both the syndicate annual accounts and the Society financial statements have been eliminated in the PFFS as set out in note 2.

NOTES TO THE PRO FORMA FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

9. SEGMENTAL ANALYSIS

The syndicate returns to Lloyd's provided additional information to derive the following table in respect of the classes of business reviewed in the market commentary.

2007	Gross written premiums £m	Net earned premium £m	Result £m
Reinsurance	**5,453**	**4.312**	**790**
Property	**3,809**	**2,975**	**408**
Casualty	**3,364**	**2,805**	**205**
Marine	**1,226**	**1,010**	**127**
Motor	**983**	**866**	**14**
Energy	**1,019**	**774**	**206**
Aviation	**464**	**323**	**50**
Life	**46**	**30**	**3**
Total from syndicate operations	**16,364**	**13,095**	**1,803**
Transactions between syndicates and the Society (notes 2 and 8) and insurance operations of the Society	**2**	**2**	**296**
Total per PFFS	**16,366**	**13,097**	**2,099**

2006	Gross written premiums £m	Net earned premium £m	Result £m
Reinsurance	5,557	4,186	802
Property	3,638	2,730	495
Casualty	3,572	2,964	327
Marine	1,153	921	105
Motor	923	829	30
Energy	1,125	737	9
Aviation	393	278	97
Life	50	40	2
Total from syndicate operations	16,411	12,685	1,867
Transactions between syndicates and the Society (notes 2 and 8) and insurance operations of the Society	3	3	275
Total per PFFS	16,414	12,688	2,142

10. LIFE BUSINESS

The PFFS include the results of all life and non-life syndicates transacting business during 2007. The results and net assets for life syndicates are not material and have not been separately disclosed in the profit and loss account and balance sheet. The results for life business are reported in the segmental analysis (note 9).

11. NET OPERATING EXPENSES

	2007 £m	2006 £m
Acquisition costs	**3,519**	3,354
Change in deferred acquisition costs	**(70)**	(163)
Administrative expenses	**1,117**	910
	4,566	4,101
(Profit)/loss on exchange	**(115)**	226
	4,451	4,327

12. FINANCIAL INVESTMENTS

	2007 £m	2006 £m
Shares and other variable yield securities and units in unit trusts	**3,075**	3,078
Debt securities and other fixed income securities	**20,811**	19,174
Participation in investment pools	**1,180**	813
Loans and deposits with credit institutions	**4,414**	4,093
Other	**4**	7
	29,484	27,165

13. CASH AT BANK AND IN HAND

Cash at bank and in hand includes letters of credit and bank guarantees held in trust within members' FAL to meet policyholder claims as required, totalling £5,399m (2006: £5,851m).

14. MEMBERS' BALANCES

	2007 £m	2006 £m
Balance at 1 January	**597**	(408)
Result for the year per syndicate annual accounts	**3,029**	2,826
Distribution on close of 2004 (2003) year of account	**(1,204)**	(1,956)
Advance distributions	**(414)**	(296)
Cash calls	**79**	571
Capital transferred into syndicate premium trust funds	**322**	–
Repayment/(collection) of syndicate loans to the Central Fund	**214**	(107)
Other movements	**29**	(33)
Balance at 31 December	**2,652**	597

Members participate on syndicates by reference to years of account. Members' ultimate results, assets and liabilities are assessed by year of account with reference to policies incepting in that year of account. Members' balances represent the net profit/(loss) to be distributed/(collected) by syndicates to/(from) the members. Where there are profits and funds at Lloyd's held in excess of members' capital requirements, they will be distributed in the second quarter of 2008.

In 2007 a rule change permitted any member that only participates on one syndicate to hold the capital supporting their underwriting in their syndicate's premium trust funds. Where a member takes advantage of this facility, the movement is reflected in the above table as 'capital transferred into syndicate PTFs'.

SECURITY UNDERLYING POLICIES ISSUED AT LLOYD'S

as at 31 December 2007

SUMMARY

Lloyd's is not an insurance company. It is a Society of members, both corporate and individual, which underwrite insurance in syndicates. These syndicates can comprise one single corporate member or any number of corporate and individual members, underwriting severally for their own account.

There were 72 syndicates, (including syndicates set up to accept RITC of orphan syndicates and Special Purpose Syndicates) as at 31 December 2007, registered to conduct business at Lloyd's. Each syndicate is managed by a managing agent. Managing agents write insurance business on behalf of the member(s) of the syndicate, which receive profits or bear losses in proportion to their share in the syndicate for each underwriting year of account. The adoption of annual accounting and presentation of the syndicate annual accounts do not change the allocation of profits and losses to members.

THE LLOYD'S CHAIN OF SECURITY

The three key features of the Lloyd's chain of security provide strong security to all Lloyd's policyholders, reflected in the high ratings assigned by leading rating agencies.

The first two links in the Lloyd's chain of security each operate on a several basis: each member's resources are only available to meet their share of claims. The third link represents assets available to meet the liabilities of any member on a mutual basis. The key features of the chain of security are summarised below and the sections which follow describe each of these links in greater detail.

The chain of security supports policies written for the 1993 and subsequent years of account for non-life business and all life business written at Lloyd's. Liabilities in relation to the 1992 and prior years of account for non-life business were reinsured into Equitas as at 31 December 1995, as part of 'Reconstruction and Renewal'.

First link – syndicate level assets
All premium receipts and reserves at syndicate level are held in premiums trust funds or overseas regulatory deposits. Profits are distributed only after provision for all outstanding liabilities.

Second link – members' funds at Lloyd's (FAL)
The capital provided by every member is assessed according to the Lloyd's Individual Capital Assessment (ICA) capital setting framework. When agreed, each ICA is then 'uplifted' (by 35% for 2007) to provide an extra buffer to support Lloyd's rating and financial strength. This uplifted ICA, which is the Economic Capital Assessment (ECA) is used to determine members' capital requirement subject to prescribed minimum levels.

The FSA delegates the annual review of syndicate ICAs to the Corporation, who review the historical performance, business plans and risk appetite of that syndicate in assessing the adequacy of the capital level proposed. The FSA reviews a small sample of syndicate ICAs in order to validate the effectiveness of the reviews carried out by the Corporation.

Third link – central assets
At the discretion of the Council, the Central Fund is available to meet any portion of any member's insurance liabilities that the member is unable to meet in full.

THE FIRST LINK

The first link in the chain of security is the member's premiums trust funds, and other assets held in trust at syndicate level. To protect the interests of policyholders, all premiums and other monies received or receivable in connection with the member's underwriting business are initially paid into the premiums trust funds of the syndicate concerned. Payments from these funds may only be made to meet permitted trust outgoings: claims, reinsurance premiums, underwriting expenses and the like, including funding overseas regulatory deposits. Profit is not distributed until provision has been made for all outstanding liabilities.

There are separate premiums trust funds for life business and non-life general business. There is a further segregation in that a number of the premiums trust funds are exclusively available to support certain overseas underwriting of members. The Lloyd's Dollar Trust Funds (LDTF) receive premiums in respect of US dollar denominated non-life business underwritten or incepting on or after 1 August 1995. Receipts in respect of non-life US dollar denominated business originally written and incepting before that date are held in the Lloyd's American Trust Fund (LATF) of each member, in New York. There are separate LATFs in New York for US dollar denominated life business, whenever written or incepting.

The other overseas premiums trust funds are the Lloyd's Canadian Trust Fund (LCTF) in Canada, comprising members' underwriting receipts in respect of Canadian situs business and the Lloyd's Asia trust funds for general business written by members through service companies in Singapore.

Members must ensure that there are sufficient funds in the members' premiums trust fund for the syndicate to meet all claims, necessary expenses and outgoings in connection with the syndicate business; they are required to meet a request to make such funds available (a 'cash call'). Cash calls are met by members from their own resources or, if necessary, from their FAL or, at the Council's discretion, the New Central Fund.

Premiums trust funds are used to fund overseas regulatory deposits. The US situs business of each syndicate is supported by US situs syndicate level trust funds (for US situs surplus lines business, US situs reinsurance business as accredited reinsurers, and for Illinois and Kentucky licensed business respectively). In addition, separate joint asset trust funds provide joint security for members' US situs surplus lines, US situs reinsurance and Kentucky business respectively.

These deposits would be available to meet judgment debts of a member in respect of business connected with the relevant overseas territory in the event that the relevant premiums trust fund of the member, even after replenishment from other links in the chain of security and other free assets of the member in question, was inadequate.

Underwriters also maintain regulatory deposit trust funds in Australia and South Africa and various deposits in other countries.

The total value of all the above funds was £30,601m at 31 December 2007.

THE SECOND LINK

The second link is members' capital provided to support their underwriting. This is commonly held as FAL but from 1 July 2007 can be held by aligned corporate members within the premiums trust fund (see first link above). FAL comprise the three trust funds in which members' assets may be held: the Lloyd's deposit, the special reserve fund and the personal reserve fund. These are each available to meet cash calls made on the member in respect of a syndicate. The assets in FAL must be readily realisable, this includes letters of credit and bank and other guarantees. A member is required to have sufficient assets at least equivalent to the aggregate of the member's ECA and certain liabilities in respect of its underwriting business. The amount of FAL assets required will depend on the net open year underwriting position of the member i.e. if the net open year position is a deficit then the member will be required to add additional FAL to cover this deficiency, if the net open year position is a surplus the member can use these surplus assets towards their ECA requirement thus reducing the value of their assets to be held as FAL.

Minimum capital ratios are set at 40% of overall premium limits (25% for those members writing mainly EU motor business).

Individual members underwrite with unlimited liability and thus may be required to meet their share of claims to the full extent of their wealth. A corporate member may also have assets, beyond its capital to support underwriting, which can be called upon to meet its underwriting liabilities.

As at 31 December 2007, the total value of capital supporting underwriting held in trust by members amounted to £9,858m in the aggregate.

THE THIRD LINK

The third link is the central resources of the Society. These are the assets of the Central Fund (comprising the New Central Fund and the 'Old' Central Fund) and other assets of the Society.

The New Central Fund has been established to be available, at the discretion of the Council of Lloyd's, to ensure that policyholders' claims are met in the event of members being unable to meet their underwriting liabilities relating to 1993 and post non-life business and all life business. In practice, this entails the payment of syndicate cash calls where a member is unable to do so from their FAL or their own resources.

The New Central Fund is funded by annual contributions from members.

The net assets of the Central Fund as at 31 December 2007 were £767m.

In 2004 and 2007, Lloyd's issued subordinated loan notes and perpetual capital securities respectively which, as at 31 December 2007, are included as a liability of £1,012m within the Society's financial statements. As set out in note 17 to the Society's financial statements, payments on the notes are subordinated to certain payments which may be made out of central assets, including payments made to discharge the liabilities of an insolvent member to any person (including any policyholders) arising out of or in connection with insurance business carried on at Lloyd's by that insolvent member.

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 (described and included in the first link).

In addition, the other assets of the Society, totalling £172m at 31 December 2007, are available to meet underwriting liabilities in the last resort.

In aggregate, the value of the central resources of the Society (excluding the subordinated debt liability and the callable layer), amounted to £1,951m at 31 December 2007.

AGGREGATE RESOURCES

The total of syndicate assets, members' capital to support underwriting (i.e. funds at Lloyd's and capital held in syndicate premiums trust funds) and central resources of the Society as at 31 December 2007 was £42,410m. The total of net syndicate technical provisions at the end of 2007 was £27,949m. The total net resources of the Society and its members were therefore £14,461m (excluding the subordinated debt liability) as shown in the PFFS on page 71.

The results on which the aggregated resources are based are determined by aggregating the assets and liabilities of all members and those of the Society. The aggregate declared resources of the Society do not represent a consolidated statement of the financial position of Lloyd's business taken as a single entity and, as indicated above, the first two links of the chain of security operate on a several, not mutual, basis.

SECURITY UNDERLYING POLICIES ISSUED AT LLOYD'S CONTINUED

as at 31 December 2007

SOLVENCY CONTROLS

One of the most important controls on the solvency of the members of Lloyd's is the annual solvency test.

The annual solvency process requires the managing agent of each syndicate to estimate and provide for all current and future liabilities for each year of account. These liabilities 'technical provisions for solvency' are subject to a statement of actuarial opinion. The requirement for an opinion and its required wording that the net technical provisions for solvency are *not less than* the current and future liabilities is a higher test than required in the UK company market. In the event that it is not possible for the managing agent to secure an unqualified actuarial opinion for any reason, the technical provisions for solvency would be determined by the Lloyd's Actuary, who would provide a report to the FSA. In addition, any syndicate which is not able to secure an unqualified actuarial opinion will normally be subject to a monitoring review by Lloyd's. There were no qualified actuarial opinions as at 31 December 2007.

The Lloyd's solvency test has two stages to the calculation:

Firstly, each member's solvency position is calculated. Each member must have sufficient assets – those held in the premiums trust funds, overseas regulatory deposits and its capital to support underwriting – to cover its underwriting liabilities and on top of this an additional margin known as the member's capital resources requirement (MCRR). The MCRR is calculated separately for each member, determined as the greater of 16% of annual premium income or 23% of average claims incurred over a three-year period. Premiums and claims in respect of certain types of liability business have their value increased by 50%, for the purpose of this calculation. Where a member's assets are not sufficient to cover the aggregate of its underwriting liabilities and its MCRR, the member has a solvency shortfall.

The second part of the solvency test calculation requires that the net central assets of the Society must be sufficient to cover the aggregate of all members' shortfalls calculated at the solvency test date. Central assets include the value of the Central Fund and the other net assets of the Society, excluding the subordinated debt liability but including the callable layer – for this purpose, the 'effective' callable layer, i.e. that part of the callable layer not attributed to members with a solvency shortfall.

Lloyd's is required to maintain solvency on a continuous basis, and the solvency position of each member – and thus of Lloyd's as a whole – is monitored on a regular basis. The FSA are advised of the results of this monitoring.

RECAPITALISATION AT MEMBER LEVEL

The free funds available to a member to meet its capital requirements may fall below the required level for two reasons: firstly, increases to syndicate ICAs, following a material change to the risk profile of the business; or secondly, erosion of funds due to losses.

In either case, the timetable for recapitalisation and the intervention by Lloyd's will depend on the extent of the shortfall.

All members are subject to bi-annual (June and November) Coming into Line (CIL), where members are required to hold free funds to meet their ECA. Lloyd's has powers to require members to meet their ECA at all times, but will normally permit recapitalisation in accordance with this bi-annual timetable, provided that members' free funds remain above their ICA. Where a member's funds fall below their ICA level, Lloyd's would expect members to inject additional capital outside of the normal CIL timetable. Where there is material exposure to the central fund and policyholder security, underwriting restrictions or other measures may be imposed to mitigate the risks until capital is lodged at Lloyd's.

In accordance with the continuous solvency regime, where a member's free funds fall below the level of regulatory solvency (underwriting losses plus MCRR), the existing powers to immediately suspend underwriting or take any other measures deemed appropriate to Lloyd's may be used.

THE LLOYD'S RETURN

Each year, Lloyd's files the Lloyd's Return with the FSA. This return is intended to ensure Lloyd's regulatory reporting requirements are in line with other UK insurers, adapted where appropriate to reflect Lloyd's unique structure. This return reports the results of the Lloyd's solvency test.

SECURITY UNDERLYING POLICIES ISSUED AT LLOYD'S: FINAL SUMMARY

as at 31 December 2007

	2007 £m	2006 £m
I Syndicate level assets (several basis)	**30,601**	28,173
Elimination of syndicate loans to Central Fund and annual interest receivable	**–**	(219)
	30,601	27,954
II Members' funds at Lloyd's (several basis)	**9,858**	11,282
III Central assets (mutual basis)		
Net Central Fund assets	**767**	843
Subordinated loan notes	**516**	497
Subordinated Perpetual Capital Securities	**496**	–
Other net assets of the Society	**172**	114
	1,951	1,454
Total resources of the Society of Lloyd's and its members	**42,410**	40,690
Net syndicate technical provisions	**(27,949)**	(27,357)
Total net resources of the Society of Lloyd's and its members	**14,461**	13,333

Notes

1. This financial summary has been compiled by aggregating the assets and liabilities of all the underlying syndicates, the declared members' qualifying assets and other net assets of the Society of Lloyd's. The statement does not purport to disclose the solvency position of each member of Lloyd's.

2. The 'total net resources of the Society of Lloyd's and its members' represents the capital, reserves and subordinated notes and securities shown in the PFFS as set out on page 71.

3. In July 2007 the Council of Lloyd's repaid the syndicate loans made to the New Central Fund.

4. Syndicate level assets includes capital to support underwriting held by aligned corporate members in the syndicate premiums trust fund.

SOCIETY REPORT

THIS REPORT

This Report sets out the principal activities, 2007 consolidated financial statements and governance arrangements of the Society of Lloyd's.

In order to obtain an overview of the Society's operations, however, this Report should be read in conjunction with the following sections of the Annual Report that look more generally at the Lloyd's market as a whole:

The Lloyd's market comprises members underwriting through syndicates and members' and managing agents each supported by the Society of Lloyd's. The interests of the Society and the market are inter-related and therefore the sections above may refer to both.

The Society's 2007 consolidated financial statements are included in this Report together with a financial review. The financial results of the members of Lloyd's are not part of those financial statements but can be found within the Market results section starting on page 68.

THE SOCIETY

By Lloyd's Act 1871, the then existing association of underwriters was incorporated as the Society and Corporation of Lloyd's (the 'Society').

Its activities are governed by statute and, since 1982, have been managed by the Council of Lloyd's pursuant to Lloyd's Act 1982.

The Society is not an insurance company, although the group does include insurance company subsidiary undertakings.

Its principal activities are:

- To facilitate the carrying on of insurance business by members of Lloyd's, who join together as syndicates to insure and reinsure risks, and the protection of their interests in this context.
- To maintain the Lloyd's Central Fund where assets are held and administered at the discretion of the Council of Lloyd's, primarily as funds available for the protection of policyholders.

FINANCIAL HIGHLIGHTS

	2007 £m	2006 £m	2005 £m	2004 £m
Operating result				
Operating and other group income	**262**	198	184	201
Central Fund contributions	**168**	152	70	191
Total income	**430**	350	254	392
Central Fund claims and provisions released/(incurred)	**18**	(116)	(224)	(126)
Contribution to Equitas – Berkshire Hathaway transaction	**(90)**	–	–	–
Net insurance claims and provisions	**(1)**	2	–	5
Other group operating expenses	**(188)**	(171)	(172)	(173)
Operating surplus/(deficit)	**169**	65	(142)	98
Profit on sale of Lloyd's buildings	**–**	–	–	24
Surplus/(deficit) before finance, associates and tax	**169**	65	(142)	122
Net finance income and unrealised exchange differences on borrowings	**57**	24	95	38
Share of profits of associates	**4**	2	2	2
Surplus/(deficit) before tax	**230**	91	(45)	162
Tax (charge)/credit	**(66)**	(7)	17	(39)
Surplus/(deficit) for the year	**164**	84	(28)	123
Balance sheet				
Net assets	**939**	957	765	690
Movement in net assets %	**(1.9%)**	25.1%	10.9%	22.1%
Solvency*				
Central assets for solvency purposes	**2,457**	2,054	1,850	1,663
Solvency shortfalls	**(168)**	(253)	(482)	(554)
Excess of central assets over solvency shortfalls	**2,289**	1,801	1,368	1,109
Solvency ratio %	**1,463%**	812%	384%	300%
Movement in central assets for solvency purposes %	**19.6%**	11.0%	11.2%	194.3%

*The solvency positon for 2007 is estimated and will be finalised in June 2008 for submission to the FSA

CORPORATE GOVERNANCE

The Council of Lloyd's is committed to good corporate governance and supports the application of the principles of the Combined Code on Corporate Governance, as far as they can be applied to the governance of a Society of members and a market of separate, competing entities.

GOVERNING BODY: THE COUNCIL OF LLOYD'S

Under Lloyd's Act 1982, the governing body of the market is the Council of Lloyd's. Under the Act, 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. In addition, the Council also has the power to make byelaws for the proper and better execution of the Lloyd's Acts and the furtherance of the objects of the Society, and for various specific purposes set out in the Act.

The members of the Council as at 2 April 2008 are listed on page 18. The Council comprises six working and six external members, together with six nominated members. Nominated members are usually appointed for three-year terms which can be renewed. Working and external members are generally elected for terms of three years by the working and external members of the Society respectively.

In accordance with Lloyd's Act 1982, the Chairman and Deputy Chairmen of Lloyd's are elected annually by the Council from among the working members of the Council.

The Chairman of Lloyd's commits as much time as is necessary to successfully undertake the role. The Council acknowledges that the Chairman has other commitments outside Lloyd's and is satisfied that these can be accommodated with the Chairmanship of Lloyd's.

The nominated members of the Council may be regarded, for the purposes of the Combined Code, as independent members of the Council with the exception of the CEO who is included within their number. Although the concept of a senior independent director does not strictly apply to the Council, Bill Knight (a nominated member) was elected a Deputy Chairman of the Council by the Council.

In the elections for working members of the Council, voting operates on a one member, one vote basis. In the elections for external members of the Council, the voting entitlement of an external member of the Society is based on the member's allocated underwriting capacity as determined under the Council and Committee Byelaw. The Council reports to the members at the Annual General Meeting. Voting entitlement at general meetings is generally capacity-based for both external and working members, except at general meetings called on the requisition of members under section 6(4) of the Lloyd's Act 1982 for the purpose of revoking or annulling byelaws, at which each member has one vote. The Council met 6 times in 2007.

GOVERNANCE POLICIES

Amongst other matters, the Governance Policies as agreed by the Council, are intended to provide clarity around the role of the Council and to maintain a structured relationship with the Franchise Board.

The Governance Policies established the Purpose for Lloyd's: 'To maintain, in accordance with Lloyd's Acts, an organisation that will enable the long-term return from carrying out the business of insurance to be maximised for capital providers' (ie members).

The Governance Policies also established the process by which the Council manages its own activities and affairs. There are certain matters that only the Council can deal with under the terms of the Lloyd's Acts – for example, the making and amending of byelaws. In addition, the Council reserves to itself the ability to set the level of contributions to the New Central Fund and the amount of the annual subscription, the right to appoint members of the Franchise Board and other committees of the Council and reviewing the budget and the Franchise Board's Three-Year and Annual Plans. The Council must approve all expenditure above a specified amount.

Under the Governance Policies, the Council is responsible for assessing the long-term strategic development of Lloyd's by reference to the interests both of capital providers and / or other stakeholders and through an evaluation of economic, political and social issues impacting the international insurance and reinsurance markets.

In respect of the majority of its other functions, the Council acts by the Franchise Board. The Governance Policies therefore define the accountability linkage between the Franchise Board and the Council. This includes determining the boundaries within which the Franchise Board will operate (the Franchise Board Limitations) and establishing a Monitoring and Assurance regime which, amongst other matters, requires the Chairman of the Franchise Board to report to the Council on all material issues impacting the world insurance market and Lloyd's as well as providing a summary of key performance indicators.

LLOYD'S ACT 1982 – LEGISLATIVE REFORM ORDER

In June 2007, the Government announced that HM Treasury ('HMT') would be developing proposals to modernise the governance arrangements at Lloyd's by way of a Legislative Reform Order ('LRO') amending Lloyd's Act 1982. A formal public consultation on HMT's proposed reforms of Lloyd's Act 1982 is currently underway. After the formal public consultation period closes on 30 May 2008, the LRO will require Parliamentary approval before the proposed reforms can come into effect.

If Parliamentary approval of the LRO is obtained, a number of provisions in the Act would be updated or removed. These would include removing the statutory restrictions on the re-election of working members; the removal of the requirement that the Chairman of Lloyd's may only be elected from among the working members of Council; the removal of the requirement for the Governor of the Bank of England to confirm the appointment of nominated members of Council; and modernising the rules on membership of disciplinary committees. Furthermore, if approved the LRO would remove the requirement that managing agents generally only accept insurance business from or through a Lloyd's broker (although the class of Lloyd's brokers would continue to exist for those that wished to describe themselves as 'Lloyd's brokers') and would remove the associated 'divestment provisions' that prohibit prescribed associations between managing agents and Lloyd's brokers.

CORPORATE GOVERNANCE CONTINUED

FRANCHISE BOARD

The Council established the Franchise Board as from 1 January 2003 and set it a goal: 'To create and maintain a commercial environment at Lloyd's in which the long-term return to all capital providers is maximised'. The Franchise Board must operate within the boundaries of the limitations established by the Council which include operating in accordance with the Franchise Principles. The latter cover three main areas: the overriding principles (relating to legal, regulatory and corporate governance); the capital principles (which emphasise equity between capital providers and prudence in capital setting); and the operating principles (including setting the market supervision framework in accordance with FSA requirements).

The members of the Franchise Board as at 2 April 2008 are listed on page 19. In 2007, the Franchise Board comprised the Chairman of Lloyd's, who was also its Chairman, the CEO, the Franchise Performance Director and the Director, Finance, Risk Management and Operations, with the balance of the Board made up of three non-executives connected with the Lloyd's market and three independent non-executives. The Franchise Board held 11 meetings in 2007. It also held one half day off-site meeting.

The main committees of the Franchise Board and their purpose are outlined below.

MARKET SUPERVISION AND REVIEW COMMITTEE (MSARC)

MSARC acts as a review body capable, where appropriate, of amending, modifying or withdrawing certain decisions taken by the executive affecting managing agents. It also acts as the body that determines whether certain decisions can be referred to the Lloyd's Appeal Tribunal and can also make certain business decisions itself. MSARC also takes decisions regarding the exercise of Lloyd's enforcement powers. The MSARC met on 4 occasions in 2007.

CAPACITY TRANSFER PANEL

The Capacity Transfer Panel has been established principally to exercise the Council's powers in relation to minority buyouts and mergers. The Panel met on 6 occasions in 2007.

INVESTMENT COMMITTEE

The Investment Committee sets the investment objectives and parameters of centrally managed assets and is responsible for monitoring the performance of these funds. In addition, it monitors the investment operations of the Lloyd's Treasury department in respect of all funds under its management and approves all investment counterparties. It may also make more general recommendations concerning investment activity at Lloyd's. The Investment Committee met on 4 occasions in 2007.

OTHER PRINCIPAL COMMITTEES OF THE COUNCIL

AUDIT COMMITTEE

The Audit Committee's role ensures that the financial activities of Lloyd's are subject to independent review and audit. The Audit Committee reviews Lloyd's annual and interim financial statements, the aggregate syndicate results and the Lloyd's Return to the FSA. It also reviews both the external and internal audit plans and the compliance plan. The CEO, Director, Finance, Risk Management and Operations, General Counsel, senior managers and external and internal auditors attend meetings as appropriate. Reports from internal and external auditors on aspects of internal control and reports from the Head of Internal Audit and Compliance on internal and overseas compliance are reviewed by the Audit Committee and appropriate action taken in response. The Audit Committee met on 5 occasions in 2007.

The terms of reference of the Audit Committee are available from the Secretary to the Council on request.

NOMINATIONS, APPOINTMENTS AND COMPENSATION COMMITTEE (NACC)

The NACC is principally responsible for making recommendations to the Council on the appointment of the Chairman, CEO, nominated Council members, Franchise Board members (including the Director, Finance, Risk Management and Operations and Franchise Performance Director), members of a number of the Council and Franchise Board committees and the Secretary to the Council. The NACC reviews and makes recommendations to Council regarding the remuneration of the members of these bodies. The NACC is also responsible for succession planning arrangements for these positions. The NACC met on 4 occasions in 2007.

The terms of reference of the NACC are available from the Secretary to the Council on request.

PERFORMANCE ASSESSMENT

An evaluation of the performance of the Council and its principal committees in 2007 (defined for this purpose as the Franchise Board, the Audit Committee and the NACC) was undertaken during the year. The evaluation also covered the performance of the Council and committee members including the chairman of each committee.

The assessment was conducted by the Secretary to the Council who met all Council and committee members on an individual basis to seek their views on 2007 performance. These discussions were based around the Performance Evaluation Guidance in the Higgs report on the 'Review of the role and effectiveness of non-executive directors'. As part of this process, Council and Franchise Board members' comments on the performance of the Chairman were discussed privately with him. The same process was followed with the chairmen of the other committees subject to the performance assessment.

The principal conclusion of the assessment was that the current governance arrangements were working effectively and in accordance with the Governance Policies, although the latter had yet to be fully tested bearing in mind relatively benign market conditions since the introduction of the Policies in 2006.

Amongst the other major findings of the review were:

- A view that the wider market might not have a full understanding of the respective roles and responsibilities of the Council and the Franchise Board as outlined in the Governance Policies.
- A need to develop a more formal mechanism for the non-executive Franchise Board members to input into the NACC's review of the executive's performance.
- The executive to ensure that non-operational issues are put to the Franchise Board at a sufficiently early stage to enable debate to be conducted at the level of principle.

These and other suggestions for performance improvements for individual committees subject to the assessment will be taken forward by those committees.

TRAINING AND INDUCTION

As part of the induction process, new members of the Council and Franchise Board without extensive knowledge of Lloyd's are offered briefing sessions with senior executive management and others. Members of the Council and Franchise Board with pre-existing knowledge and involvement at Lloyd's are given the opportunity to receive briefings on subjects of particular interest to them.

In 2007, briefing sessions on a range of Lloyd's related topics were made available to all members of the Council and the Franchise Board.

INDEPENDENT PROFESSIONAL ADVICE

Members of the Council and Franchise Board have access to independent professional advice, if required.

AUTHORITY TO ACT

The Franchise Board may act through the CEO, directors and employees of the Corporation save in respect of those functions and powers reserved to it, the Council and their committees. The CEO, directors and employees must act in accordance with the Franchise Board Limitations (including the Franchise Principles) and in accordance with the Franchise Goal and Principles and in accordance with the strategy, policy and principles set by the Franchise Board. During 2007 the Franchise Board reviewed, and were satisfied with, the scope of the current authorities exercisable by the executive.

CORPORATE GOVERNANCE OF THE LLOYD'S MARKET

The corporate governance of each entity within the Lloyd's market is the responsibility of that entity. The Council provides, through the Corporation, a framework for the governance of these businesses including the assessment of capital adequacy and market supervision (including inspections, visits and audits of market entities). Managing agents' governance arrangements are also reviewed on registration and as part of risk management assessments.

ATTENDANCE RECORD

	Council	Franchise Board	Audit Committee	NACC[1]	MSARC[2]	CTP	Investment Committee
Council and Franchise Board members:							
Chairman of the Council of Lloyd's:							
Lord Levene of Portsoken	[a]6/6	[a]11/11					
Executive Directors							
Richard Ward	6/6	11/11					
Luke Savage		10/11					4/4
Rolf Tolle		11/11					

CORPORATE GOVERNANCE CONTINUED

ATTENDANCE RECORD CONTINUED

	Council	Franchise Board	Audit Committee	NACC[1]	MSARC[2]	CTP[3]	Investment Committee
Non-Executive Council members							
Rupert Atkin	5/6			3/3			
Ewen Gilmour	6/6		4/5	2/4			
Nigel Hanbury	5/6			3/3			
Christopher Harman	5/6						
Graham White	6/6						
External members							
Alan Lovell	5/6					6/6	
Barbara Merry	5/6						
Peter Morgan	6/6			3/4			
Dermot O'Donohoe	5/6						
David Shipley	5/6		5/5				
Anthony Townsend	5/6			3/3			
Nominated members							
Celia Denton	5/6		5/5		4/4		
Reg Hinkley	1/1						
Bill Knight	6/6		4/5	[a]4/4	[a]3/3		
Philip Lader	4/6			2/3			
Andreas Prindl	6/6		5/5			[a]6/6	[a]4/4
Non-Executive Franchise Board members							
Roy Brown		10/11					
Steven Burns		10/11					
Edward Creasy		10/11					
Stephen Hodge		10/11	[a]5/5				
Andrew Kendrick		6/10					
Jim Stretton		10/11	5/5				
Former Council members							
Christine Dandridge				1/1			
Judith Hanratty	3/4			2/3	[a]2/2		
Bronek Masojada				1/1			
Charles Philipps				1/1			
Other Committee members							
Ian Agnew					4/4		
Lady Delves Broughton						6/6	4/4
Margaret Chamberlain						5/6	
David Gilchrist					4/4		
David Gittings						6/6	
Mark Graham							4/4
Michael Green							4/4
Richard Hextall							2/2
Ian Salter						5/6	
Paul Swain						5/6	
David Winkett							2/2

[a] Chairman

1 Nominations, Appointments and Compensation Committee

2 Market Supervision and Review Committee

3 Capacity Transfer Panel

INTERNAL CONTROL STATEMENT

The Franchise Board, on behalf of the Council of Lloyd's, has responsibility for the Society's system of internal control and for reviewing its effectiveness. The Executive Team is responsible for the implementation and maintenance of the internal control system. This incorporates an embedded, ongoing process for identifying, evaluating and managing significant business, operational, financial, compliance and other risks. The system is designed to reduce, rather than eliminate, the risk of failure to achieve business objectives and can only provide reasonable but not absolute assurance against material misstatement or loss.

The Audit Committee monitors and reviews the effectiveness of the system of internal control of the Society and biannual reports are provided to the Franchise Board. There is an ongoing process, in accordance with the guidance of the Turnbull Committee on internal control, which has been established for identifying, evaluating and managing significant risks. Other procedures such as whistle-blowing whereby any member of staff may take matters that concern them to the Head of Internal Audit and Compliance or, where appropriate, to the Chairman or Deputy Chairman of the Audit Committee or the FSA, are clearly set out. This process has been in place throughout 2007 and up to the date of the approval of the financial statements. Associate companies, Ins-sure Holdings Limited and Xchanging Claims Services Limited, are not dealt with as part of the group for the purposes of applying the Turnbull Guidance.

The group's key risk management processes and the system of internal control procedures include the following:

MANAGEMENT STRUCTURE

'Lloyd's Governance Arrangements: The Guide for Members of Lloyd's Committees' outlines the governance structure and committee members' duties and responsibilities, including confidentiality; and conflicts and declaration of interest.

There is a clearly defined organisation structure with terms of reference agreed for the CEO and all directors which set out, inter alia, their functions and powers, authority to act and limitations on authority. Employees have role profiles agreed by their line manager which set out equivalent information.

The Society is committed to the highest standards of business conduct. Corporate policies and procedures are available to all staff and include the Compliance Manual, Employee Handbook, Health & Safety Policy, Information Security and Computer Usage Policy, Procurement Policy, Financial Policies and authorisation limits.

Lloyd's maintains an internal audit function that reports to the CEO and the Audit Committee. The Head of Internal Audit and Compliance is supported by KPMG LLP who provide resources to complete the internal audit plan.

IDENTIFICATION AND EVALUATION OF BUSINESS RISKS

A Risk Management Framework has been developed in recent years to identify, assess and monitor the major risks affecting the Society. A comprehensive franchise risk and control assessment was provided on a quarterly basis during 2007. This review re-assesses the existing risks and identifies any new risks. It evaluates controls in terms of adequacy of design and performance and also seeks to monitor the action plans in place to help manage risks. These processes are described in more detail in the Risk Management section on pages 38 to 41.

A Risk Committee, a sub-committee of the Executive Team, considers the different aspects of the assessment of the risk, control and regulatory environment. This includes determining and assessing the Society's inherent and residual risks, compliance and monitoring of control exceptions. Its function is to provide assurance that the Society and franchise risks are identified and managed in accordance with approved policy and appetite.

A framework of self-certification is in place; quarterly for the risk assessment in 2007 and monthly for control exceptions. Where control failures have been reported, details of the circumstances are required together with appropriate corrective actions. A summary of these reports is reviewed by the Executive Team and Franchise Board on a regular basis.

Internal auditors also perform independent reviews of control activities as part of their annual programme as approved by the Audit Committee. The Head of Internal Audit and Compliance reports to the Executive Team on a regular basis and to each Audit Committee meeting.

A compliance plan is in place to manage the risk associated with non-compliance with FSA regulatory processes. The Head of Internal Audit and Compliance provides progress reports to the Risk Committee and the Audit Committee. The Risk Committee also oversees the wider coordination of overseas regulatory compliance.

INFORMATION AND FINANCIAL REPORTING SYSTEMS

An annual budget for the Society is reviewed in detail by the executive and is considered and approved by the Franchise Board and Council. Monthly financial reports compare actual performance with the annual budget and management action is taken, where appropriate, when variances arise. Revised forecasts are prepared regularly.

REPORT OF THE NOMINATIONS, APPOINTMENTS AND COMPENSATION COMMITTEE

This report is based upon best practice as set out in the Combined Code. This code is directed at companies listed on the London Stock Exchange, whereas Lloyd's is a market of many separate and competing trading entities; nonetheless, Council supports its principles in so far as they can be applied to the governance of the Society.

COMPOSITION OF THE NACC

The Nominations, Appointments and Compensation Committee (NACC) currently comprises 3 nominated, 2 external and 3 working members of the Council. The NACC members for 2007 are indicated within the remuneration table on page 98.

The Committee met four times during the year. The attendance at meetings by members of the Committee is set out in the Corporate Governance report, page 90. The Committee's terms of reference are available on request from the Secretary to the Council.

NOMINATIONS AND APPOINTMENTS

The NACC is responsible for making recommendations to Council on the appointment of the Chairman, Chief Executive Officer (CEO), nominated Council members, Franchise Board members and members of a number of Council committees and the Capacity Transfer Panel (the latter is a committee of the Franchise Board). It also makes recommendations to the Franchise Board in respect of the membership of the Market Supervision and Review Committee and the Investment Committee.

Apart from the annual exercise of making recommendations with respect to the composition of Council and Franchise Board committees, the NACC made the following recommendations to Council during 2007:

- To appoint Reg Hinkley as a new nominated member of Council to replace Judith Hanratty following her retirement from Council.
- To reappoint Jim Stretton and Stephen Hodge as independent non-executive directors on the Franchise Board. Jim Stretton will serve a two year term and Stephen Hodge will serve until 2 April 2008. Both terms will commence on 1 January 2008.
- To appoint two independent non-executive directors to the Franchise Board. Claire Ighodaro will serve a three year term from the beginning of 2008 and Dipesh Shah will join the Franchise Board for a three year term following Stephen Hodge's retirement in April 2008.
- To appoint Andrew Kendrick as a market connected non-executive director on the Franchise Board for a three year term as from 5 February 2007.
- To reappoint Rolf Tolle for two years following his normal retirement date at the end of 2007.

These recommendations were accepted by Council.

To assist it with its work in this area, the NACC employs external search consultants from time to time as well as making use of its own resources and expertise.

REMUNERATION AND COMPENSATION

The Council of Lloyd's is assisted in determining the remuneration of members of the Council, Franchise Board and their committees by the NACC. The NACC also recommends for approval by the Council, the fees, salaries, bonuses and the terms and conditions of office of the Chairman, the CEO, the Director, Finance, Risk Management and Operations and the Franchise Performance Director.

In determining their recommendations for the year, the NACC consulted with the Chairman and the CEO as well as engaging the assistance of remuneration advisers, Deloitte & Touche LLP. During the year, Deloitte & Touche LLP also provided other services to the Corporation including overseas professional advice.

REMUNERATION OF COUNCIL AND FRANCHISE BOARD MEMBERS WHO ARE EMPLOYEES OF THE CORPORATION

Lloyd's remuneration policy for all current and future employees is set out in the Employee Handbook as follows:

'Lloyd's remuneration policy is designed to meet individual and business needs by providing rewards that are linked to individual performance and the delivery of business objectives.

Our total remuneration approach is supported by the following practices:

- We look beyond base salary to the value of the total reward package in meeting the needs of employees.
- We recognise and reward superior performance.

Lloyd's policy is therefore based on providing a package of rewards (salary plus benefits) that is business driven, competitive, fair and flexible. It is founded on the proposition that the ultimate source of value is people. Putting this together means a policy which:

- Emanates from business strategies and priorities.
- Is based on business success (ability to pay).
- Provides a flexible mix of rewards which will attract, retain and motivate the high calibre people we need with the varied range of experience and skills the business requires.
- Is externally competitive and regularly monitored by means of remuneration surveys.
- Rewards for performance not the cost of living.

- Ensures employees understand the criteria by which rewards are determined and reviewed.
- Gives managers as much freedom as possible in deciding the rewards of their teams.
- Is in line with our equal opportunities and diversity policy.

REMUNERATION

The current remuneration package of Council and Franchise Board members who are employees of the Corporation comprises both performance and non-performance related components. The performance related components comprise annual bonuses as well as a long-term incentive plan, while the non-performance related components comprise base salaries, benefits and pension entitlements.

The annual salary of the Chairman, CEO, Director, Finance, Risk Management and Operations and the Franchise Performance Director is reviewed by the NACC annually with increases taking effect from 1 April. No director plays a part in any discussion about his or her own remuneration.

The Chairman is entitled to receive private medical and life insurance. The CEO, Director, Finance, Risk Management and Operations and the Franchise Performance Director are entitled to receive certain benefits including a car or car allowance, private medical and life insurance in addition to their base salary.

It is NACC policy that a significant proportion of executive remuneration should be at risk and determined by performance reviews.

LONG-TERM INCENTIVE PLAN

As part of its continuous assessment of the remuneration package the NACC has reviewed the current long-term incentive plan and concluded that it is appropriate to introduce a new Lloyd's Performance Plan (LPP) available to all employees, which has been designed to meet strategic objectives by enabling the Corporation to offer an incentive which:

- Is directly linked to the profitability of the Lloyd's market and will therefore encourage an attitude of commercial partnership with the market and align the interests of participants with capital providers.
- Will provide a competitive reward and therefore assist Lloyd's in attracting and retaining the talented individuals required to develop and support future strategy.

The first year of operation of the LPP will be the financial year commencing on 1 January 2008.

The plan is operated at the discretion of the NACC and can be amended or terminated at any time.

LONG-TERM INCENTIVE PLAN APPLICABLE FOR THE YEAR ENDED 31 DECEMBER 2007 (THE '2004 LTIP')

The 2004 LTIP for the CEO and other senior executives of the Corporation was established with the approval of the NACC and Council in March 2004. This replaced the previous LTIP with effect from 1 January 2004, although transitional measures applied for 2004 only. The last vested awards under the previous LTIP fell due and were paid in October 2007.

OPERATION OF THE 2004 LTIP

THREE-YEAR POOLING PRINCIPLE

Payments made under the 2004 LTIP are based on the aggregate profitability of the Lloyd's market over three years, taking into account both profits and losses over that three-year period. The principle of pooling means that any losses made over the three-year period will offset profits when determining payments, thus encouraging prudential behaviour. Pooling also means that awards may be made in loss making years. This would be the case if the aggregate profits outweighed the aggregate losses over the relevant three-year period.

The three-year profits pool are calculated each year on a rolling basis.

PROFIT/LOSS

Profit or loss is defined as the pro forma profit or loss on ordinary activities before tax as reported in the Lloyd's Annual Report, excluding notional investment returns on funds at Lloyd's.

ELIGIBILITY

Selected senior permanent employees of the Corporation are eligible for the scheme including the CEO, directors and existing staff in role level one as at 1 January each year. The NACC retains absolute and sole discretion as to who participates in the LTIP in any particular year.

LIMITS

There is an overall limit such that the total LTIP awards for all participants in any year will not exceed 0.075% of the aggregate profits and losses for the relevant three-year period.

JOINING EMPLOYMENT

Subject to NACC's discretion, executives who are newly recruited or promoted may be made an LTIP award on a pro-rated basis. When this occurs, awards will normally be pro-rated in relation to the number of full months of employment during the 36-month period to which the three-year pool relates.

REPORT OF THE NOMINATIONS, APPOINTMENTS AND COMPENSATION COMMITTEE CONTINUED

LEAVING EMPLOYMENT

The NACC retains absolute discretion over the treatment of any and all LTIP awards (or any part thereof) on the termination of employment for any reason whatsoever of the CEO, Director, Finance, Risk Management and Operations and the Franchise Performance Director. Unless the NACC resolves otherwise, the CEO retains absolute discretion over the treatment of any and all LTIP awards (or any part thereof) on the termination of employment of all other participants. If a participant leaves employment due to retirement, redundancy, death, disability or ill-health prior to the end of the deferred payment period, he or she will normally receive any outstanding instalments of previous awards, which will usually be paid on the normal payment dates. Any awards partially earned in the year of departure may be paid on a pro-rated basis.

If a participant leaves employment for any other reason, any outstanding instalments due in respect of previous financial years and any LTIP award due in respect of the financial year during which employment is terminated will normally both be forfeited immediately. The NACC or the CEO, in respect of participants other than the CEO himself, the Director, Finance, Risk Management and Operations and the Franchise Performance Director, have discretion to make payments if they consider it appropriate.

CALCULATION OF AWARD AND TIMING OF PAYMENTS

The value of the LTIP award is calculated as a percentage of the aggregate profits for the relevant three-year period for each £1m of aggregate LTIP participants' salaries. For the CEO and for each director, this percentage is 0.008%. For other participants, the percentage used is lower, 0.004%. The percentages have been set by reference to external market data on remuneration levels as measured against other organisations of similar complexity and size.

For the financial year 2007, the award made under the 2004 LTIP, subject to adjustment for discretionary awards, is the aggregate profits of the Lloyd's market for the financial years 2005–2007 of £5,499m x relevant % x salary of LTIP participant per £1m.

The payment of each award is made in three tranches, subject to continued employment with the Corporation, in April of each of the three years following the end of the LTIP year. For participants other than the CEO, the Director, Finance, Risk Management and Operations, and the Franchise Performance Director, the first tranche of each award is discretionary and that award may be increased or decreased by a maximum of 100%, to reflect the individual's performance over the year. However, in no circumstances can an adjustment be made to increase the total value of discretionary awards. The further two payments (of equal amounts) will be paid in the following two years, subject to the individual remaining in employment with the Corporation. With the introduction of the LPP from 1 January 2008, transitional rules will apply for outstanding payments due under the LTIP as at 1 January 2009.

Details of the awards to the CEO, the Director, Finance, Risk Management and Operations and the Franchise Performance Director are shown on page 100.

LLOYD'S PERFORMANCE PLAN (THE LPP) APPLICABLE FOR THE YEAR ENDING 31 DECEMBER 2008

ELIGIBILITY

All employees of the Corporation and overseas offices are eligible to participate in the LPP on the basis set out below.

New employees will become eligible to participate in the LPP from the first full financial year following their recruitment.

CALCULATION OF LPP AWARDS

Awards under the LPP ('LPP Awards') are calculated by reference to profit on ordinary activities before tax ('PBT'), as reported in the pro forma financial statements in the Lloyd's Annual Report for each financial year. LLP Awards will only be triggered if PBT in excess of £100m is achieved.

The LPP Awards for each financial year will be calculated as a percentage of the participants' salaries at 31 December in that year, for each £1bn of PBT.

The LLP Awards are as follows:

Job level	Amount of LPP Award	Limits on LPP Awards ('trigger')	Limits on LPP Awards ('cap')
CEO and directors	20% salary per £1bn of PBT	LPP Awards will be triggered only on the achievement of a minimum threshold of £100m PBT. If PBT is below £100m, no LPP Awards will be made for that financial year.	100% of salary i.e. £5bn of PBT
Senior managers (Level 1)	10% salary per £1bn of PBT		30% of salary i.e. £3bn of PBT
Other employees (Level 2–4)	5%–3% salary per £1bn of PBT depending on grade		15% – 9% of salary (depending on grade) i.e. £3bn of PBT

STRUCTURE AND TIMING OF PAYMENTS

Subject to the transitional arrangements set out below, for directors and Level 1 employees the LPP will operate as an ongoing fund, rather than as a series of annual awards. For these employees, the LPP Award for each financial year will be added to the particular employee's notional LPP fund (the 'LPP Fund') and paid out in future years as described in the table below:

Job level	Awards	Payments
CEO and directors Level 1 employees	Any LPP Award will be notified to the employee after the PBT for the relevant year has been announced (e.g. the employee will be notified in May 2009 of any LPP Award relating to the financial year 2008). The total amount of the LPP Award will be added to the particular employee's LPP Fund.	Each October one half of the total contents of the LPP Fund will be paid to the employee

Subject to the transitional arrangements set out below, for Level 2–4 employees, any LPP Award will be paid in full during the year in which it is notified to the employee. For example, for the financial year 2009, employees will be notified of any LPP Award normally in May 2010 (once PBT for 2009 has been announced) and the LPP Award for 2009 will be paid to these employees in full in October 2010.

LEAVING EMPLOYMENT

The NACC will retain absolute discretion over the payment of any and all LPP Awards to participants whose employment is terminated (regardless of the reason for termination).

Directors and Level 1 participants

(a) If a director or Level 1 participant leaves the Corporation's employment due to retirement, redundancy, death, disability or ill-health (each as determined by the NACC acting in its absolute discretion) the provisions set out in paragraph (b) to (d) below will apply.

(b) The director or Level 1 participant will receive a pro rated LPP Award for each complete month of service in respect of his/her year of departure. The LPP Award will be notified to the employee and paid in accordance with the usual timescales.

(c) Any balance which remains in the LPP Fund for directors or Level 1 participants will be paid in full in the October at the same time as the final LPP Award which is due to the employee.

(d) If a director or Level 1 participant leaves the Corporation's employment due to any reason other than those listed in paragraph (a) above (as determined by the NACC acting in its absolute discretion), he/she will forfeit any and all outstanding and future LPP Awards (including, for the avoidance of any doubt, any balance of the LPP Fund) with immediate effect from the date that he/she serves or receives notice of termination.

Level 2–4 participants

(a) If a Level 2–4 participant serves or receives notice of termination (regardless of the reason of termination), he/she will forfeit any and all outstanding and future LPP Awards with immediate effect from the date of such notice.

TRANSITIONAL ARRANGEMENTS

Directors and Level 1 employees

(a) Directors and Level 1 employees who were employed by the Corporation prior to 1 January 2008 and who participated in the 2004 LTIP will be subject to the transitional arrangements set out below.

(b) For the financial years 2008, 2009 and 2010, the Corporation will assess the awards potentially payable to these directors and Level 1 employees under both the 2004 LTIP and the LPP. These directors and Level 1 employees will receive the higher of the two potential awards with respect to each financial year. If, for example, the award under the LPP would be higher than the award under the 2004 LTIP, the LPP Award shall apply, and the 2004 LTIP Award shall not be made. If the award under the 2004 LTIP would be higher, the 2004 LTIP Award will be paid and the LPP Award shall not be made.

(c) With effect from 1 January 2011, all awards to the directors and Level 1 employees will be calculated in accordance with the LPP, and these employees shall have no further entitlements under the 2004 LTIP.

(d) With respect to the timing of any payments pursuant to these transitional arrangements, the following shall apply:

(i) For 2008, all payments will continue to be made under the rules of the 2004 LTIP.

(ii) From 1 January 2009 all payments will be under the Rules of the LPP (regardless of whether the director or Level 1 employee has received awards under the 2004 LTIP or the LPP). For example, if a director or Level 1 employee receives an award under the 2004 LTIP for the financial year 2008 (on the basis that the potential award for this individual under the 2004 LTIP is greater than the potential award under the LPP), the amount of this award will be added to the individual's LPP Fund. Directors and Level 1 employees will receive half of the value of the LPP Fund in October 2009.

REPORT OF THE NOMINATIONS, APPOINTMENTS AND COMPENSATION COMMITTEE CONTINUED

Level 2–4 employees

(a) For all Level 2–4 employees who are eligible to participate in the LPP for the financial year 2008 (i.e. all employees who were employed by the Corporation as at 2 January 2008), the provisions set out below shall apply.

(b) For the financial year 2008 only, any LPP Award for Level 2–4 employees described above shall be based on the adjusted interim PBT for the six months to 30 June 2008 (as determined in October 2008), and paid to these employees in December 2008. A further LPP award determined by the actual PBT for 2008 will be payable in October 2009.

(c) For the financial year 2009 and beyond, the provisions set out in the paragraph Structure and Timing of Payments shall apply to all Level 2–4 employees.

PENSION ARRANGEMENTS

The CEO, Director, Finance, Risk Management and Operations and the Franchise Performance Director are members of the Lloyd's Pension Scheme. Their dependants are eligible for dependants' pensions and the payment of a lump sum in the event of death in service. The pension arrangements for the Director, Finance, Risk Management and Operations and the Franchise Performance Director provide for a pension at normal retirement of two-thirds base annual salary after 20 years' eligible service less any entitlement from previous pension arrangements and subject to a Scheme earnings cap of £112,800 from 6 April 2007. The pension arrangements for the CEO provide for a pension on retirement based on a standard accrual rate of one sixtieth of base annual salary subject to the Scheme earnings cap, for each year of eligible service, with the facility to increase the accrual rate to one thirtieth for an additional contribution via salary sacrifice. No other payments to the CEO, the Director, Finance, Risk Management and Operations and the Franchise Performance Director are pensionable.

Pensions legislation changed from 'A day' on 6 April 2006 with the introduction of Life Time Allowance requirements. Due to these changes the Lloyd's Pension Scheme rules have been changed to restrict the earnings that can be counted towards the calculation of benefits to a maximum earnings cap, which from 6 April 2007 was £112,800 for those who joined the Scheme on or after 1 June 1989. This will increase each tax year in line with inflation.

In 2007 the CEO, Director, Finance, Risk Management and Operations and the Franchise Performance Director were each entitled to a cash allowance of 20% of their base salary. Due to the tax changes affecting Funded Unapproved Retirement Benefit Schemes (FURBS) from 6 April 2006, the 20% of annual base salary that Lloyd's had paid into the FURBS accounts of the executive directors was paid as a cash allowance. It is anticipated that cash allowances will continue to be paid in the future.

A cash allowance of £44,700 was payable in respect of the Chairman for 2007. Due to the Life Time Allowance rules introduced from 'A day' it is no longer possible for Lloyd's to make payments to the Chairman's personal pension. From 6 April 2006, this payment which equates to 40% of the maximum earnings cap has been paid as a cash allowance.

The Lloyd's Pension Scheme introduced member contributions with effect from 1 July 2006 and from this date the Director, Finance, Risk Management and Operations and the Franchise Performance Director paid 10% of the earnings cap as a contribution via salary sacrifice and the CEO paid 5% of the earnings cap as a contribution for a sixtieth accrual rate and an extra 24.1% increasing to 26.1% with effect from 1 July 2007 of the earnings cap to increase the accrual rate to thirtieths, both paid via salary sacrifice.

CONTRACTS OF EMPLOYMENT

The Chairman has a three-year contract and is subject to a 12 months' notice of termination by either party, expiring in November 2008. As outlined in the Corporate Governance section on page 87, HM Treasury is promoting changes to Lloyd's Act 1982 by means of a Legislative Reform Order (LRO). If successfully implemented this will update aspects of Lloyd's governance structure and would enable the Chairman to stand again for election to Council when his current term expires. On the assumption that the LRO is implemented, the NACC recommended to Council that Lord Levene should continue as Chairman on a rolling one year contract. This is subject to both Lord Levene being successfully re-elected and the Council formally resolving each year to re-elect Lord Levene as Chairman. Council agreed the NACC's recommendation.

The CEO, Director, Finance, Risk Management and Operations and Franchise Performance Director have rolling one-year contracts providing for a maximum of one year's notice.

Details of these contracts are summarised in the table below.

MEMBERS OF THE COUNCIL AND FRANCHISE BOARD WHO ARE EMPLOYEES OF THE CORPORATION

	Contract date	Unexpired term as at 31 Dec 2007	Notice Period(i)
Lord Levene of Portsoken	01/11/02	10 months	12 months
Richard Ward(ii)	24/04/06	rolling 1 year	12 months
Luke Savage(iii)	20/09/04	rolling 1 year	12 months
Rolf Tolle(iv)	03/03/03	rolling 1 year	12 months

(i) Employment contracts do not contain provisions for compensation payable upon early termination.

(ii) Richard Ward was appointed to the Franchise Board and Council on 24 April 2006.

(iii) Luke Savage was appointed to the Franchise Board on 30 September 2004.

(iv) Rolf Tolle was appointed to the Franchise Board on 3 March 2003.

REMUNERATION AND CONTRACTS OF SERVICE FOR MEMBERS OF THE COUNCIL OF LLOYD'S AND FRANCHISE BOARD WHO ARE NOT EMPLOYEES OF THE CORPORATION

Remuneration for all members of Council and Franchise Board who are not employees of the Corporation is designed to attract people of sufficient calibre and experience to govern Lloyd's affairs by providing an appropriate level of fees which reflects the demands made upon them. Reference is also made to independent surveys of fees paid to non-executive directors of similar organisations.

In 2007, fees for members of Council and Franchise Board were £28,000 and £45,000 per annum, respectively. The Deputy Chairmen are paid £38,000 per annum. Fees are also payable in respect of membership of a number of Council and Franchise Board committees, including a number of ad hoc committees established to consider specific issues requiring a significant time commitment. Non-employee members of the Council and Franchise Board are not eligible to join the Lloyd's Pension Scheme.

Individual remuneration of all members of the Council and Franchise Board can be found in the table overleaf.

External and working members are elected to Council while nominated members are appointed to Council, usually for a three-year period. Members of the Franchise Board are appointed by Council with non-executive directors' terms of office varying between one and three years. These are not contractual arrangements and compensation is not paid if a member leaves early.

INFORMATION SUBJECT TO AUDIT

BASIS OF PREPARATION

The following section provides details of the remuneration of all members of the Council of Lloyd's and the Franchise Board for the year ended 31 December 2007. This section contains the following information in the form specified in Schedule 7A Part 3 of the Companies Act 1985:

- → Amount of each member's emoluments and compensation in the current and previous financial year.
- → Details of each member's accrued benefits in the Lloyd's Pension Scheme and transfer values of those accrued benefits.
- → Details of each member's interests under the Long-Term Incentive Plan.

REPORT OF THE NOMINATIONS, APPOINTMENTS AND COMPENSATION COMMITTEE CONTINUED

REMUNERATION OF MEMBERS OF THE COUNCIL OF LLOYD'S AND THE FRANCHISE BOARD

Individual remuneration, excluding LTIP Awards, for the year to 31 December is shown in the table below. LTIP Awards are shown on page 100.

	Salary/Fees		Taxable benefits[i]		Annual bonus		Other[ii]		Total	
	2007 £000	2006 £000	2007 £000	2006 £000	2007 £000	2006 £000	2007 £000	2006 £000	2007 £000	2006 £000
Chairman of Council of Lloyd's										
Lord Levene of Portsoken[iii][iv]	460	450	–	7	150	150	72	58	682	665
Executive Directors										
Richard Ward[iii][iv][xi]	460	307	12	8	464	300	97	88	1,033	703
Luke Savage[iii][v]	394	369	12	10	200	265	82	77	688	721
Rolf Tolle[iii][v][xxv]	522	492	21	27	520	500	128	121	1,191	1,140
Non-Executive Council Members										
Working members										
Rupert Atkin[vi][vii][viii]	32	–	–	–	–	–	–	–	32	–
Ewen Gilmour, Deputy Chairman[vi]	52	43	–	–	–	–	–	–	52	43
Nigel Hanbury[vi][vii]	34	28	–	–	–	–	–	–	34	28
Christopher Harman[viii]	26	–	–	–	–	–	–	–	26	–
Graham White, Deputy Chairman[xxvi]	37	26	–	–	–	–	–	–	37	26
External members										
Alan Lovell[viii]	33	–	–	–	–	–	–	–	33	–
Barbara Merry[viii][xii]	26	–	–	–	–	–	–	–	26	–
Peter Morgan[vi][xiii]	35	36	1	1	–	–	–	–	36	37
Dermot O'Dononhoe[viii][xiv]	26	–	–	–	–	–	–	–	26	–
David Shipley[xvi]	35	38	–	–	–	–	–	–	35	38
Anthony Townsend[vi][vii][viii][xvii]	34	26	–	–	–	–	–	–	34	26
Nominated members										
Celia Denton	44	44	–	–	–	–	–	–	44	44
Reg Hinkley[x]	7	–	–	–	–	–	–	–	7	–
Bill Knight, Deputy Chairman of the Council of Lloyd's[vi]	62	65	–	–	–	–	–	–	62	65
Philip Lader[vi][vii][xv]	34	39	8	2	–	–	–	–	42	41
Andreas Prindl	52	57	–	–	–	–	–	–	52	57
Non-Executive Franchise Board Members										
Roy Brown	45	45	–	–	–	–	–	–	45	45
Steven Burns[xxii]	45	48	–	–	–	–	–	–	45	48
Edward Creasy	45	45	–	–	–	–	–	–	45	45
Stephen Hodge	56	59	–	–	–	–	–	–	56	59
Andrew Kendrick[xxiv]	41	–	–	–	–	–	–	–	41	–
Jim Stretton	52	54	6	5	–	–	–	–	58	59
Former Members of Council										
John Coldman	–	4	–	–	–	–	–	–	–	4
Tom Corfield[viii][xviii]	2	14	–	–	–	–	–	–	2	14
Sean Dalton[xviii]	–	20	–	–	–	–	–	–	–	20
Christine Dandridge[vii][viii]	3	43	–	–	–	–	–	–	3	43
Quentin Davies[viii][xix]	2	39	–	–	–	–	–	–	2	39
Judith Hanratty[vii][ix]	28	51	–	–	–	–	–	–	28	51
Bronek Masojada[vii][viii]	4	46	–	–	–	–	–	–	4	46
Charles Philipps[vii][viii][xx]	3	36	–	–	–	–	–	–	3	36
Preben Prebensen[xxi]	–	2	–	–	–	–	–	–	–	2
Former Members of the Franchise Board										
Stephen Catlin[xxiii]	–	45	–	–	–	–	–	–	–	45

(i) Taxable benefits include items such as company car or car allowance, medical and life insurance.

(ii) Up to 5 April 2006, other includes payments into a Funded Unapproved Retirement Benefit Scheme (FURBS) of 20% of executive directors' total salary. The amount stated in respect of the Chairman represents pension contributions to a personal pension scheme. From 6 April, 2006 following the introduction of new Life Time Allowance requirements, these payments were made as cash allowances.

(iii) Employee of the Corporation of Lloyd's.

(iv) Member of both Council and the Franchise Board for 2007.

(v) Member of the Franchise Board only.

(vi) Member of the Nominations, Appointments & Compensations Committee (NACC) for 2007.

(vii) Christine Dandridge, Bronek Masojada and Charles Philipps were members of the NACC until 31 January 2007. Rupert Atkin, Nigel Hanbury, Anthony Townsend and Philip Lader joined NACC in February 2007. Judith Hanratty retired from NACC on 4 August 2007, when her term of office on Council expired.

(viii) Rupert Atkin, Christopher Harman, Alan Lovell, Barbara Merry (representative of Hardy Underwriting Limited) and Dermot O'Donohoe (representative of Dornoch Limited) were elected as members of Council as from 1 February 2007. Anthony Townsend (representative of Brit Underwriting Limited) was re-elected at the same time. Tom Corfield (representative of Liberty Corporate Capital Limited), Christine Dandridge, Quentin Davies (representative of SUMAC Underwriting (UK) Limited), Bronek Masojada and Charles Philipps (representative of Amlin Corporate Member Limited) retired from Council as of 31 January 2007.

(ix) Judith Hanratty retired as a Nominated member of Council on 4 August 2007.

(x) Reg Hinkley joined as a Nominated member of Council on 29 October 2007.

(xi) Richard Ward joined the Corporation of Lloyd's on 24 April 2006 and was appointed to the Franchise Board and Council on the same date.

(xii) Representative of Hardy Underwriting Limited.

(xiii) Representative of AJSLP 9 Limited.

(xiv) Representative of Dornoch Limited.

(xv) Philip Lader was reappointed as a Nominated member of Council for a three year term on 3 March 2007.

(xvi) Representative of MAP Underwriting Limited.

(xvii) Representative of Brit UW Limited.

(xviii) Sean Dalton resigned as the representative of Liberty Corporate Capital Limited in July 2006. Tom Corfield took his place in August 2006.

(xix) Representative of of SUMAC Underwriting (UK) Limited.

(xx) Representative of Amlin Corporate Member Limited.

(xxi) Preben Prebensen was the representative of Wellington (Five) Limited until 31 January 2006.

(xxii) Steven Burns was the representative of Limit (No. 2) Limited on Council until its term of office came to an end on 31 January 2006. He was a member of the Franchise Board for 2006 and 2007.

(xxiii) Stephen Catlin's term of office on the Franchise Board came to an end on 31 December 2007.

(xxiv) Andrew Kendrick was appointed to the Franchise Board on 5 February 2007.

(xxv) Rolf Tolle occupies a property leased to Lloyd's. Rolf Tolle pays the lease rental of £36,000 (2006: £48,000) on the property by salary sacrifice. These amounts are not included in the table above.

(xxvi) Graham White became a Deputy Chairman in February 2007.

REPORT OF THE NOMINATIONS, APPOINTMENTS AND COMPENSATION COMMITTEE CONTINUED

LLOYD'S PENSION SCHEME PROVISIONS

	Salary sacrifice in year to 31 Dec 2007[i] £000	Age at 31 Dec 2007	Increase in pension in year to 31 Dec 2007 – actual £000	Increase in pension in year to 31 Dec 2007 – net of price inflation £000	Total accrued annual pension in year to 31 Dec 2007 £000 pa	Normal Retirement age
Richard Ward	34	50	4	4	6	65
Luke Savage	11	46	3	3	9	60
Rolf Tolle	11	60	4	4	18	60

(i) The Lloyd's Pension Scheme was made a contributory pension scheme with effect from 1 July 2006. The contributions due from the CEO, Director, Finance, Risk Management and Operations and the Franchise Performance Director are collected by salary sacrifice.

TRANSFER VALUES OF ACCRUED PENSION BENEFITS

	Transfer value of accrued pension as at 31 Dec 2006 £000	Transfer value of accrued pension as at 31 Dec 2007 £000	Increase in transfer value over the year less director's contributions via salary sacrifice £000
Richard Ward	22	65	9
Luke Savage	73	113	29
Rolf Tolle	254	354	89

The transfer value represents a liability of the Lloyd's Pension Scheme, not a sum paid or due to the individual.

MEMBERS OF THE COUNCIL OF LLOYD'S AND FRANCHISE BOARD'S SHARE OF THE LONG TERM INCENTIVE PLAN

			Estimated long-term bonus						
	Award year	Performance bonus £000	As at 31 Dec 2006 £000	Change in year £000	As at 31 Dec 2007 £000	Total £000	Amount paid in prior years £000	Amount paid during the year ended 31 Dec 2007 £000	Total award outstanding as at 31 Dec 2007 £000
Richard Ward	2006	8	17	–	17	25	–	8	17
	2007	–	–	113	113	113	–	–	113
Luke Savage	2004	6	13	–	13	19	12	7	–
	2005	15	30	–	30	45	15	15	15
	2006	32	63	–	63	95	–	32	63
	2007	–	–	176	176	176	–	–	176
Rolf Tolle	2004	89	281	–	281	370	214	156	–
	2005	21	41	–	41	62	21	21	20
	2006	46	92	–	92	138	–	46	92
	2007	–	–	247	247	247	–	–	247

Bill Knight, Chairman
Nominations, Appointments and Compensation Committee

REPORT OF THE AUDIT COMMITTEE

This report sets out the role, remit and activities of the Audit Committee during 2007.

COMPOSITION OF THE AUDIT COMMITTEE

In 2007 the Audit Committee comprised three nominated members of Council, one working and one external member of the Council and two non-executive members of the Franchise Board. The Committee met five times during the year. The members of the Committee in 2007 and their attendance at meetings are shown in the Corporate Governance report on page 87.

All of the Committee have extensive commercial experience. For the purposes of the Combined Code, Celia Denton, Ewen Gilmour and Stephen Hodge, the Chairman of the Committee, are considered by the Council to have recent and relevant financial experience.

TERMS OF REFERENCE

The Council has delegated to the Committee responsibility for overseeing the financial reporting and internal controls of the Society and its subsidiaries and the Central Fund. The Committee follows an agreed annual work plan. The principal responsibilities of the Committee include:

- Ensuring that the financial activities of Lloyd's are subject to independent review and audit. The Committee reviews Lloyd's published annual and interim financial statements including the pro forma financial statements, the Aggregate Accounts, the group financial statements of the Society of Lloyd's and Lloyd's Return to the FSA.
- Reviewing and monitoring the arrangements for ensuring the objectivity and effectiveness of the external and internal audit functions;
- Considering, on behalf of the Council, the appointment or removal of the external auditors.
- Reviewing and monitoring the effectiveness of the systems of internal control of the Society.
- Ensuring that appropriate arrangements are in place for ensuring compliance by the Society with relevant laws and regulations.
- Ensuring appropriate whistle-blowing arrangements are in place by which members of staff can, in confidence, raise concerns relating to possible improprieties.

The Committee's terms of reference are available on request from the Secretary to the Council.

REPORT ON THE COMMITTEE'S ACTIVITIES IN 2007

The principal issues addressed during 2007 were:

- The annual financial statements for 2006 including pro forma financial statements and Aggregate Accounts, the financial statements of the Society and financial disclosures and various accounting matters raised by management and auditors.
- The interim financial statements for the six months to 30 June 2007 including the pro forma financial statements and the financial statements of the Society of Lloyd's.
- Considering those accounting policies which involved significant estimates and assumptions.
- The 2006 Lloyd's Return to the FSA.
- The external auditors' status reports and management letters.
- The independence and objectivity of the external auditors, including a review of non-audit fees.
- The external and internal audit plans.
- The reports of the Head of Internal Audit and Compliance, including follow-up of internal audit findings and the annual compliance plan.
- Reports from the Risk Committee, including the development of the Syndicate Risk Matrix and the Lloyd's Risk Management Framework.
- Assessment of the effectiveness of internal controls.

Following a request from the Committee, management undertook a survey of all staff in the 4th quarter of 2006 to increase awareness of the whistle-blowing policy and procedures. The results of the survey and new internal procedures were considered at its February 2007 meeting. The survey assessed the extent to which the policy was understood by employees and concluded that generally employees were aware of the policy and that matters of concern should be raised.

REPORT OF THE AUDIT COMMITTEE CONTINUED

The Committee also carried out an effectiveness review of internal and external auditors. With respect to the external audit it was agreed that this should not be re-tendered in 2007 as the Committee were satisfied with the external auditor's performance.

The Committee held a workshop training session during 2007 facilitated by partners from PricewaterhouseCoopers where, amongst other topics, it considered the Transparency Directive, narrative reporting and IFRS Phase II. The Committee also reviewed its own performance.

SUPPORT

The CEO, Director, Finance, Risk Management and Operations, General Counsel, Head of Internal Audit and Compliance, Financial Controller, Head of Market Reporting and the external and internal auditors attended meetings as appropriate. During the year, the Committee met separately with the external and internal auditors without executive management present.

The Committee has access to external independent advice, if required.

Stephen Hodge, Chairman
Audit Committee

REPORT OF THE LLOYD'S MEMBERS' OMBUDSMAN

REPORT BY SIR ROBIN MOUNTFIELD, LLOYD'S MEMBERS' OMBUDSMAN

I am pleased to present the Annual Report of the Lloyd's Members' Ombudsman to the Council of Lloyd's for the year ending 31 December 2007. I succeeded Sir Brian Hayes as Ombudsman on 1 April, and this report covers the final three months of his term as well as the first nine months of mine.

The role of the Lloyd's Members' Ombudsman is to investigate complaints by members and former members who were members at any time after 30 November 2001, who believe that they have suffered injustice in consequence of maladministration in relation to any action taken by or on behalf of the Society.

COMPLAINTS RECEIVED

During the year six complaints were received, but none justified a finding of maladministration.

Four cases fell outside my jurisdiction as Ombudsman.

In one case I recommended, after conducting the necessary investigations, that action should be taken as a result of the complaint to change certain arrangements relating to the administration of shareholdings held as part of Funds at Lloyd's.

I also considered a matter previously considered by Sir Brian Hayes who had first considered and rejected the complaint in 2005, but found no ground to change his conclusion.

COSTS

The expenses incurred by my office amounted to £21,475.

REPORT OF THE CHAIRMAN OF THE MEMBERS' COMPENSATION PANEL

BILL KNIGHT, CHAIRMAN OF THE MEMBERS' COMPENSATION PANEL

An application was made for compensation in the order of £20m under the Members' Compensation Scheme Byelaw. The application relates to Cotesworth & Co Limited and to syndicates 535 and 536. The Council appointed a Members' Compensation Panel, comprising nominated members of Council, to consider and administer the application. The Panel has required the applicants to pursue proceedings in the High Court before proceeding with the application, which has been adjourned pending the outcome of the proceedings. Payment of any compensation under the Scheme is met by contributions or reimbursement from underwriting agents and members in accordance with the terms of the Byelaw.

During 2007, the Panel reviewed the current Scheme and issued a consultation document on 22 August 2007 which sought market feedback on a number of proposals to amend the Scheme. The Panel will make its final recommendations to Council during 2008.

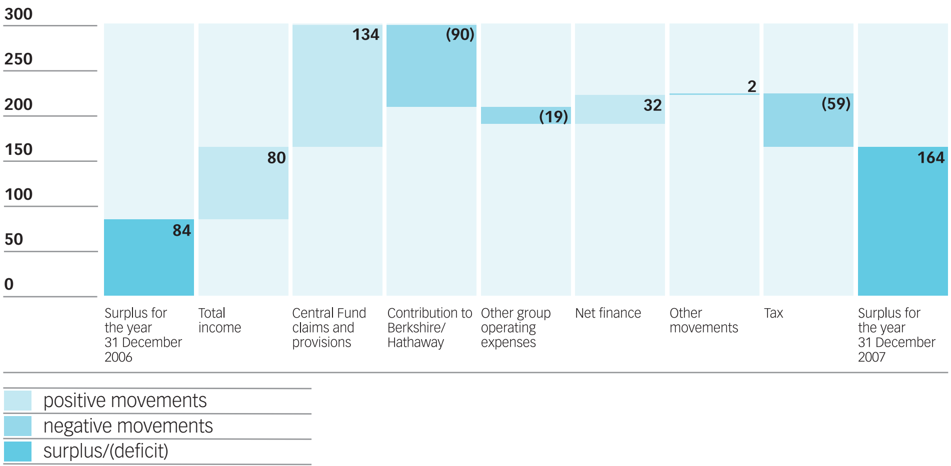
FINANCIAL REVIEW

This review should be read in conjunction with the financial statements of the Society on pages 114 to 150.

OVERALL FINANCIAL RESULT

The surplus for the year after taxation is £164.4m (2006: surplus of £83.6m). This increase is due to higher members' contributions and subscriptions, reflecting higher capacity in the year, an improvement to Central Fund recoveries, including litigation settlement receipts, and a release of provisions established to meet unpaid cash calls of insolvent members. This has been offset by the contribution of £90m in respect of the Equitas-Berkshire Hathaway transaction (see page 106). The movement in the surplus for the year is shown below:

Movement in group income statement
£m



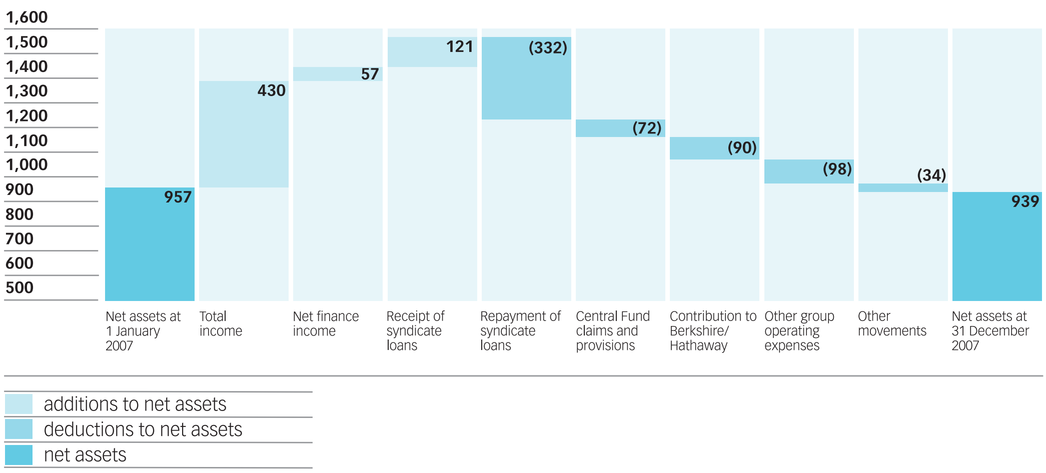
In 2007, members contributed to the Central Fund based on a percentage of their overall premium limit. However, as in 2006, this was partly achieved by contributions of 1.00% (2006: 1.00%) and partly by way of interest-bearing loans from syndicate premiums trust funds, referred to as syndicate loans, of 0.75% (2006: 0.75%). New corporate members underwriting on new syndicates are required to contribute to the New Central Fund at an increased rate for their first three years of operations at Lloyd's. The rate for 2007 was 2.00% (2006: 2.50%).

The syndicate loans were treated as part of the Society's equity rather than as contributions from members in the group income statement and would have ordinarily been repaid on the closure of the year of account after three years. Annual interest payable on the loans is accounted for when the Council formally approves the interest payments to be made. On 16 April 2007, an interest payment of £7.6m was distributed in respect of interest for the year ended 31 March 2007. On 26 July 2007, following the issue of £500m Tier 1 perpetual subordinated capital securities, the Council formally approved the early repayment of all syndicate loans and any related interest. The capital was repaid in full on 31 July 2007 (£331.6m) with interest of £5.8m relating to the period 1 April 2007 to 30 July 2007 distributed on 17 August 2007.

Members' subscriptions which are used to finance the operations of the Corporation were unchanged in 2007 at 0.50% of overall premium limits.

The Society's net assets have decreased in 2007 from £956.9m to £938.6m reflecting the repayment of the syndicate loans. Details are set out opposite.

Movement of net assets
£m



The net assets of the Central Fund are included within the above amounts and at 31 December were £767m (2006: £843m).

SOLVENCY

Total assets for solvency purposes are set out below. The 2007 position is an estimate of the amount which will be finalised in June 2008 for submission to the FSA:

	2007 £m	2006 £m
Net assets at 31 December	**939**	957
Subordinated notes and perpetual subordinated capital securities	**1,012**	497
Central assets	**1,951**	1,454
Callable Central Fund contributions	**478**	484
Other solvency adjustments	**28**	116
Central assets for solvency purposes	**2,457**	2,054
Solvency shortfalls	**(168)**	(253)
Excess of central assets over solvency shortfalls	**2,289**	1,801

Based on central assets for solvency purposes of £2.5bn (2006: £2.1bn), the estimated solvency ratio is 1,463% (2006: 812%). In setting contribution levels, account is taken of the Society's ICA to ensure that Lloyd's is prudently but competitively capitalised. The current medium-term target is that the central asset position, net of outstanding liabilities, should exceed £1.7bn.

FINANCIAL REVIEW CONTINUED

OPERATING SURPLUS

The operating surplus before tax and financing by business segment is set out below:

	Corporation of Lloyd's £000	Central Fund £000	Insurance activities £000	2007 Total £000	2006 Total £000
Total income	**178,694**	**245,662**	**5,367**	**429,723**	350,035
Central Fund claims and provisions released/(incurred)	**–**	**18,208**	**–**	**18,208**	(115,735)
Contribution to Equitas-Berkshire Hathaway transaction	**–**	**(90,000)**	**–**	**(90,000)**	–
Gross insurance claims	**–**	**–**	**16,330**	**16,330**	(55,461)
Insurance claims recoverable from reinsurers	**–**	**–**	**(17,041)**	**(17,041)**	56,804
Other group operating expenses	**(170,949)**	**(12,372)**	**(4,545)**	**(187,866)**	(170,795)
Operating surplus before tax and financing	**7,745**	**161,498**	**111**	**169,354**	64,848

INCOME

The Society's income has increased in 2007 by £79.7m to £429.7m (2006: £350.0m). New Central Fund contributions recognised within income increased from £152.2m to £168.3m, an increase of £16.1m, reflecting the increase in members' overall premium limits during the year. Members' subscriptions increased from £74.5m to £81.4m, an increase of £6.9m, and again reflect the change of premium limits in 2007. Both the Central Fund contribution and the members' subscription rates remained unchanged during 2007 at 1.00% and 0.50% respectively. In 2008, the Central Fund contribution rate has been reduced to 0.50%, thereby reducing the costs of mutuality, with the members' subscription rate remaining unchanged at 0.50%. The basis of these charges has, however, changed in 2008 from capacity to written premiums.

Other income receivable by the Central Fund in 2007 increased by £56.1m to £77.3m reflecting litigation settlements and increased recoveries from insolvent members.

CENTRAL FUND CLAIMS AND PROVISIONS

Central Fund claims and provisions decreased in 2007 by £133.9m, resulting in a release of £18.2m (2006: charge of £115.7m). This includes a reassessment of provisions as at 31 December 2007 which resulted in £43m being released. Undertakings to meet the liabilities of insolvent members to policyholders are approved at the discretion of the Council and are normally based on anticipated cash flow requirements of insolvent members in the following 12 months. During 2007, payments made in respect of insolvent corporate members reduced to £9.3m (2006: £131.1m) with additional payments made in respect of individual members of £0.3m (2006: £1.3m).

CONTRIBUTION TO EQUITAS-BERKSHIRE HATHAWAY TRANSACTION

Note 26 on page 150 provides details of the retrocession and run-off contract between Equitas Holdings Limited, Equitas Limited and National Indemnity Company (a subsidiary of Berkshire Hathaway). During 2007, a charge of £90m has been recognised being £72m towards the initial premium, paid by Lloyd's on 27 March 2007, and £18m payable by 31 December 2009. Lioncover Insurance Company Limited received a return premium of £2.4m from Equitas Holdings Limited as part of Phase 1 of the transaction. It is the intention to pass the benefit of the return premium to members on syndicates formerly managed by PCW Underwriting Agencies Limited, WMD Underwriting Agencies Limited and Richard Beckett Underwriting Agencies Limited and on syndicates 2 and 49 (collectively referred to as 'the PCW syndicates') net of any applicable tax. This is reflected within these financial statements and disclosed in note 26, but the Council will be required to approve proposals before any payments are made.

GROSS INSURANCE CLAIMS INCURRED AND INSURANCE CLAIMS RECOVERABLE FROM REINSURERS

The Society has three insurance company subsidiary undertakings, Centrewrite Limited, Lioncover Insurance Company Limited and Lloyd's Reinsurance Company (China) Limited ('LRCCL'). Centrewrite provides Exeat insurance to resigned members participating only on run-off syndicates, allowing an early exit from Lloyd's and Estate Protection Plan insurance to members. Subsequent to the year end, Centrewrite has entered into a reinsurance to close contract reinsuring the liabilities of a Lloyd's syndicate. The insurance contract liabilities of Lioncover were wholly reinsured into Equitas in 1997 and the company does not accept new business. Further security in respect of Lioncover's insurance liabilities has been provided as a result of the retrocession and run-off contract between Equitas and NICO. LRCCL, which was capitalised at RMB 200m (approximately £14m), commenced underwriting onshore reinsurance business throughout China during 2007. Lloyd's syndicates may participate in LRCCL by means of retrocession agreements which allow a 100% risk transfer.

OTHER GROUP OPERATING EXPENSES

Operating expenses increased in 2007 to £187.9m (2006: £170.8m) and are principally attributable to the Corporation. The increase includes an additional £10.0m contribution to the Lloyd's Pension Scheme to fund future discretionary increases to pensions in payment. Maintaining cost discipline is a priority, and opportunities to improve the efficiency of operations and bring down the cost of doing business at Lloyd's will continue to be sought, while focusing on achieving the rolling Three-Year Plan.

NET FINANCE INCOME

Finance costs of £53.8m in 2007 (2006: £32.9m) include interest on subordinated loan notes issued in November 2004 and on £500m perpetual subordinated capital securities issued during 2007of £52.5m (2006: £32.0m). Further details on the perpetual subordinated capital securities are included in note 17 on pages 137 and 138. The increase in finance income to £128.5m (2006: £52.9m) reflects strong returns from the Society's fixed income investments in 2007 and the increase in these holdings following investment of the proceeds of the perpetual subordinated capital securities during the year. The overall gross investment return on central assets was 6.6% (2006: 3.2%). The disposition of the Society's financial investments is set out in note 15 on pages 135 to 137.

TAXATION

A tax charge of £66.0m (2006: £7.0m) on the surplus before tax of £230.4m (2006: £90.6m) has been recognised for the year ended 31 December 2007. Further details are set out in note 8 on pages 127 and 128.

PENSION SCHEMES

Lloyd's Pension Scheme

On an IFRS valuation basis, the group pension scheme valuation at 31 December 2007 improved from a deficit of £45.1m to a surplus of £16.5m before allowance for deferred tax of £4.6m (31 December 2006: £45.8m deficit before allowance for a deferred tax asset of £13.5m). The movement in the pension liabilities during the year is summarised below:

	2007 £m
Pension liabilities as at 1 January 2007	**(45.1)**
Pension expense recognised in the group income statement	**(17.8)**
Employer contributions – normal	**4.1**
– special	**22.9**
Actuarial gain recognised in the group statement of recognised income and expense	**52.4**
Pension asset as at 31 December 2007	**16.5**

The actuarial valuation of liabilities is particularly sensitive to changes in market conditions, which determine the discount rate, and changes to mortality assumptions. Further details are provided in note 18 on pages 138 to 142 which includes the sensitivity of the valuation to changes in these assumptions.

Overseas pension schemes

Overseas pension schemes actuarial valuation at 31 December 2007 was unchanged from 2006 at £0.7m. Further details are provided in note 18.

FINANCIAL REVIEW CONTINUED

CASH FLOWS AND LIQUIDITY

Cash and cash equivalents decreased during the year ended 31 December 2007 by £28.6m to £181.7m (2006: £210.3m). Cash balances are maintained at appropriate levels to meet the short-term operating expenses of the Society. Any surplus cash balances are invested and are included as financial investments within the group balance sheet.

The Corporation's free cash balances are regularly monitored. Free cash represents the amounts, both at bank and on deposit, held in the UK and available to the Corporation to meet operating expenses, including those of overseas operations, excluding any client money balances held in respect of insurance and arbitration activities. Such free cash balances during the year ended 31 December 2007 increased by £5.3m to £84.0m (2006: £78.7m).

The liquidity of the Central Fund is monitored separately. Cash balances are managed to meet short-term operational commitments including the payment of drawdowns. Any surplus cash balances are invested in compliance with defined investment parameters approved by the Lloyd's Investment Committee.

CENTRAL FUND INVESTMENT STRATEGY

Central Fund investment strategy is considered in three parts: A prudent estimate of possible net cash flow requirements, to a 3-year horizon, is used to determine the value of assets to be maintained for liquidity purposes. These are commingled with other liquid assets of Lloyd's group companies and invested in bank deposits and other short-term securities, with maturities of up to 12 months, with the objective to maximise current income, with low risk, whilst ensuring that all cash flow requirements are met as they arise.

A significant element of Central Fund assets is invested to manage the financial risks arising from the Society's obligations to service and redeem its debt issues in the financial markets. Such obligations currently total more than £1 billion. Assets of similar value and currency to these liabilities are invested in fixed-interest securities of high credit quality, having average terms similar to those of the liabilities. In this way the currency and interest rate risks arising on the liabilities are off-set. Because fluctuations in the market value of the assets are reflected in the income statement, whilst changes in the value of the liabilities are not, the effect of this risk management process is not apparent in the short term. However, it will be effective over the life of the relevant liabilities.

Assets not identified as being required to meet particular liabilities are assumed to be available for investment in the longer term. The investment strategy applying to these assets has recently been reviewed, leading to changes in their disposition during 2007. Value at risk (VAR) methodology has been applied to assist with the objective of maximising expected investment returns over longer periods whilst controlling risk within defined limits.

Diversification amongst non-correlated asset classes has been used to ensure efficient risk management. Equity and bond exposures have been globally diversified and emerging market equity and bond investments have been added during 2007, as well as high yield bonds. The Fund has had exposure to global property, via a portfolio of property related equity securities, since 2006. Management of cash and fixed interest investments of high credit quality is undertaken 'in-house' by Lloyd's. Specialist third party investment managers are appointed to manage all other exposures. During 2007, Lloyd's utilised the services of investment consultants to assist with the selection of investment managers.

Also in pursuit of investment diversification, the Central Fund made a modest initial investment in hedge funds during 2007. These exposures are structured to provide Lloyd's with a high level of transparency, allowing risks to be carefully monitored. Investment is not via 'fund of hedge fund' vehicles, but directly in a diversified portfolio of hedge funds, for which a specialist manager is responsible. The initial performance of these investments has been encouraging. They have delivered a positive investment return in the period as well as demonstrating low volatility overall.

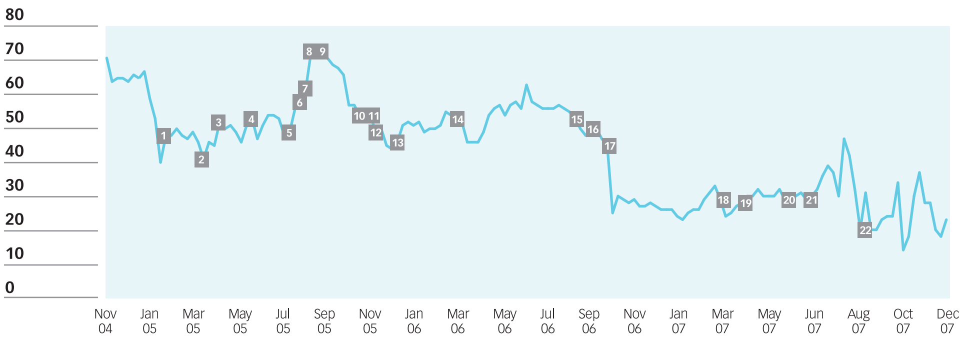
INVESTMENT PERFORMANCE

During the year ended 31 December 2007, the Society reported a 6.6% gross investment return (2006: 3.2%). This performance was aided by the high credit quality of the majority of the Society's fixed interest investments. New asset class exposures, resulting from revisions in investment strategy, were added gradually during the year and had limited effect on overall performance during the period.

CENTRAL FUND SUBORDINATED LOAN NOTES AND SUBORDINATED PERPETUAL CAPITAL SECURITIES

The yield of the Society's capital market debt issues, relative to the yield of other, similar insurance hybrid debt, is shown in the table below:

Lloyd's subordinated debt (2004 & 2007) issues: yield spread versus similar insurance hybrid debt
Spread (basis points)



1	CF Arbitration – announcement of worst case scenario	12	Fitch affirms Lloyd's 'A' rating
2	CF Arbitration – final settlement	13	Announcement of Lloyd's 3yr strategy
3	Lloyd's results for 2004	14	Announcement of Lloyd's 2005 results
4	London bombings	15	S&P reaffirms Lloyd's 'A' rating
5	Hurricane Katrina	16	Lloyd's 2006 interim results
6	S&P put Lloyd's debt on Creditwatch	17	Announcement of Equitas Reinsurance Deal
7	Lloyd's announces provisional estimate of net loss from Hurricane Katrina	18	Equitas deal/Fitch upgrade/Results released
8	Rita upgraded to major hurricane	19	S&P upgrade
9	Lloyd's interim results announced	20	Announcement of Lloyd's to issue Tier 1 Subordinated Debt
10	Lloyd's gives hurricanes update and 2006 capacity outlook	21	Sub-prime mortgage crisis starts
11	S&P affirms Lloyd's 'A' rating	22	Lloyd's 2007 interim result

The graph shows the difference between the yield at which the Lloyd's debt issues have traded in the capital markets and the yield on similar insurance hybrid debt, in the period since the Lloyd's debt was issued. Changes in this yield spread may be indicative of changes in investors' perceptions of the credit quality of Lloyd's debt obligations although other, more generic, capital market developments will also have an effect.

From the graph, it can be seen that the relative yield has varied significantly over the period. The substantial increases during 2005 coincide with Hurricane Katrina, while the fall in spreads at the end of 2006 reflects the announcement of the Equitas-Berkshire Hathaway reinsurance transaction and subsequent positive comments from the rating agencies.

During 2007, changes in this spread have been quite volatile, reflecting significant volatility in capital markets generally. However, on balance it has continued to decline. This comparative spread has now fallen by 50 basis points since Lloyd's first issued capital market debt in 2004, suggesting a significant improvement in investor's perception of Lloyd's, relative to other insurers, during this period.

FINANCIAL REVIEW CONTINUED

FINANCIAL RISK MANAGEMENT AND TREASURY POLICIES

OVERVIEW

The Society's principal financial instruments comprise cash and cash equivalents, investments, borrowings, provisions and items that arise directly from operations such as trade receivables and payables. These include assets and liabilities of the Central Fund.

The Society's treasury operations and investments are managed by reference to established policies which are reviewed regularly by the Lloyd's Investment Committee. Policies for managing these risks, in particular credit risk, liquidity risk and market risk, are summarised below:

CREDIT RISK

Credit risk represents the risk of financial loss to the Society if a counterparty, or the issuer of a security, fails to meet its contractual obligations.

Trade and other receivables

The Society's main source of income is from the Lloyd's market based primarily in the UK. The Society has established procedures to minimise the risk of default by trade and other receivables, which are mainly in respect of the Lloyd's market. These procedures include minimum standard checks for new market entrants.

Financial investments

A list of permissible bank counterparties, for the purposes of money-market investment, is maintained and restricted to banks having strong balance sheets and credit ratings. Investment parameters exist for all investment assets, controlling overall credit quality and ensuring appropriate risk diversification. Permitted counterparties to capital market transactions are also carefully controlled. All applicable parameters are reviewed regularly by the Lloyd's Investment Committee.

Guarantees

The Society provides certain financial guarantees as security for the underwriting activities of the members of Lloyd's. Further details are provided in note 25B on page 149.

LIQUIDITY RISK

The value and term of short-term assets are carefully monitored against those of the Society's liabilities. The Society maintains sufficient liquid assets to meet liabilities as they fall due.

The liquidity of the Central Fund is monitored separately. Cash balances are managed to meet short-term operational commitments including the payment of drawdowns. Any surplus cash balances are invested in compliance with defined investment parameters approved by the Lloyd's investment Committee.

The Society has no committed borrowing facilities as at 31 December 2007 (2006: £nil).

MARKET RISK

Market risk represents the risk that movements in financial markets will affect the financial position of the Society's. Market risks arising from the disposition of the Society's investments are monitored against defined parameters using Value at Risk (VAR) methodology. The position is reviewed regularly by the Lloyd's Investment Committee. As investments are actively monitored on a fair value basis, all investments are designated as fair value through profit or loss.

FOREIGN CURRENCY RISK

The Society enters into a variety of foreign exchange transactions in response to the foreign currency requirements of Lloyd's group companies. In managing the exposures arising from such foreign exchange activity, which may involve transactions for forward settlement, the net risk arising from all such exposures is considered and the level of this risk is managed within closely defined parameters. Consequently, while some net foreign exchange exposures may accrue to the Society from time to time as a result of this activity, the level of such exposures is carefully monitored and is not significant in the context of its combined activities.

Foreign currency exposures arising from overseas investments are considered together with foreign currency liabilities of the Society and net foreign currency exposures arising are managed through the use of forward foreign exchange contracts.

Separately, the Society provides a Currency Conversion Service (CCS) to participating Lloyd's syndicates, converting insurance premiums and claims between pounds sterling and other Lloyd's settlement currencies as required. Foreign exchange exposures arising from the provision of the CCS are again managed on a net basis, within defined parameters. The CCS is operated separately from other foreign exchange activity of the Society because, under the terms of the service, any profit (or loss) arising from CCS exposures is distributed to (or collected from) syndicates participating in the CCS. Currency exposures arising from CCS activity consequently do not, ultimately, represent risks to the Society.

INTEREST RATE RISK

Borrowings from the Lloyd's market for the purpose of funding statutory insurance deposits do not bear a fixed rate of interest. Instead, investment returns earned on the borrowed assets are passed on to lenders. Consequently, no interest rate risk arises on such borrowings.

Short-term assets held by the Society may be significant at certain times but such balances cannot be accurately predicted. These are invested in money market instruments of up to 12 months in duration with the objective of maximising current income while meeting liquidity requirements.

Interest rate risk arising from the requirement to make fixed rate coupon payments in respect of the Lloyd's subordinated loan notes and the perpetual subordinated capital securities is managed by investing relevant assets in securities having similar term profiles to the Lloyd's issues.

CAPITAL MANAGEMENT

The Society monitors its capital to ensure that it maintains sufficient assets for both operational and solvency purposes. During 2007, the Society issued £500m Tier 1 perpetual subordinated capital securities enabling the repayment of the syndicate loans. Further details are provided on pages 137 and 138.

Further disclosures with regard to financial instruments are provided in note 21 on pages 144 to 146.

RELATED PARTY TRANSACTIONS

Except for disclosures made in note 24 (see page 148), no other related party has had material transactions with the Society in 2007.

GOING CONCERN STATEMENT

After making enquiries, the members of the Council of Lloyd's have a reasonable expectation that the Society has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the Society's financial statements.

STATEMENT AS TO DISCLOSURE OF INFORMATION TO AUDITORS

Having made enquiries, the Council of Lloyd's confirms that:

- To the best of each Council member's knowledge and belief there is no information relevant to the preparation of the Society Report of which the Society's auditors are unaware.
- Each Council member has taken all the steps a Council member might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Society's auditors are aware of that information.

OUTLOOK

Central assets, which exclude subordinated liabilities, are expected to remain stable at £1.9bn in 2008.

On 2 April 2008, the Council of Lloyd's gave further undertakings to certain corporate members to use the New Central Fund to discharge the liability of those members where they have unpaid cash calls and do not have the resources to meet those cash calls. After taking account of the expiry of unutilised undertakings, the net increase in undertakings, which will be reflected as a charge in the 2008 income statement is £13m (see note 4 on pages 125 and 126).

The operating expenses for the Corporation are budgeted to increase by £8m to £182m in 2008 (2007: actual £174m) reflecting the continuing focus of achieving the rolling Three-Year Plan.

STATEMENT OF THE COUNCIL OF LLOYD'S RESPONSIBILITIES IN RELATION TO THE FINANCIAL STATEMENTS

The Council of Lloyd's is responsible for preparing the group financial statements in accordance with byelaws made under Lloyd's Act 1982 and International Financial Reporting Standards (IFRS) adopted by the European Union.

The Council of Lloyd's is required to prepare group financial statements for each financial year which present fairly the financial position of the Society and the financial performance and cash flows of the Society for that period. In preparing those group financial statements, the Council of Lloyd's is required to:

→ Select suitable accounting policies and then apply them consistently.

→ Present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information.

→ Provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Society's financial position and financial performance.

→ State that the Society has complied with IFRS, subject to any material departures disclosed and explained in the group financial statements.

The Council of Lloyd's is responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Society and enable it to ensure that the group financial statements comply with Article 4 of the IAS Regulation. As the Society's subordinated debt and perpetual subordinated capital securities are admitted to trading in a regulated market in the European Union, Article 4 requires group financial statements to be prepared in conformity with International Accounting Standards. The Council of Lloyd's is also responsible for safeguarding the assets of the Society and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Council of Lloyd's is responsible for the maintenance and integrity of the corporate and financial information included on the Society's website (www.lloyds.com). Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF LLOYD'S

We have audited the group financial statements of the Society of Lloyd's ('the Society') for the year ended 31 December 2007 which comprise the group income statement, group statement of recognised income and expense, group balance sheet, group cash flow statement and the related notes 1 to 26. These group financial statements have been prepared under the accounting policies set out therein. We have also audited the information in the Report of the Nominations, Appointments and Compensation Committee that is described as having been audited.

This report is made solely to the members of Lloyd's, as a body, in accordance with the Council of Lloyd's instructions summarised under 'Respective responsibilities of the Council of Lloyd's and auditors' below. Our audit work has been undertaken so that we might state to the members of Lloyd's as a body those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the members of Lloyd's as a body, for our audit work, for this report or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF THE COUNCIL OF LLOYD'S AND AUDITORS

The Council of Lloyd's is responsible for the preparation of the group financial statements in accordance with byelaws made under Lloyd's Act 1982 and International Financial Reporting Standards (IFRS) as adopted by the European Union as set out in the Statement of the Council of Lloyd's Responsibilities and for the preparation of the Report of the Nominations, Appointments and Compensation Committee.

Our responsibility is to audit the group financial statements and the part of the Report of the Nominations, Appointments and Compensation Committee to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). We report to you our opinion as to whether the group financial statements give a true and fair view and are properly prepared in accordance with Article 4 of the IAS Regulation and the part of the Report of the Nominations, Appointments and Compensation Committee to be audited is properly prepared in accordance with the basis described therein. We also report to you if, in our opinion, the Report of the Nominations, Appointments and Compensation Committee is not consistent with the group financial statements, if the Society has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding members' remuneration and other transactions is not disclosed. We read other information contained in the Annual Report and consider whether it is consistent with the audited group financial statements. This other information comprises the Society's Financial Highlights and Financial Review. We consider the implications for our report if we become aware of any apparent misstatement or material inconsistencies with the group financial statements. Our responsibilities do not extend to any other information.

BASIS OF AUDIT OPINION

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the group financial statements and the part of the Report of the Nominations, Appointments and Compensation Committee to be audited. It also includes an assessment of the significant estimates and judgments made by the Council of Lloyd's in the preparation of the group financial statements, and of whether the accounting policies are appropriate to the group's and Society's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the group financial statements and the part of the Report of the Nominations, Appointments and Compensation Committee to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the group financial statements and the part of the Report of the Nominations, Appointments and Compensation Committee to be audited.

OPINION

In our opinion:

→ The group financial statements give a true and fair view, in accordance with IFRS as adopted by the European Union, of the state of the group's affairs as at 31 December 2007 and of its surplus for the year then ended and have been properly prepared in accordance with Article 4 of the IAS Regulation.

→ The part of the Report of the Nominations, Appointments and Compensation Committee to be audited have been properly prepared in accordance with the basis described therein.

Ernst & Young LLP, Registered Auditor, London

2 April 2008

GROUP INCOME STATEMENT

for the year ended 31 December 2007

	Note	2007 £000	2006 £000
Operating income		**177,853**	171,498
Central Fund contributions		**168,346**	152,226
General insurance net premium income		**2,046**	2,834
Other group income		**81,478**	23,477
Total income	3B	**429,723**	350,035
Central Fund claims and provisions released/(incurred)	4	**18,208**	(115,735)
Contribution to Equitas – Berkshire Hathaway transaction	26	**(90,000)**	–
Gross insurance claims	13	**16,330**	(55,461)
Insurance claims recoverable from reinsurers	13	**(17,041)**	56,804
Other group operating expenses	5	**(187,866)**	(170,795)
Operating surplus		**169,354**	64,848
Finance costs	7	**(53,752)**	(32,921)
Finance income	7	**128,468**	52,942
Unrealised exchange (losses)/gains on borrowings		**(18,059)**	3,842
Share of profits of associates	12A	**4,395**	1,867
Surplus before tax		**230,406**	90,578
Tax charge	8A	**(65,994)**	(7,012)
Surplus for the year		**164,412**	83,566

GROUP STATEMENT OF RECOGNISED INCOME AND EXPENSE

for the year ended 31 December 2007

	Note	2007 £000	2006 £000
Exchange difference on translating foreign operations		**43**	(17)
Unrealised gain on revaluation of Lloyd's Collection	12B	**1,138**	–
Actuarial gain/(loss) on pension liabilities – group	18	**52,452**	(1,867)
– associates	12A	**1,835**	970
Tax (charge)/credit on items taken directly to equity		**(18,357)**	193
Net income and expense recognised directly in equity		**37,111**	(721)
Surplus for the year		**164,412**	83,566
Total recognised income and expense for the year		**201,523**	82,845

GROUP BALANCE SHEET

as at 31 December 2007

	Note	2007 £000	2006 £000
Assets			
Intangible assets	9	**438**	319
Lloyd's Collection	12B	**10,848**	9,710
Property, plant and equipment	10	**15,463**	12,036
Deferred tax asset	8C	**–**	7,423
Investment in associates	12A	**7,504**	4,379
Insurance contract assets – Lioncover Insurance Company Limited	13	**387,440**	432,405
– other insurance activities		**381**	–
Pension asset	18	**16,500**	–
Loans recoverable	14	**61,826**	62,201
Financial investments	15	**1,981,476**	1,498,343
Inventories		**197**	184
Trade and other receivables due within one year		**51,956**	26,568
Prepayments and accrued income		**39,650**	12,397
Tax receivable		**–**	6,759
Forward currency contracts	21	**9,440**	3,500
Cash and cash equivalents	16	**181,689**	210,298
Total assets		**2,764,808**	2,286,522
Equity and liabilities			
Equity			
Accumulated reserve	22	**927,684**	733,667
Syndicate loans	22	**–**	213,560
Revaluation reserve	22	**10,848**	9,710
Foreign currency translation reserve	22	**42**	(1)
Total equity		**938,574**	956,936
Liabilities			
Subordinated notes and perpetual subordinated capital securities	17	**1,011,754**	497,374
Insurance contract liabilities – Lioncover Insurance Company Limited	13	**387,440**	432,405
– other insurance activities	13	**14,319**	14,148
Pension liabilities	18	**667**	45,776
Deferred tax liability	8C	**13,654**	–
Provisions	19	**132,226**	162,160
Loans funding statutory insurance deposits		**101,562**	120,812
Trade and other payables	20	**68,019**	30,406
Accruals and deferred income		**44,045**	23,795
Tax payable		**31,788**	–
Forward currency contracts	21	**20,760**	2,710
Total liabilities		**1,826,234**	1,329,586
Total equity and liabilities		**2,764,808**	2,286,522

Approved and authorised for issue by the Council of Lloyd's on 2 April 2008 and signed on their behalf by

Lord Levene of Portsoken, Chairman **Richard Ward, Chief Executive Officer**

GROUP CASH FLOW STATEMENT

for the year ended 31 December 2007

	Note	2007 £000	2006 £000
Surplus before tax		**230,406**	90,578
Net finance income	7	**(74,716)**	(20,021)
Unrealised exchange losses/(gains) on borrowings		**18,059**	(3,842)
Share of profits of associates	12A	**(4,395)**	(1,867)
Operating surplus		**169,354**	64,848
Central Fund claims and provisions (released)/incurred		**(18,208)**	115,735
Operating surplus before Central Fund claims and provisions		**151,146**	180,583
Adjustments for:			
Depreciation of property, plant and equipment	10	**2,536**	1,966
Amortisation of intangible assets	9	**161**	167
Impairment losses		**352**	354
(Profit)/loss on sale of plant and equipment		**(41)**	51
Operating surplus before working capital changes and claims paid		**154,154**	183,121
Changes in Pension obligations	18	**(8,600)**	–
(Increase)/decrease in receivables		**(57,681)**	12,238
(Increase)/decrease in inventories		**(13)**	217
Increase/(decrease) in payables		**62,661**	(46,190)
Decrease in provisions other than for Central Fund claims		**(814)**	(1,925)
Cash generated from operations before claims paid		**149,707**	147,461
Claims paid in respect of corporate members		**(9,348)**	(131,099)
Tax and interest payments in respect of corporate members		**(83)**	(125)
Claims paid in respect of individual members		**(307)**	(1,274)
Claims paid in respect of Limited Financial Assistance Agreements		**(1,174)**	(2,270)
Cash generated from operations		**138,795**	12,693
Tax (paid)/received		**(20,183)**	1,836
Net cash from operating activities		**118,612**	14,529
Cash flows from investing activities			
Purchase of plant, equipment and intangible assets		**(6,531)**	(7,603)
Proceeds from the sale of equipment		**233**	83
Purchase of financial investments		**(2,354,029)**	(1,176,951)
Sale of financial investments		**1,797,931**	670,892
Increase in short-term deposits		**121,069**	113,378
Dividends received from associates	12A	**2,554**	2,329
Interest received		**76,601**	74,886
Dividends received		**4,494**	4,253
Gain on forward currency contracts		**5,777**	14,401
Net cash used in investing activities		**(351,901)**	(304,332)
Cash flows from financing activities			
Syndicate loan interest paid		**(13,401)**	(4,365)
Other interest paid		**(32,675)**	(46,515)
(Decrease)/increase in borrowings for statutory insurance deposits		**(32,625)**	20,165
Issue of perpetual subordinated capital securities		**500,000**	–
Issue costs in respect of perpetual subordinated capital securities		**(4,494)**	–
Receipt of syndicate loans		**121,107**	112,578
Repayment of syndicate loans		**(331,611)**	–
Net proceeds from financing activities		**206,301**	81,863
Net decrease in cash and cash equivalents		**(26,988)**	(207,940)
Effect of exchange rates on cash and cash equivalents		**(1,621)**	1,129
Cash and cash equivalents at 1 January		**210,298**	417,109
Cash and cash equivalents at 31 December	16	**181,689**	210,298

NOTES TO THE FINANCIAL STATEMENTS

as at 31 December 2007

1. BASIS OF PREPARATION AND CONSOLIDATION

In 1871, by Lloyd's Act 1871, the then existing association of underwriters was incorporated as the Society and Corporation of Lloyd's (the 'Society'). Its activities are accordingly governed by statute and, since 1982, have been managed by the Council of Lloyd's (the 'Council') pursuant to Lloyd's Act 1982.

The Society's main corporate purposes are to facilitate the carrying on of insurance business by members of Lloyd's and the advancement and protection of their interests in this context. The group financial statements of the Society of Lloyd's (the 'Society') comprise the financial statements of the Society of Lloyd's and all its subsidiary undertakings, the Lloyd's Central Fund and the group's interest in associates as at each balance sheet date. Subsidiary undertakings are consolidated from the date of their acquisition, being the date on which the Society obtains control, and continue to be consolidated until the date that such control ceases. The financial statements are prepared using consistent accounting policies. All intra-group balances and transactions have been eliminated in full.

The financial statements of subsidiary undertakings are prepared for the same reporting year as the parent company with the exception of Lioncover Insurance Company Limited (Lioncover) which has a reporting year of 31 March. This reporting date is the consequence of all Lioncover's reinsurance liabilities being reinsured with Equitas Reinsurance Limited (Equitas) and hence its alignment to Equitas' reporting year. Reinsurance contract assets and liabilities at 31 March have been adjusted to reflect claims settled from April to December.

The group financial statements have been prepared in accordance with International Financial Reporting Standards (as adopted by the European Union) and on a historic cost basis, except for financial assets and liabilities at fair value through profit or loss and the Lloyd's Collection, which are measured at fair value. Loans and receivables and other financial liabilities are carried at amortised cost. The group financial statements are presented in sterling and all values are rounded to the nearest thousand (£000).

The Society has adopted IFRS 7 (Financial Instruments: Disclosures). The Society has also adopted the amendments to IAS 1 (Presentation of Financial Statements – Capital Disclosures).

There has been no impact on the primary financial statements as a result of adopting this standard or amendments.

The Society is regulated by the FSA.

2. PRINCIPAL ACCOUNTING POLICIES

GENERAL

In preparing the financial statements significant estimates and assumptions are made in respect of some of the items reported. The main accounting policies identified involving such assessments are considered to be:

- Central Fund claims and provisions – undertakings (see note 2Q and note 19).
- Employee benefits – defined benefit pension scheme (see note 2I and note 18).
- Insurance contracts – liabilities and reinsurance assets (see note 2G and note 13).
- Loans recoverable – hardship loans (see note 2J and note 19).

A. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are held at cost less accumulated depreciation and any impairment in value.

Depreciation is charged on a straight line basis on the following principal categories:

- Freehold buildings are depreciated over 60 years.
- Plant, vehicles and equipment are depreciated over 3 to 25 years according to the estimated life of the asset.
- Equipment on hire or lease is depreciated over the period of the lease.
- Land is not depreciated.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

2. PRINCIPAL ACCOUNTING POLICIES CONTINUED

B. SOFTWARE DEVELOPMENT

Costs incurred in acquiring and developing computer software are capitalised as intangible assets where the software supports a significant business system and the expenditure leads to the creation of an identifiable asset of value. Software development is held at cost less accumulated depreciation and any impairment in value. Capitalised software is amortised over three years.

C. LLOYD'S COLLECTION

Lloyd's Collection represents various paintings, antiques and artefacts which are included at fair value. Any revaluation surplus or deficit is taken to equity and is reflected in the revaluation reserve.

D. INVESTMENT IN ASSOCIATES

An associate is an entity in which the Society has significant influence and which is not a subsidiary undertaking or joint venture. The Society's investment in associates is accounted for under the equity method of accounting.

Under the equity method, the investment in associates is carried in the group balance sheet at cost plus post-acquisition changes in the Society's share of net assets of the associate. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised. After application of the equity method, the Society determines whether it is necessary to recognise any additional impairment loss with respect to the Society's net investment in the associate. The group income statement reflects the share of the results of operations of the associate. Where there has been a change recognised directly in the equity of the associate, the group recognises its share of any changes and discloses this, when applicable, in the group statement of recognised income and expense.

E. IMPAIRMENT OF ASSETS

The Society performs annual impairment testing to assess whether there is an indication that an asset may be impaired. If any such indication exists the Society makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. When the carrying amount exceeds its recoverable amount, the asset is considered impaired and written down to its recoverable amount.

F. FINANCIAL INSTRUMENTS

The Society classifies its financial instruments within the scope of IAS 39 into the following categories: financial assets and liabilities at fair value through profit or loss, loans and receivables and other financial liabilities. The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of its financial instruments at initial recognition as follows:

i) Financial assets and liabilities at fair value through profit or loss (including derivatives held for trading)

Financial assets and liabilities at fair value through profit or loss include financial instruments held for trading and those assets designated at fair value through profit or loss. A financial instrument is classified in this category if it is so designated by management on initial recognition. Financial investments are classified in this category, and meet the recognition criteria under IAS 39, as the investment portfolios are managed on a fair value basis. Derivatives are included as held for trading.

ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the group provides money, goods or services directly to a debtor with no intention of trading the receivable.

iii) Other financial liabilities

Other financial liabilities, which include the subordinated loan notes and the subordinated perpetual capital securities, are carried at amortised cost using the effective interest method.

2. PRINCIPAL ACCOUNTING POLICIES CONTINUED

F. FINANCIAL INSTRUMENTS CONTINUED

When financial instruments are recognised initially, they are measured at fair value plus, in the case of loans and receivables and other financial liabilities, transaction costs. Gains and losses arising from changes in the fair value of financial assets and liabilities at fair value through profit or loss are included in the group income statement in the period in which they arise. When financial assets and liabilities are interest-bearing, interest calculated using the effective interest method is recognised in the group income statement. Loans and receivables and other financial liabilities are carried at amortised cost using the effective interest method.

The Society assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. When a financial investment or a loan and receivable is impaired, the impairment is recorded separately within an allowance account except for when the Society considers the amount owing to be irrecoverable; at this point, the amount is written off directly against the financial asset. When a financial investment is impaired, the impairment is recognised within finance income in the group income statement. When a loan and receivable is impaired the impairment is recognised within other group operating expenses in the group income statement. Purchases and sales of investments are recognised on the settlement date. Other investments are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Society has transferred substantially all risks and rewards of ownership.

iv) Fair value estimation

The fair value of financial instruments traded in organised active financial markets is based on quoted market prices at the close of business on the balance sheet date. The quoted market price used for financial assets held by the Society is the current bid price; the appropriate quoted market price for financial liabilities is the current offer price.

The fair value of financial instruments for which there is no quoted market price is determined by a variety of methods incorporating assumptions that are based on market conditions existing at each balance sheet date.

The fair value of forward currency contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

The nominal value less estimated credit adjustments of trade receivables and payables are assumed to approximate to their fair values.

G. INSURANCE CONTRACTS (LIABILITIES AND REINSURANCE ASSETS)

In accordance with IFRS 4 'Insurance contracts', the Society applies established UK accounting practices for insurance contracts, modified as appropriate to comply with the IFRS framework and applicable standards. This includes the application of the Statement of Recommended Practice (SORP) on accounting for insurance business issued by the Association of British Insurers in December 2005 (amended December 2006).

Insurance contracts are defined as those containing significant insurance risk which arises if, and only if, an insured event could cause an insurer to pay significant additional benefits in any scenario, excluding scenarios that lack commercial substance, at the inception of the contract. Such contracts remain insurance contracts until all rights and obligations are extinguished or expire. Contracts can be reclassified as insurance contracts after inception if insurance risk becomes significant.

Reinsurance assets primarily include amounts due from Equitas arising from the reinsurance arrangements entered into by Lioncover as described in note 13. An impairment review is performed on all reinsurance assets when an indication of impairment occurs. Reinsurance assets are impaired only if there is objective evidence that the Society may not receive all amounts due to it under the terms of the contract and that this can be measured reliably.

H. INVENTORIES

Inventories are stated at the lower of cost and net realisable value on a first in, first out (FIFO) basis. Net realisable value is the estimated selling price in the ordinary course of business less estimated costs necessary to make the sale.

I. EMPLOYEE BENEFITS

The Society accounts for pensions and similar benefits (principally income protection due to ill-health) under IAS 19 'Employee Benefits'. The Society operates a number of defined benefit pension schemes in which obligations are measured at discounted present value using the projected unit credit method, while plan assets are recorded at fair value. The operating and financing income and costs of the scheme are recognised in the group income statement. Service costs and financing income and costs are recognised in the periods in which they arise. Actuarial gains and losses are recognised in full in the group statement of recognised income and expense in the period in which they occur. Costs of discretionary awards in respect of past service are recognised in the group income statement when amounts are committed to be paid or there is a constructive liability to make awards to pensioners.

Payments to separately administered defined contribution schemes are charged to the group income statement as they fall due.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

2. PRINCIPAL ACCOUNTING POLICIES CONTINUED

J. LOANS RECOVERABLE

Recoverable Central Fund loans made to hardship members are managed on a fair value basis and are designated as fair value through profit or loss. Any gains and losses arising from changes in the fair value are included in the group income statement in the period in which they arise.

Fair values are determined by reference to an estimate of the valuation of the underlying securities at the dates at which they may be exercised and discounted back to present day values. A security can normally only be exercised on the later date of death of the member or of their spouse. This date is assessed using actuarial assumptions.

K. TAXATION

Corporation tax on the surplus or deficit for the periods presented comprises current and deferred tax. Corporation and income tax is recognised in the group income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax liabilities are recognised for all taxable temporary differences and deferred tax assets are recognised for all deductible temporary differences and unutilised tax losses to the extent that it is probable that taxable profits will be available against which the deductible temporary differences or tax losses can be utilised.

Deferred tax is measured on an undiscounted basis at the rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantially enacted at the balance sheet date.

L. SUBORDINATED LOAN NOTES AND PERPETUAL SUBORDINATED CAPITAL SECURITIES

Subordinated debt is initially recognised at cost, being the fair value of the consideration received net of issue costs associated with the borrowing.

After initial recognition, the subordinated debt is subsequently recorded at amortised cost using the effective interest rate over the period to the earliest option date. Amortised cost is calculated after taking into account issue costs and issue discount.

M. CASH AND CASH EQUIVALENTS

For the purposes of the group cash flow statement, cash comprises cash at banks and demand deposits, and cash equivalents comprise highly liquid investments that are convertible into cash with an insignificant risk of changes in value with original maturities of less than three months.

N. INCOME RECOGNITION

Income which is stated net of value added tax comprises the fair value of amounts receivable. Income is recognised as follows:

i) Members' subscriptions, market charges and other services

Members' subscriptions, market charges and other services are recognised in the period to which the service is provided. They are recognised on a basis that reflects the timing, nature and value of the benefits provided.

ii) Central Fund contributions

Central Fund contributions from members underwriting in the year are recognised when no significant uncertainty as to its collectibility exists.

iii) Interest income

Interest receivable is recognised in the group income statement on a time apportioned basis using the effective interest method. Any unwinding of discount is recognised as interest income.

iv) Dividend income

Dividend income from equity investments is included in the group income statement on the ex-dividend date.

v) Other income

Other income is recognised when recoverability is agreed.

O. INSURANCE PREMIUMS

Insurance premiums represent premiums on business incepting during the year, together with adjustments for premiums written in previous accounting periods. Premiums written are stated before deduction of commissions but net of taxes, duties levied on premiums and other deductions.

P. INSURANCE CLAIMS

Claims incurred in insurance related activities consist of claims and claims handling expenses paid during the year together with the movement in outstanding claims. Outstanding claims are the estimated final cost of all claims incurred but not settled at the balance sheet date, including claims incurred but not reported (IBNR). Outstanding claims are not discounted. Subsequent information and events may result in the ultimate liability being less than, or greater than, the amount provided. Any differences between the provision and subsequent settlements are reflected within the group financial statements of later years.

2. PRINCIPAL ACCOUNTING POLICIES CONTINUED

Q. CENTRAL FUND CLAIMS AND PROVISIONS

Central Fund claims and provisions (undertakings) are accounted for when they are approved by the Council and become contractual commitments. These undertakings are granted wholly at the discretion of the Council for a fixed period, normally one year, and therefore are not deemed to be constructive obligations, except for renewals of those commitments previously granted. For those corporate members in provisional liquidation, the Council provides a supporting commitment, which will ensure that in no circumstance will an insurance creditor receive less than the amount it would have received in a winding up, commencing on the date of the provisional liquidation. As the supporting undertakings are legally enforceable commitments, an estimate of their value is included within provisions in the group financial statements and changes during the period are reflected in the group income statement.

Recoveries in respect of the undertakings previously given are credited to the group income statement when contractually committed to be received.

R. FOREIGN CURRENCY AND DERIVATIVE INSTRUMENTS

i) Functional and presentation currency

The group financial statements are presented in sterling, which is the Society's functional and presentation currency. Items included in the financial statements of each of the Society's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency).

ii) Transactions and balances

Transactions in foreign currencies are recorded at the exchange rate prevailing on the date of the transaction. At each balance sheet date, monetary assets and liabilities denominated in foreign currencies are retranslated at the exchange rate prevailing at the balance sheet date. Translation differences on monetary items are taken to the group income statement.

Translation differences on non-monetary items measured at fair value are reported as part of the fair value gain or loss and are included in the group income statement.

The results and financial position of overseas Society operations are translated into sterling as follows:

- → Assets and liabilities are translated at the closing rate at the date of that balance sheet.
- → Income and expenses are translated at the average exchange rate for the year.
- → All resulting exchange differences are recognised as a separate component of equity.

The Society enters into forward currency contracts to manage exposures to fluctuation in foreign exchange rates, and to provide a service to the Lloyd's market. Where gains and losses are not expected to be refunded to or recovered from the Lloyd's market, these amounts are taken to the group income statement.

The principal year end exchange rates were:

	2007	2006
US$	**1.99**	1.96
Can$	**1.96**	2.28
Euro	**1.36**	1.48

S. LEASES

Payments made under operating leases are charged to the group income statement on a straight-line basis over the period of the lease.

T. SYNDICATE LOANS

Syndicate loans are treated as equity in the financial statements until they are repaid as they have no fixed repayment date and the payment of interest is made only at the discretion of the Council. Interest on these loans is accounted for when the Council formally approve interest payments to be made. All syndicate loans were repaid on 31 July 2007 (see note 22).

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

2. PRINCIPAL ACCOUNTING POLICIES CONTINUED

U. NEW STANDARDS AND INTERPRETATIONS NOT APPLIED

The International Accounting Standards Board and International Financial Reporting Interpretations Committee have issued the following standards and interpretations relevant to the Society. At the date these financial statements were approved, the following standards were in issue but not effective:

	Effective date (for accounting periods beginning on or after)
International Accounting Standards	
IFRS 8 Operating Segments	1 January 2009
IAS 1 Presentation of Financial Statements (revision)	1 January 2009
International Financial Reporting Interpretations Committee (IFRIC)	
IFRIC 14 IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their interaction	1 January 2008

The Council does not consider that the adoption of these standards and interpretations will have a material impact on the Society's financial statements in the period of initial application.

3. SEGMENTAL ANALYSIS

Segment information is presented in respect of the Society's business segments. The primary business segments are based on the Society's management and internal reporting structure.

Intra-segment pricing is determined on an arm's length basis.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one period.

Segment information in respect of geographical location is not presented. The Society's main source of income is from the Lloyd's market based primarily in the UK. Assets are primarily held by the Society's UK based operations.

The Society's primary business segments are as follows:

i) Corporation of Lloyd's and non-insurance related subsidiary undertakings: the main corporate purposes are to facilitate the carrying on of insurance business by members of Lloyd's and the advancement and protection of their interests in this context. The activities of authorised insurance company subsidiary undertakings are excluded from this business segment.

ii) Lloyd's Central Fund: these funds comprising the New Central Fund and the 'Old' Central Fund are assets of the Society and are held and administered at the discretion of the Council, primarily as funds available for the protection of policyholders. Unless the approval of members is obtained, the New Central Fund may not be used for the purposes of extinguishing or reducing liabilities which have been reinsured by Equitas.

iii) Insurance activities: the Society has three insurance company subsidiary undertakings, Centrewrite Limited, Lioncover Insurance Company Limited, and Lloyd's Reinsurance Company (China) Limited. Centrewrite provides Exeat insurance to resigned members participating only on run-off syndicates allowing an early exit from Lloyd's and Estate Protection Plan insurance to members. The insurance contract liabilities of Lioncover were wholly reinsured into Equitas in 1997 and the company does not accept new business. Lloyd's Reinsurance Company (China) Limited commenced underwriting onshore reinsurance business throughout China in 2007.

3. SEGMENTAL ANALYSIS CONTINUED

A. Information by business segment	Note	2007 Corporation of Lloyd's £000	2007 Lloyd's Central Fund £000	2007 Insurance activities £000	2007 Society total £000
Segment income					
Segment income (unconsolidated)		181,968	245,662	5,367	432,997
Less intra-segment income		(3,274)	–	–	(3,274)
Total income from external sources	3B	178,694	245,662	5,367	429,723
Segment operating expenses (consolidated)					
Central Fund claims and provisions released	4	–	18,208	–	18,208
Contribution to Equitas – Berkshire Hathaway transaction		–	(90,000)	–	(90,000)
Gross claims released		–	–	16,330	16,330
Claims payable to reinsurers		–	–	(17,041)	(17,041)
Other group operating expenses:					
Employment (including pension costs)	6	(81,665)	–	(1,087)	(82,752)
Premises		(34,942)	–	(429)	(35,371)
Legal and professional	5	(14,579)	(1,714)	(287)	(16,580)
Systems and communications		(18,864)	–	(429)	(19,293)
Other		(20,899)	(10,658)	(2,313)	(33,870)
Total other group operating expenses		(170,949)	(12,372)	(4,545)	(187,866)
Total segment operating expenses		(170,949)	(84,164)	(5,256)	(260,369)
Central Fund finance costs	7	–	(53,339)	–	(53,339)
Central Fund and Insurance activity finance income	7	–	117,136	3,548	120,684
Unrealised exchange losses on borrowings		–	(18,059)	–	(18,059)
Segment surplus		7,745	207,236	3,659	218,640
Corporation finance costs	7	(413)	–	–	(413)
Corporation finance income	7	7,784	–	–	7,784
Share of profits of associates	12A	4,395	–	–	4,395
Tax charge					(65,994)
Surplus for the year					164,412
Segment assets and liabilities					
Segment assets		292,210	2,008,193	456,901	2,757,304
Investment in associates	12A	7,504	–	–	7,504
Total assets					2,764,808
Segment liabilities		(170,547)	(1,203,323)	(406,922)	(1,780,792)
Tax liabilities					(45,442)
Total liabilities					(1,826,234)
Other segment information					
Capital expenditure	9/10	5,807	–	980	6,787
Depreciation	10	2,424	–	112	2,536
Amortisation of intangible assets	9	93	–	68	161
Impairment of long-term assets	10	352	–	–	352
Average number of UK employees (permanent and contract)		673	–	3	676
Average number of overseas employees (permanent and contract)		85	–	11	96
Average number of total employees (permanent and contract)		758	–	14	772

Included within Central Fund other group operating expenses is the difference between the cost and the fair value at the date of acquisition, deemed to be nil, of an asset-backed commercial paper acquired from the Joint Asset Trust Fund.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

3. SEGMENTAL ANALYSIS CONTINUED

A. Information by business segment continued	Note	2006 Corporation of Lloyd's £000	2006 Lloyd's Central Fund £000	2006 Insurance activities £000	2006 Society total £000
Segment income					
Segment income (unconsolidated)		175,474	174,635	2,834	352,943
Less intra-segment income		(2,908)	–	–	(2,908)
Total income from external sources	3B	172,566	174,635	2,834	350,035
Segment operating expenses (consolidated)					
Central Fund claims and provisions incurred	4	–	(115,735)	–	(115,735)
Gross claims incurred		–	–	(55,461)	(55,461)
Claims recoverable from reinsurers		–	–	56,804	56,804
Other group operating expenses:					
Employment (including pension costs)	6	(72,586)	–	(410)	(72,996)
Premises		(34,629)	–	–	(34,629)
Legal and professional	5	(14,819)	(3,541)	(82)	(18,442)
Systems and communications		(20,394)	–	–	(20,394)
Other		(22,108)	(2,136)	(90)	(24,334)
Total other group operating expenses		(164,536)	(5,677)	(582)	(170,795)
Total segment operating expenses		(164,536)	(121,412)	761	(285,187)
Central Fund finance costs	7	–	(32,604)	–	(32,604)
Central Fund and Insurance activities finance income	7	–	46,119	501	46,620
Unrealised exchange gains/(losses) on borrowings		–	3,966	(124)	3,842
Segment surplus		8,030	70,704	3,972	82,706
Corporation finance costs	7	(317)	–	–	(317)
Corporation finance income	7	6,322	–	–	6,322
Share of profits of associates	12A	1,867	–	–	1,867
Tax charge					(7,012)
Surplus for the year					83,566
Segment assets and liabilities					
Segment assets		281,399	1,505,902	480,660	2,267,961
Investment in associates	12A	4,379	–	–	4,379
Tax assets					14,182
Total assets					2,286,522
Segment liabilities		(220,215)	(662,240)	(447,131)	(1,329,586)
Other segment information					
Capital expenditure	9/10	7,374	–	–	7,374
Depreciation	10	1,966	–	–	1,966
Amortisation of intangible assets	9	167	–	–	167
Impairment of long-term assets	10	354	–	–	354
Average number of UK employees (permanent and contract)		666	–	3	669
Average number of overseas employees (permanent and contract)		92	–	–	92
Average number of total employees (permanent and contract)		758	–	3	761

3. SEGMENTAL ANALYSIS CONTINUED

B. Income	Corporation of Lloyd's 2007 £000	2006 £000	Lloyd's Central Fund 2007 £000	2006 £000	Insurance activities 2007 £000	2006 £000	Society total 2007 £000	2006 £000
Market charges								
Managing agents and syndicates	**61,282**	56,949	**–**	–	**255**	–	**61,537**	56,949
Members and members' agents	**14,133**	14,893	**–**	–	**–**	–	**14,133**	14,893
Franchise performance and risk Management charge	**12,442**	12,041	**–**	–	**–**	–	**12,442**	12,041
Total market charges	**87,857**	83,883	**–**	–	**255**	–	**88,112**	83,883
Members' subscriptions	**81,376**	74,455	**–**	–	**–**	–	**81,376**	74,455
Other charges	**7,680**	11,907	**–**	1,253	**685**	–	**8,365**	13,160
Total operating income	**176,913**	170,245	**–**	1,253	**940**	–	**177,853**	171,498
Central Fund contributions	**–**	–	**168,346**	152,226	**–**	–	**168,346**	152,226
General insurance net premium income	**–**	–	**–**	–	**2,046**	2,834	**2,046**	2,834
Litigation settlement receipts	**–**	–	**26,000**	–	**–**	–	**26,000**	–
Equitas return premium	**–**	–	**–**	–	**2,381**	–	**2,381**	–
Other income	**1,781**	2,321	**51,316**	21,156	**–**	–	**53,097**	23,477
Other group income	**1,781**	2,321	**77,316**	21,156	**2,381**	–	**81,478**	23,477
Total income	**178,694**	172,566	**245,662**	174,635	**5,367**	2,834	**429,723**	350,035

In 2007, members contributed 1.00% (2006: 1.00%) of their allocated overall premium limit to the Central Fund. On 2 April 2007, members also made interest bearing loans to the Society from syndicate premium trust funds of 0.75% (2006: 0.75%), referred to as syndicate loans. The syndicate loans were treated as part of the Society's equity rather than as contributions from members in the group income statement. Following the issuance of £500m perpetual subordinated capital securities on 21 June, the syndicate loan capital was repaid in full on 31 July 2007 (see note 22).

The Society's subsidiary undertaking, Lioncover Insurance Company Limited, received a return premium of £2.4m from Equitas Holdings Limited as part of Phase 1 of the Equitas – Berkshire Hathaway transaction (see note 26). It is the intention to pass the benefit of the return premium to members on syndicates formerly managed by PCW Underwriting Agencies Limited, WMD Underwriting Agencies Limited and Richard Beckett Underwriting Agencies Limited and on syndicates 2 and 49 (collectively referred to as 'the PCW syndicates') net of any applicable tax. This is reflected within these financial statements, but the Council will be required to approve proposals before any payment is made.

Other group income includes market settlement recoveries which represent continuing debt recoveries from the 1996 'Reconstruction and Renewal' settlement and recoveries in respect of undertakings given by the Central Fund.

4. CENTRAL FUND CLAIMS AND PROVISIONS

	2007 £000	2006 £000
Undertakings released/(granted)	**14,828**	(114,576)
Decrease in the value of supporting commitments (note 19)	**6,057**	5,128
Provisions made in respect of Limited Financial Assistance Agreements (note 19)	**(2,287)**	(4,888)
Claims payable in respect of individual members	**(307)**	(1,274)
Tax and interest payable in respect of insolvent members	**(83)**	(125)
	18,208	(115,735)

The Council has given undertakings with financial limits to certain corporate members to use the New Central Fund to discharge the liability of those members where they have unpaid cash calls and do not have the resources to meet those cash calls. The purpose of these undertakings is primarily to allow valid claims made on policies underwritten by those insolvent members to continue to be paid in full. Undertakings are accounted for when they are approved by the Council and become contractual commitments. These undertakings are granted wholly at the discretion of the Council principally on an annual basis and therefore are not deemed constructive obligations (see note 19). Unutilised undertakings as at 31 December 2007 were £166m. Of these amounts, £123m were included in undertakings granted on 2 April 2008 and the balance of £43m has been released to the group income statement in these financial statements. On 2 April 2008, further annual undertakings of £13m were granted and no provision has been included in these financial statements in respect of these amounts.

Welcome to Lloyd's
Strategic review
Performance
Delivering value
Market results
Society report

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

4. CENTRAL FUND CLAIMS AND PROVISIONS CONTINUED

For those corporate members in provisional liquidation, the Council has also provided a supporting commitment, which will ensure that in no circumstance will an insurance creditor receive less than the amount it would have received in a winding up commencing on the date of the provisional liquidation.
As the supporting undertakings are legally enforceable commitments an estimate of their value, if applicable, has been included within provisions in the group financial statements and changes during the year are reflected in the group income statement, as shown in the table above.

5. OTHER GROUP OPERATING EXPENSES

	2007 Corporation of Lloyd's £000	2007 Lloyd's Central Fund £000	2007 Insurance activities £000	2007 Total £000
Other group operating expenses include:				
Employment costs (note 6)	**81,665**	**–**	**1,087**	**82,752**
Operating lease rentals – Lloyd's 1986 building	**16,767**	**–**	**–**	**16,767**
Operating lease rentals – other	**2,311**	**–**	**–**	**2,311**
Professional fees, including legal fees and related costs	**13,170**	**1,660**	**203**	**15,033**
Audit services	**287**	**54**	**65**	**406**
Assurance services payable to Ernst & Young LLP	**665**	**–**	**–**	**665**
Actuarial services payable to Ernst & Young LLP	**100**	**–**	**19**	**119**
Tax services payable to Ernst & Young LLP	**49**	**–**	**–**	**49**
Other services payable to Ernst & Young LLP	**308**	**–**	**–**	**308**
Total legal and professional fees	**14,579**	**1,714**	**287**	**16,580**
Charitable donations	**422**	**–**	**–**	**422**

Fees of £98,500 paid to Ernst & Young LLP in 2007 in relation to the perpetual subordinated capital securities issued in June 2007 have been capitalised and are not included above.

	2006 Corporation of Lloyd's £000	2006 Lloyd's Central Fund £000	2006 Insurance activities £000	2006 Total £000
Other group operating expenses include:				
Employment costs (note 6)	72,579	–	417	72,996
Operating lease rentals – Lloyd's 1986 building	16,767	–	–	16,767
Operating lease rentals – other	1,542	–	–	1,542
Professional fees, including legal fees and related costs	13,786	3,489	–	17,275
Audit services	284	52	63	399
Assurance services payable to Ernst & Young LLP	578	–	–	578
Actuarial services payable to Ernst & Young LLP	120	–	19	139
Tax services payable to Ernst & Young LLP	–	–	–	–
Other services payable to Ernst & Young LLP	51	–	–	51
Total legal and professional fees	14,819	3,541	82	18,442
Charitable donations	423	–	–	423

6. EMPLOYMENT

	2007 £000	2006 £000
Salaries and wages (including performance-related bonus)	**45,414**	42,923
Long-term Incentive Plan (excluding social security costs – note 19)	**822**	1,886
Lloyd's Pension Scheme costs (note 18)	**17,833**	10,524
Other pension costs	**224**	668
Social security costs	**5,338**	5,159
Severance costs	**1,629**	2,013
Contract and agency staff	**5,065**	5,708
Other employment costs	**6,427**	4,115
	82,752	72,996

The emoluments of the Chairman, CEO, members of the Council and Franchise Board are included in the report of the Nominations, Appointments and Compensation Committee on page 98.

7. FINANCE

	2007 Corporation of Lloyd's £000	2007 Lloyd's Central Fund £000	2007 Insurance activities £000	2007 Total £000	2006 Total £000
Finance costs					
Interest payable on financial liabilities measured at amortised cost	**–**	**(52,523)**	**–**	**(52,523)**	(32,046)
Other interest payable and similar charges	**(413)**	**–**	**–**	**(413)**	(317)
Amortisation of issue costs and discount	**–**	**(816)**	**–**	**(816)**	(558)
Total interest payable on financial liabilities	**(413)**	**(53,339)**	**–**	**(53,752)**	(32,921)
Finance income					
Bank interest received	**7,037**	**15,860**	**626**	**23,523**	17,772
Dividends received	**–**	**4,494**	**–**	**4,494**	4,253
Other returns on investments designated at fair value through profit or loss	**623**	**159,966**	**1,853**	**162,442**	14,826
Unrealised fair value movement of investments designated at fair value through profit or loss	**215**	**(58,379)**	**1,069**	**(57,095)**	(3,279)
Unrealised fair value movement of forward contracts held for trading	**(91)**	**(12,082)**	**–**	**(12,173)**	947
Realised fair value movement of forward contracts held for trading	**–**	**5,779**	**–**	**5,779**	14,400
Increase in valuation of loans recoverable designated at fair value through profit or loss	**–**	**1,498**	**–**	**1,498**	4,023
Total finance income	**7,784**	**117,136**	**3,548**	**128,468**	52,942

8. TAXATION

A. ANALYSIS OF CHARGE IN THE YEAR

	2007 £000	2006 £000
Current tax:		
Corporation tax based on profits for the year at 30% (2006: 30%)	**(61,800)**	(2,551)
Adjustments in respect of previous years	**(714)**	31
Foreign tax suffered	**(234)**	(112)
Total current tax	**(62,748)**	(2,632)
Deferred tax:		
Origination and reversal of temporary differences – current year	**(4,923)**	(19,817)
– prior year	**1,677**	15,437
Tax charge	**(65,994)**	(7,012)

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

8. TAXATION CONTINUED

B. RECONCILIATION OF EFFECTIVE TAX RATE

	2007 £000	2007 £000	2006 £000	2006 £000
Surplus on ordinary activities before tax		**230,406**		90,578
Corporation tax at 30%	**30.0%**	**(69,122)**	30.0%	(27,173)
Expenses not deductible for tax purposes	**2.1%**	**(4,798)**	1.2%	(1,138)
Non-taxable income	**(0.3%)**	**588**	(6.3%)	5,739
Utilisation of tax credits	**(0.1%)**	**279**	(0.1%)	103
Unutilised tax losses	**–**	**–**	0.6%	(545)
Utilisation of capital losses not previously recognised	**(2.1%)**	**4,952**	–	–
Overseas tax	**0.1%**	**(234)**	0.1%	(112)
Other	**(0.8%)**	**1,818**	(0.7%)	646
Deferred tax prior year adjustments	**(0.7%)**	**1,677**	(17.1%)	15,437
Deferred tax adjustment for change in tax rate	**0.2%**	**(440)**	–	–
Corporation tax prior year adjustments	**0.3%**	**(714)**	–	31
Tax charge (note 8A)	**28.6%**	**(65,994)**	7.7%	(7,012)

The deferred tax prior year credit of £1.7m arises from a reassessment of the assets qualifying for capital allowances (2006: £15.4m) arising from reassessment of tax base in respect of financial investments and loans recoverable.

C. DEFERRED TAX

	2007 Balance at 1 January £000	2007 Income Statement £000	2007 Equity £000	2007 Balance at 31 December £000
Property, plant and equipment	**4,590**	**(391)**	**–**	**4,199**
Loans recoverable	**(11,616)**	**1,958**	**–**	**(9,658)**
Financial investments	**(2,982)**	**1,810**	**–**	**(1,172)**
Pension liabilities/(assets)	**13,534**	**(3,360)**	**(14,794)**	**(4,620)**
Other employee benefits	**636**	**(8)**	**–**	**628**
Unutilised tax losses	**3,261**	**(3,261)**	**–**	**–**
Other items	**–**	**6**	**(3,037)**	**(3,031)**
	7,423	**(3,246)**	**(17,831)**	**(13,654)**

	2006 Balance at 1 January £000	2006 Income Statement £000	2006 Equity £000	2006 Balance at 31 December £000
Property, plant and equipment	2,760	1,830	–	4,590
Loans recoverable	–	(11,616)	–	(11,616)
Financial investments	(9,839)	6,857	–	(2,982)
Pension liabilities	15,663	(2,613)	484	13,534
Other employee benefits	952	(316)	–	636
Unutilised tax losses	173	3,088	–	3,261
Other items	1,610	(1,610)	–	–
	11,319	(4,380)	484	7,423

There were no unrecognised losses or deductible temporary differences in 2007 (2006: £8.9m).

9. INTANGIBLE ASSETS – SOFTWARE DEVELOPMENT

	Total £000
Cost:	
At 1 January 2006	4,568
Additions	342
Disposals	(29)
At 31 December 2006	4,881
Additions	**280**
At 31 December 2007	**5,161**
Amortisation:	
At 1 January 2006	4,392
Charge for the year	167
Impairment losses	32
Disposals	(29)
At 31 December 2006	4,562
Charge for the year	**161**
At 31 December 2007	**4,723**
Net book value at 31 December 2007	**438**
Net book value at 31 December 2006	319

The amortisation charge is included in other group operating expenses in the group income statement.

10. PROPERTY, PLANT AND EQUIPMENT

	Freehold land and buildings £000	Plant and equipment £000	Total £000
Cost:			
At 1 January 2006	413	38,113	38,526
Additions	–	7,032	7,032
Disposals	–	(1,575)	(1,575)
At 31 December 2006	413	43,570	43,983
Additions	**–**	**6,507**	**6,507**
Disposals	**(344)**	**(5,991)**	**(6,335)**
At 31 December 2007	**69**	**44,086**	**44,155**
Depreciation and impairment:			
At 1 January 2006	381	30,719	31,100
Depreciation charge for the year	–	1,966	1,966
Impairment losses	32	290	322
Disposals	–	(1,441)	(1,441)
At 31 December 2006	413	31,534	31,947
Depreciation charge for the year	**–**	**2,536**	**2,536**
Impairment losses	**–**	**352**	**352**
Disposals	**(344)**	**(5,799)**	**(6,143)**
At 31 December 2007	**69**	**28,623**	**28,692**
Net book value at 31 December 2007	**–**	**15,463**	**15,463**
Net book value at 31 December 2006	–	12,036	12,036

IMPAIRMENT LOSSES

Impairment reviews are undertaken annually in which assets within plant and other assets have their recoverable amounts reassessed. As part of this assessment of the carrying value of assets, £352,000 was written off in 2007 (2006: £322,000). The charge is included within other group operating expenses.

Welcome to Lloyd's
Strategic review
Performance
Delivering value
Market results
Society report

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

11. INVESTMENTS IN SUBSIDIARY UNDERTAKINGS AND ASSOCIATES

Entity	Nature of business	Proportion of equity capital held
Principal subsidiary undertakings		
Additional Securities Limited	Provision of deposits overseas on behalf of Lloyd's underwriters to comply with local insurance regulations	100%
Centrewrite Limited	Authorised UK insurance company	100%
Lioncover Insurance Company Limited	Authorised UK insurance company	100%
Lloyd's Reinsurance Company (China) Limited	Authorised reinsurance company in China (incorporated in 2007 with a share capital of RMB 200,000,000)	100%
Associates		
Ins-sure Holdings Limited	Provision of premiums and claims accounting and settlement, policy production and ancillary insurance services principally to the London insurance market	25%
Xchanging Claims Services Limited	Provision of claims and recoveries services	50%

The issued share capital of Ins-sure Holdings Limited is £4,000. There are three classes of shares. The Society holds 1,000,000 B shares of 0.1p each that have the right to participate in 25% of any profits available for distribution.

The issued share capital of Xchanging Claims Services Limited is £4,001. There are three classes of shares. The Society holds 1,000 A shares of £1 each and 2,001 C shares of £1 each. The A and C shares have the following rights with respect to dividends:

a) The C shares carry a right to a fixed cumulative preference dividend of 5% calculated on the nominal capital and a variable participating dividend calculated by reference to trading profits.

b) The A shares participate in 50% of any profits available for distribution after taking account of the dividend rights outlined above.

12. INVESTMENTS

A. INVESTMENTS IN ASSOCIATES

	2007 Goodwill £000	2007 Share of other net assets £000	2007 Total £000	2006 Total £000
At 1 January	**861**	**3,518**	**4,379**	4,162
Share of operating profits	**–**	**5,720**	**5,720**	2,794
Share of interest income	**–**	**334**	**334**	175
Share of tax on profit on ordinary activities	**–**	**(1,659)**	**(1,659)**	(1,102)
Total share of profits of associates	**–**	**4,395**	**4,395**	1,867
Share of actuarial gain on pension liability	**–**	**1,835**	**1,835**	970
Share of tax on items taken directly to equity	**–**	**(551)**	**(551)**	(291)
Dividends received	**–**	**(2,554)**	**(2,554)**	(2,329)
At 31 December	**861**	**6,643**	**7,504**	4,379

12. INVESTMENTS CONTINUED

A. INVESTMENTS IN ASSOCIATES CONTINUED

Summary financial information for associates – 100%:

	Assets £000	Liabilities £000	Revenues £000	Profit after tax £000
2007				
Ins-sure Holdings Limited	**43,968**	**(22,791)**	**61,052**	**7,530**
Xchanging Claims Services Limited	**14,150**	**(10,397)**	**35,789**	**3,876**
	58,118	**(33,188)**	**96,841**	**11,406**
2006				
Ins-sure Holdings Limited	27,900	(17,233)	57,211	3,935
Xchanging Claims Services Limited	12,824	(8,675)	29,383	3,748
	40,724	(25,908)	86,594	7,683

B. LLOYD'S COLLECTION

The Lloyd's Collection represents various paintings, antiques and artefacts. The collection was valued at £10.8m by Gurr Johns Limited, valuers and fine art consultants in September 2007, on the basis of open market auction value assuming all items are not sold at the same time taking into account the nature, age, condition and quality of each chattel. This resulted in a revaluation gain of £1.1m.

13. INSURANCE ACTIVITIES

For insurance contracts, claims provisions (comprising provisions for claims reported by policyholders and claims incurred but not reported) are established to cover the ultimate cost of settling the liabilities in respect of claims that have occurred and are estimated based on known facts at the balance sheet date. Outstanding claims provisions are not discounted for the time value of money.

	2007 Lioncover Insurance Company Limited £000	2007 Other insurance activities £000	2007 Total £000	2006 Total £000
Insurance claims				
Gross claims:				
Claims paid	**(21,592)**	**(1,064)**	**(22,656)**	(87,021)
Change in provision for claims	**38,718**	**268**	**38,986**	31,560
	17,126	**(796)**	**16,330**	(55,461)
Claims recoverable from reinsurers:				
Claims recovered from reinsurers	**21,592**	**–**	**21,592**	86,262
Change in reinsurance contract assets	**(38,718)**	**85**	**(38,633)**	(29,458)
	(17,126)	**85**	**(17,041)**	56,804

LIONCOVER INSURANCE COMPANY LIMITED

Lioncover Insurance Company Limited (Lioncover) is a wholly owned subsidiary undertaking of the Society of Lloyd's. Since its formation, Lioncover has reinsured the liabilities of private members on syndicates formerly managed by PCW Underwriting Agencies Limited, WMD Underwriting Agencies Limited and Richard Beckett Underwriting Agencies Limited and on syndicates 2 and 49 (collectively referred to as 'the PCW syndicates'). On 18 December 1997, Lioncover entered into an unlimited reinsurance of those liabilities with Equitas Reinsurance Limited (ERL).

Notwithstanding the reinsurance of liabilities by ERL, Lioncover remains liable to its policyholders in respect of the business originally underwritten. Accordingly, the Society's financial statements reflect a provision for claims outstanding, including losses incurred but not reported (IBNR), in respect of that business and an equal amount as recoverable from ERL.

Lioncover's long-term insurance liabilities include pollution and asbestos. Lioncover does not underwrite any new policies.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

13. INSURANCE ACTIVITIES CONTINUED

LIONCOVER INSURANCE COMPANY LIMITED CONTINUED

Insurance contract liabilities may be analysed as follows:

	2007 Insurance contract liabilities £000	2007 Reinsurer's share of liabilities £000	2007 Net £000	2006 Insurance contract liabilities £000	2006 Reinsurer's share of liabilities £000	2006 Net £000
Provision for claims reported	194,447	(194,447)	–	200,608	(200,608)	–
Provision for IBNR claims	192,993	(192,993)	–	231,797	(231,797)	–
Insurance contract liabilities	387,440	(387,440)	–	432,405	(432,405)	–

The movement in provision for insurance contract liabilities can be analysed as follows:

	2007 Insurance contract liabilities £000	2007 Reinsurer's share of liabilities £000	2007 Net £000	2006 Insurance contract liabilities £000	2006 Reinsurer's share of liabilities £000	2006 Net £000
At 1 January	432,405	(432,405)	–	526,848	(526,848)	–
Claims (released)/incurred	(17,126)	17,126	–	56,978	(56,978)	–
Claims paid (see below)	(21,592)	21,592	–	(86,262)	86,262	–
Effect of exchange rates	(6,247)	6,247	–	(65,159)	65,159	–
At 31 December	387,440	(387,440)	–	432,405	(432,405)	–

The comparative claims paid figures for 2006 have been restated from £124m to £86m to correct an overstatement of £38m. The overstatement had no net effect on the income statement or net assets.

The provision for claims outstanding is based upon actuarial and other studies of the ultimate cost of liabilities performed by ERL including exposure based and statistical estimation techniques.

Significant delays occur in the notification and settlement of certain claims, and a substantial measure of experience and judgement is involved in making the assumptions for assessing outstanding liabilities, the ultimate cost of which cannot be known with certainty at the balance sheet date. The gross provision for claims outstanding and related reinsurance recoveries is estimated on the basis of information currently available.

The provision for claims outstanding includes significant amounts in respect of notified and potential IBNR claims for long-tail liabilities. The settlement of these claims is not expected to occur for many years, and there is considerable uncertainty as to the amounts at which they will be settled.

Where a claim is disputed, the validity of the claim is ultimately an issue that can only be determined by the courts. The provision for a disputed claim is based on Lioncover's view as to the expected outcomes of such court decisions.

Uncertainty is further increased because of the potential for unforeseen changes in the legal, judicial, technological or social environment, which may increase or decrease the cost, frequency or reporting of claims, and because of the potential for new sources or types of claim to emerge.

ASBESTOS CLAIMS

In estimating asbestos liabilities, Lioncover follows a highly developed actuarial framework. The majority of asbestos reserves are estimated by modelling the expected claims from policyholders of the reinsured syndicates.

The number of future claims is projected for direct policyholders based on past claims experience combined with the results of epidemiological and, other relevant studies that predict the incidence of asbestos-related diseases into the future. This is then combined with estimates of the average cost of settling different types of claims for each policyholder to give a total value of claims to the relevant underlying policyholders. The results of these projections are then applied to the insurance coverage available for those policyholders, resulting in an estimation of Lioncover's liabilities arising from claims against those policyholders. The results are then adjusted to take into account liabilities in respect of policyholders that are not modelled explicitly, including an amount for those liabilities of which Lioncover may be currently unaware.

13. INSURANCE ACTIVITIES CONTINUED

ASBESTOS CLAIMS CONTINUED

The techniques described above include a number of important assumptions, including:

- The projected level of future valid claims filings for each policyholder by disease type.
- Future levels of claims settlements values.
- The impact of bankruptcy of policyholders on the amount and timing of claims payments.
- The legal interpretation of insurance policies and the outcome of litigation, based upon legal advice received.
- The period between the filing and payment of claims.

The assumptions on the proportion of claims filings that will ultimately lead to claims payments reflect an assessment that the claims management strategies adopted by Lioncover will reduce claims payments below the level that they would otherwise have been.

POLLUTION AND HEALTH HAZARD CLAIMS

Pollution liabilities are estimated for policyholders of the reinsured syndicates by evaluating the expected costs to be incurred by the policyholders in cleaning up polluted sites and then applying these costs to the insurance coverage available. The pollution liabilities expected by means of inward reinsurance are evaluated in a similar manner, but with the additional step of applying the ceding companies' expected liabilities to the reinsurance cover available.

Allowance is then made for liabilities in respect of policyholders for which either sufficient information is unavailable to carry out the above analysis or, which have not yet been identified.

Health hazard liabilities are estimated using similar principles to the above, in that the liabilities of the policyholder are estimated for the majority of reserves and then applied to the insurance coverage.

These evaluation techniques involve a number of important assumptions, including:

- The validity and quantum of the claims potentially faced by the policyholder.
- The legal interpretation of insurance policies and the outcome of litigation, based upon legal advice received.
- The degree to which potential or unforeseen health hazards may have an effect on the liabilities.

REINSURANCE RECOVERIES

The run-off and reinsurance contract that ERL and its subsidiary undertaking, Equitas Limited, have entered into with National Indemnity Company (NICO), as described in note 26, provides substantial additional cover for Equitas and therefore Lioncover. Despite significant uncertainties regarding the determination of the ultimate cost of claims borne by ERL, the likelihood that ERL will not be able to pay claims in full has been considerably reduced by this transaction.

OTHER INSURANCE ACTIVITIES

Other insurance activities represent those of Centrewrite Limited and Lloyd's Reinsurance Company (China) Limited.

Centrewrite Limited's principal activities in 2007 were to underwrite the Lloyd's Members' Estate Protection Plan and to reinsure individual members of Lloyd's participations on syndicates for underwriting years of account which have not been closed.

Lloyd's Reinsurance Company (China) Limited (LRCCL) is a wholly owned subsidiary undertaking of the Society of Lloyd's. The company's principal activity is the reinsurance of non-life business in the China insurance market. Lloyd's syndicates participate in LRCCL by means of retrocession agreements which allow a 100% risk transfer. LRCCL retains 5% of premiums to offset against operating costs.

The insurance contract liabilities may be analysed as follows:

	2007 Insurance contract liabilities £000	2006 Insurance contract liabilities £000
Provision for claims reported	**14,149**	14,076
Provision for IBNR claims	**170**	72
Insurance contract liabilities	**14,319**	14,148

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

13. INSURANCE ACTIVITIES CONTINUED

OTHER INSURANCE ACTIVITIES CONTINUED

The movement in provision for insurance contract liabilities can be analysed as follows:

	2007 Insurance contract liabilities £000	2006 Insurance contract liabilities £000
At 1 January	**14,148**	16,424
Claims incurred/(released)	**1,235**	(1,517)
Claims paid	**(1,064)**	(759)
At 31 December	**14,319**	14,148

Claims incurred consist of claims and claims handling expenses paid during the year, together with the movement in outstanding claims. Full provision is made, on the basis of available information, for the estimated ultimate cost of claims notified but not settled as at the date of the balance sheet, after taking into account handling costs and settlement trends. A provision for claims incurred but not notified is also established as at that date on a statistical basis. The provision also reflects claims settlement expenses and anticipated reinsurance and other recoveries. The provision for outstanding claims is based on information available at the balance sheet date. Subsequent information and events may result in the ultimate liability being less than, or greater than, the amount provided. Any difference between the provision and subsequent settlements are dealt with in the group income statements of later years.

CLAIMS DEVELOPMENT TRIANGLES

The tables below show the development of claims over a period of time on a gross basis.

The tables show the cumulative incurred claims, including both notified and IBNR claims for each successive year at balance sheet date, together with cumulative claims at the current balance sheet date.

LIONCOVER INSURANCE COMPANY LIMITED

	2003 and prior £000	2004 £000	2005 £000	2006 £000	**2007 £000**	**Total £000**
At end of underwriting year	840,945	–	–	–	**–**	
One year later	848,850	–	–	–	**–**	
Two years later	942,492	–	–	–	**–**	
Three years later	934,311	–	–	–	**–**	
Four years later	910,938	–	–	–	**–**	
Current estimate of cumulative claims	910,938	–	–	–	**–**	
Cumulative payments to date	(523,498)	–	–	–	**–**	
Insurance contract liabilities	387,440	–	–	–	**–**	**387,440**

The impact of exchange rate movements has decreased the claims provision by £6.2m (2006: increase in claims provision of £65.2m). This is represented in the movement in claims in the table above.

OTHER INSURANCE ACTIVITIES

	2003 and prior £000	2004 £000	2005 £000	2006 £000	**2007 £000**	**Total £000**
At end of underwriting year	105,208	4,101	3,407	2,647	**2,384**	
One year later	75,439	3,621	3,001	2,337		
Two years later	66,791	3,211	2,940			
Three years later	33,409	3,329				
Four years later	27,420					
Current estimate of cumulative claims	27,420	3,329	2,940	2,337	**2,384**	
Cumulative payments to date	(22,139)	(705)	(537)	(507)	**(203)**	
Insurance contract liabilities	5,281	2,624	2,403	1,830	**2,181**	**14,319**

14. LOANS RECOVERABLE

	2007 £000	2006 £000
At 1 January	**62,201**	61,609
Recoveries during the year	**(1,873)**	(3,431)
Change in valuation	**1,498**	4,023
At 31 December	**61,826**	62,201

None of the change in valuation of loans recoverable during 2007 or 2006 relates to changes in credit risk.

15. FINANCIAL INVESTMENTS

	2007 £000	2006 £000
Statutory insurance deposits (note 15A)	**108,615**	126,742
Other investments (note 15B)	**1,872,861**	1,371,601
	1,981,476	1,498,343

A. STATUTORY INSURANCE DEPOSITS

	2007 Securities £000	2007 Deposits £000	2007 Total £000	2006 Total £000
Market value at 1 January	**47,819**	**78,923**	**126,742**	121,484
Additions at cost	**10,100**	**206,324**	**216,424**	322,292
Disposal proceeds	**(20,279)**	**(217,605)**	**(237,884)**	(306,712)
Surplus/(deficit) on the sale and revaluation of investments	**1,630**	**1,703**	**3,333**	(10,322)
Market value at 31 December	**39,270**	**69,345**	**108,615**	126,742

Analysis of securities at year end:	2007 Cost £000	2007 Valuation £000	2006 Cost £000	2006 Valuation £000
Government	**16,860**	**16,934**	21,010	19,663
Corporate securities (see below)	**22,778**	**22,336**	30,132	28,156
Market value at 31 December	**39,638**	**39,270**	51,142	47,819

Analysis of corporate securities:

AAA	**20,011**	24,549
AA	**2,325**	3,607
	22,336	28,156

Finance is arranged by advances from syndicates in the Lloyd's market. These advances are renewed annually. By agreement with the lenders, investment returns earned on these assets are paid, in appropriate proportions, to the lenders. In this way, the Society avoids any risk arising from a mismatch between borrowing and lending terms.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED
as at 31 December 2007

15. FINANCIAL INVESTMENTS CONTINUED

The provision of funds by members is in respect of the establishment and maintenance of overseas deposits and is a condition of permission to underwrite insurance business at Lloyd's.

B. OTHER INVESTMENTS

	2007 Corporation of Lloyd's £000	2007 Lloyd's Central Fund £000	2007 Insurance activities £000	2007 Total £000	2006 Total £000
Market value at 1 January	37,589	1,291,624	42,388	1,371,601	1,031,662
Additions at cost	–	1,850,740	44,727	1,895,467	627,903
Increase in short-term deposits	21,842	96,429	2,798	121,069	113,378
Disposal proceeds	–	(1,513,550)	(41,090)	(1,554,640)	(364,180)
Surplus/(deficit) on the sale and revaluation of investments	39	38,594	731	39,364	(37,162)
Market value at 31 December	59,470	1,763,837	49,554	1,872,861	1,371,601

Analysis of securities at year end:	2007 Corporation of Lloyd's £000	2007 Lloyd's Central Fund £000	2007 Insurance activities £000	2007 Total £000	2006 Total £000
Fixed interest:-					
Government	–	1,015,838	37,002	1,052,840	668,632
Corporate securities (see below)	–	249,355	9,754	259,109	274,938
Emerging markets	–	17,491	–	17,491	–
High yield	–	19,101	–	19,101	–
	–	1,301,785	46,756	1,348,541	943,570
Equities:-					
Global	–	185,949	–	185,949	295,956
Emerging markets	–	18,656	–	18,656	–
	–	204,605	–	204,605	295,956
Hedge funds	–	65,162	–	65,162	–
Short-term deposits	59,470	171,285	2,798	233,553	111,075
Security deposits (see below)	–	21,000	–	21,000	21,000
Market value at 31 December	59,470	1,763,837	49,554	1,872,861	1,371,601

Analysis of corporate securities:	2007 Corporation of Lloyd's £000	2007 Lloyd's Central Fund £000	2007 Insurance activities £000	2007 Total £000	2006 Total £000
AAA	–	89,480	6,401	95,881	92,790
AA	–	80,495	3,353	83,848	105,420
A	–	79,380	–	79,380	76,728
	–	249,355	9,754	259,109	274,938

SECURITY DEPOSITS

Tutelle Limited

In 1996 the Council set aside, under a Lloyd's special account, £20m of the 'Old' Central Fund to secure the Society's obligations under staff indemnities and certain indemnities which have been given by Lloyd's to certain individuals and advisers in respect of the 'Reconstruction and Renewal' plan. These include members of the Reserve Group, directors and officers of Equitas, members of the Council, Lloyd's Regulatory Board, Lloyd's Market Board (the latter two boards ceased during 2002) and of their respective sub-committees and Corporation staff.

Unless and until there is any default under the security documentation, interest earned on the trust fund is paid to the 'Old' Central Fund. The security was deposited for an initial period of two years and the Council exercised its discretion to renew this in June 1998. The Council further amended the period of the deposit, in November 1998, so that the security could only be released if the Council was satisfied that there was no reasonable prospect of a claim being made under these indemnities. Tutelle's position is under biennial review and, having been reviewed in June 2006, will be reviewed again in June 2008. The security may continue for a period of up to 80 years. Any of the funds remaining after this period will be repaid to the 'Old' Central Fund.

15. FINANCIAL INVESTMENTS CONTINUED

Lioncover Insurance Company Limited

In 1999, the Society assigned to Lioncover £1m of the 'Old' Central Fund by way of security for a period of ten years for its obligations to Lioncover under the indemnity bond referred to in note 25B. The security was provided as consideration to those private members whose underwriting liabilities are reinsured by Lioncover for the release of Lloyd's syndicate 9001, for which Lioncover was substituted as direct reinsurer to close of those members. Any of the funds remaining after this period will be repaid to the 'Old' Central Fund.

Unless and until there is any default under the security documentation, interest earned on the security is paid to the 'Old' Central Fund.

16. CASH AND CASH EQUIVALENTS

	2007 £000	2006 £000
Cash at banks	**30,274**	30,521
Short-term deposits	**151,415**	179,777
	181,689	210,298

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods of between one day and three months, depending on the immediate cash requirements of the Society, and earn interest at the respective short-term deposit rates. The fair value of cash and cash equivalents is £181.7m (2006: £210.3m).

17. SUBORDINATED NOTES AND PERPETUAL SUBORDINATED CAPITAL SECURITIES

	2007 £000	2006 £000
Details of loans payable wholly or partly after more than five years:		
6.875% subordinated notes of £300m maturing 17 November 2025	**300,000**	300,000
5.625% subordinated notes of €300m maturing 17 November 2024	**220,345**	202,129
7.421% perpetual subordinated capital securities of £500m redeemable on 21 June 2017	**500,000**	–
	1,020,345	502,129
Less: issue costs to be charged in future years	**(6,980)**	(2,996)
Less: discount on issue to be unwound in future years	**(1,611)**	(1,759)
	1,011,754	497,374

SUBORDINATED DEBT ISSUED IN 2004

The Sterling Notes mature on 17 November 2025, although the Society may redeem them on 17 November 2015 and 17 November 2020. In the event that the Society does not redeem the Sterling Notes on 17 November 2015, the rate of interest payable will be the rate per annum which is the aggregate of the Gross Redemption Yield on the relevant Benchmark Gilt (a UK government security having a maturity date on or nearest to the next reset date) plus a margin of 3.07%.

The Euro Notes mature on 17 November 2024, although the Society may redeem them on 17 November 2014 or on any interest payment date thereafter. In the event that the Society does not redeem the Euro Notes on 17 November 2014, the rate of interest payable will be three month Euribor plus a margin of 2.72%.

The Notes are subordinated obligations of the Society. Each tranche of the Notes will rank *pari passu* with the other in a winding-up of the Society. Upon the occurrence of any winding-up proceedings of the Society, payments on the Notes will be subordinated in right of payment to the prior payment in full of all other liabilities of the Society, except for liabilities which rank equally with or junior to the Notes. Payments on the Notes will also be subordinated to certain payments which may be made out of central assets including payments made to discharge the liabilities of an insolvent member to any person (including any policyholders) arising out of or, in connection with insurance business carried on at Lloyd's by that insolvent member and payments made in respect of the costs required by or under any insolvency procedure to which the Society or the Lloyd's market may be subject. However, in the event of a winding-up of the Society, the claims of the holders of the Notes rank senior to the distribution of any central assets to members of Lloyd's generally (other than payments made to members in their capacity as senior creditors of the Society).

Welcome to Lloyd's
Strategic review
Performance
Delivering value
Market results
Society report

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

17. SUBORDINATED NOTES AND PERPETUAL SUBORDINATED CAPITAL SECURITIES CONTINUED

SUBORDINATED DEBT ISSUED IN 2007

The perpetual subordinated capital securities ('capital securities') are perpetual securities and have no fixed redemption date. However, they are redeemable in whole on 21 June 2017 at the option of the Society or on any interest payment date thereafter provided certain conditions have been met by the Society. The capital securities bear interest at a rate of 7.421% per annum until 20 June 2017, payable annually in arrears on 21 June in each year, and thereafter at a rate per annum reset semi-annually of 2.41% per annum above the London interbank offered rate for six-month sterling deposits, payable semi-annually in arrear on the interest payment dates falling on 21 June and 21 December in each year.

The capital securities are subordinated obligations of the Society. Upon the occurrence of any winding-up proceedings of the Society, the claims of the holders of the capital securities will rank junior to all other claims of creditors of the Society (including any creditor who is the holder of any of the Sterling or Euro Notes issued by the Society in 2004) except for those creditors having claims which rank equally with or junior to the claims of the holders of the capital securities. The claims of the holders of the capital securities will also rank junior to any payments made to discharge the liabilities of a member in connection with insurance business carried on at Lloyd's by that member and also to the claims of any person in respect of whom a New Central Fund undertaking has been made. However, in the event of a winding-up of the Society, the claims of the holders of the capital securities rank senior to the distribution of any central assets to members of Lloyd's generally (other than payments made to members in their capacity as senior creditors of the Society).

18. PENSION SCHEMES

The Society operates a number of defined benefit and defined contribution pension schemes. The principal scheme is the Lloyd's Pension Scheme which is a defined benefit scheme. Other schemes have been established for certain employees based overseas. These schemes are generally funded by the payment of contributions to separately administered funds.

DEFINED BENEFIT PLANS

The pension assets/(liabilities) of the schemes at 31 December 2007 are as follows:

	2007 £000	2006 £000
Lloyd's Pension Scheme	**16,500**	(45,113)
Overseas pension schemes	**(667)**	(663)

The amounts charged to the group income statement and group statement of recognised income and expense, in respect of defined benefit plans are as follows:

	2007 £000	2006 £000
Group income statement:		
Lloyd's Pension Scheme	**17,833**	10,524
Overseas pension schemes	**224**	77
	18,057	10,601
Group statement of recognised income and expense:		
Lloyd's Pension Scheme	**52,452**	(1,613)
Overseas pension schemes	**–**	(254)
	52,452	(1,867)

Lloyd's Pension Scheme

The Lloyd's Pension Scheme is a defined benefit pension scheme with assets held in a separately administered fund. For the purposes of determining the funding position of the scheme and future contributions, a formal actuarial valuation of the scheme was carried out by Watson Wyatt Limited, actuaries and consultants, as at 30 June 2007 using the projected unit credit method. The principal actuarial assumptions adopted in the valuation were:

- Assumed future price inflation of 3.4% per annum.
- Pensions would increase in payment at 3.4% per annum (relating to benefits accrued between 6 April 1997 and 5 April 2005) or 2.5% per annum (benefits accrued post 5 April 2005).
- Total pensionable remuneration would increase by 5.2% per annum.
- The rate of return on investments held at the valuation date and on future contributions receivable after the valuation date was assumed to be 6.8% per annum for periods before benefits come into payment and 5.4% per annum for periods after benefits come into payment.
- Mortality assumptions were based on the '00' series of tables published by the actuarial profession with improvements projected to 2007. From 2007, medium cohort improvements are assumed, subject to a minimum improvement of 1.0% per annum.

18. PENSION SCHEMES CONTINUED

The total market value of the scheme's assets at the date of valuation were £391m, which equates to 100% of the value placed on the benefits that had accrued to members, after allowing for assumed future increases in pensionable remuneration. These figures exclude both liabilities and the related assets in respect of money purchase AVCs.

No allowance has been made for discretionary increases to pre 6 April 1997 benefits when in payment. In 2003, the Society instructed Watson Wyatt Limited not to allow for such increases in calculating the scheme's liabilities for future actuarial valuations. Such increases have always been payable at the discretion of the Society and will continue to be considered on the basis of affordability, but are not taken into account by the actuary in determining the funding level.

In recent years, in order to mitigate exposure to pension scheme liabilities several changes have been made to the Lloyd's Pension Scheme. From February 2005 the senior management section of the scheme was closed to new entrants and the normal retirement age for joiners was increased from 60 to 65. The final salary scheme was closed to new joiners at the end of June 2006. New entrants from July 2006 have been eligible to join the Lloyd's Pension Scheme but accrue benefits on an 80ths career average basis and are contracted-in to the State Second Pension. Employee contributions at 5%, or 10% for members of the senior management section, of pensionable earnings up to the Scheme earnings cap where applicable, normally payable by salary sacrifice, have been introduced from July 2006. Following the 2007 actuarial valuation employer contributions as a percentage of basic salaries are 21.8% for pre-February 2005 final salary members, 12% for post-January 2005 entrants and 6.2% for members accruing benefits on a career average basis.

PRINCIPAL ACTUARIAL ASSUMPTIONS IN RESPECT OF IAS 19

The demographic assumptions which are the most financially significant are those relating to the longevity of retired members. The assumptions for the purposes of the IAS 19 valuation as at 31 December 2007 are as applied in the triennial actuarial valuation as at 30 June 2007.

These assumptions are equivalent to expected longevity at age 60 approximately as follows:

- For pensioners currently aged 60: ranging from 25 years to 29 years (2006: 27 years to 29 years).
- For non-pensioners currently aged 45: ranging from 27 years to 30 years (2006: 28 years to 30 years).

The other major financial assumptions used by the actuary as at 31 December 2007 for the purposes of IAS 19 were:

	2007 % per annum	2006 % per annum	2005 % per annum	2004 % per annum
General salary and wage inflation	**5.20%**	4.80%	4.60%	4.60%
Rate of increase in pensions in payment				
– pre 6 April 1997 (in excess of GMPs)	**–**	–	–	–
– 6 April 1997 to 5 April 2005	**3.40%**	3.00%	2.80%	2.80%
– post 5 April 2005	**2.50%**	2.50%	2.80%	n/a
Increases to deferred pensions	**3.40%**	3.00%	2.80%	2.80%
Discount rate	**5.90%**	5.10%	4.80%	5.40%
Price inflation	**3.40%**	3.00%	2.80%	2.80%
Expected rate of return – Bonds	**5.20%**	4.70%	4.40%	5.00%
– Equities	**8.10%**	7.80%	7.90%	8.20%
– Cash and net current assets	**5.30%**	4.90%	3.80%	3.60%

An allowance is made for members commuting 20% (2006: 20%) of their pension on retirement.

The expected rate of return on assets is determined based on market prices prevailing on that date, applicable to the period over which the obligation is to be settled.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

18. PENSION SCHEMES CONTINUED

SENSITIVITY OF PENSION OBLIGATION TO CHANGES IN ASSUMPTIONS

The actuarial valuation of liabilities under IAS 19 is particularly sensitive to changes in market conditions, which determine the rate at which pension liabilities are discounted.

A change of 0.1% pa in the discount rate as at 31 December 2007 would result in a change to the pension liabilities at that date of around 2%, or approximately £8m.

A change in the mortality assumptions could have a significant impact on the pension liability. For instance, if the allowance for future improvements were amended to incorporate the 'long cohort', this would add up to another two years to expected future longevity (in addition to that based on the medium cohort). This could increase the pension liabilities by a further 3%.

Amounts for the current and previous years were:

Asset analysis of the scheme	**2007 Fair value £000**	2006 Fair value £000	2005 Fair value £000	2004 Fair value £000
Bonds	**162,611**	135,839	126,363	104,686
Equities	**238,734**	215,386	193,226	162,835
Cash and net current assets	**22,569**	437	203	235
Total market value of assets	**423,914**	351,662	319,792	267,756
Actuarial value of scheme liabilities	**(407,414)**	(396,775)	(372,001)	(321,456)
Surplus/(deficit) in the scheme	**16,500**	(45,113)	(52,209)	(53,700)

Changes in the present value of the defined benefit obligation are:

	2007 £000	2006 £000
Actuarial value of scheme liabilities at 1 January	**396,775**	372,001
Interest cost on pension scheme liabilities	**20,616**	17,525
Current service cost (net of employee contributions)	**6,823**	8,667
Past service cost	**14,400**	4,860
Employee contributions	**1,946**	1,326
Benefits paid	**(16,738)**	(16,643)
Experience losses arising in scheme liabilities	**12,070**	6,509
Change in assumptions underlying the present value of the scheme liabilities	**(58,778)**	2,530
LPSO Limited and other companies (see below)	**30,300**	–
Actuarial value of scheme liabilities at 31 December	**407,414**	396,775

Changes in the fair value of plan assets are:

	2007 £000	2006 £000
Fair value of scheme assets at 1 January	**351,662**	319,792
Expected return on pension scheme assets	**23,896**	20,528
Employer contributions – normal	**4,094**	4,933
– special	**22,900**	14,300
Employee contributions	**1,946**	1,326
Benefits paid	**(16,738)**	(16,643)
Actuarial gain on scheme assets	**5,744**	7,426
LPSO Limited and other companies (see below)	**30,410**	–
Fair value of scheme assets at 31 December	**423,914**	351,662

The valuation as at 31 December 2006 excluded both liabilities and the related assets in respect of the accrued benefits of scheme members employed by LPSO Limited, LCO Marine Limited and LCO Non-Marine and Aviation Limited which ceased to be subsidiary undertakings in 2001. Following negotiations with these companies during 2007, their participation in the scheme ceased with effect from 30 June 2007. Active members were granted deferred pensions in the scheme based on their accrued entitlements. For the purpose of the valuation as at 31 December 2007, the entirety of the scheme assets have therefore been taken into account, the residual deferred liabilities in respect of the former members are now entirely attributable to the Society. The net impact of the cessation of participation is shown as an increase in the assets attributable to the Society of £30.4m, offset by an increase in liabilities of £30.3m, a net gain of £0.1m.

18. PENSION SCHEMES CONTINUED

Under the participation terms, any debt payable on cessation became a liability of the Society. As a result the Society paid £8.6m to the scheme in respect of the resulting debt attributable to LPSO Limited, LCO Marine Limited and LCO Non-Marine and Aviation Limited under section 75 of the Pensions Act 1995.

The Society expects to contribute approximately £5.0m in normal contributions to the pension scheme in 2008.

ANALYSIS OF THE AMOUNT RECOGNISED IN THE GROUP STATEMENT OF RECOGNISED INCOME AND EXPENSE (SORIE)

	2007 £000	2006 £000
Actual return on pension scheme assets	**29,640**	27,954
Less expected return on pension scheme assets	**(23,896)**	(20,528)
Actual return less expected return on pension scheme assets	**5,744**	7,426
Experience losses arising on scheme liabilities	**(12,070)**	(6,509)
Changes in the assumptions underlying the present value of the scheme liabilities	**58,778**	(2,530)
Actuarial gain/(loss) recognised in the SORIE	**52,452**	(1,613)

The cumulative actuarial gain recognised in the group statement of recognised income and expense since 1 January 2004 is £47.4m (2006: £5.1m actuarial loss).

ANALYSIS OF THE AMOUNT CHARGED TO THE GROUP INCOME STATEMENT (RECOGNISED IN OTHER GROUP OPERATING EXPENSES)

	2007 £000	2006 £000
Current service cost	**6,823**	8,667
Past service cost	**14,400**	4,860
Expected return on pension scheme assets	**(23,896)**	(20,528)
Interest on pension scheme liabilities	**20,616**	17,525
Settlement/curtailment	**(110)**	–
Total operating charge	**17,833**	10,524

The Society recognises the cost of discretionary increases to pre 6 April 1997 benefits in payment when there is a constructive liability to make such increases. Past service costs of £14.4m represent the costs of an increase for 2008 of £4.4m and a further £10.0m to meet future discretionary increases which was paid to the scheme in December 2007. The £10.0m has been notionally segregated from the scheme's other assets (the 'notional fund') and its investment performance will be tracked on the assumption that it is invested in the same way as the scheme's other assets. The notional fund will be used to facilitate the award of future discretionary pension increases when the Society carries out its annual review of pensions in accordance with the Scheme's Definitive Trust Deed. As long as there is a notional fund set aside for this purpose, discretionary increases will continue to be made.

The measurement bases set by IAS 19 are likely to give rise to significant fluctuations to the scheme's assets and liabilities. However, this may not necessarily require changes to the contribution rate, as recommended by the independent actuary, which is based on expected long-term rates of return.

HISTORY OF EXPERIENCE GAINS AND LOSSES

	2007 £000	2006 £000	2005 £000	2004 £000
Difference between the expected and actual return on scheme assets:				
amount	**5,744**	7,426	31,904	10,312
percentage of scheme assets	**1.4%**	2.1%	10.0%	3.9%
Experience (losses)/gains on scheme liabilities:				
amount	**(12,070)**	(6,509)	606	44
percentage of the present value of the scheme liabilities	**(3.0%)**	(1.6%)	0.2%	0.0%
Total amount recognised in the SORIE:				
amount	**52,452**	(1,613)	(2,354)	(1,100)
percentage of the present value of the scheme liabilities	**12.9%**	(0.4%)	(0.6%)	(0.3%)

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

18. PENSION SCHEMES CONTINUED

Overseas pension schemes

The Society operates a number of defined benefit plans for qualifying employees based overseas. The actuarial valuations of these pension liabilities at 31 December 2007 were £0.7m (2006: £0.7m). The total expense recognised in other operating expenses of £0.3m (2006: £0.1m) represents the related current service cost of these schemes. No actuarial gain or loss (2006: loss £0.3m) has been recognised in the group statement of recognised income and expense.

Defined contribution plans

The Society operates a number of defined contribution retirement benefit plans for qualifying employees based overseas. The assets of the plans are held separately from those of the Society in funds under the control of the trustees.

In some countries, employees are members of state-managed retirement benefit plans. The Society is required to contribute a specified percentage of payroll costs to fund these benefits. The only obligation of the Society with respect to the retirement benefit plan is to make the specified contributions.

The total expense recognised in the group income statement of £0.5m (2006: £0.2m) represents contributions payable to these plans by the Society at rates specified in the rules of these plans.

19. PROVISIONS

	2007 Undertakings given to insolvent members £000	2007 Limited Financial Assistance Agreements £000	2007 Income support schemes £000	2007 Long-term incentive plan £000	2007 Other £000	2007 Total £000	2006 Total £000
Balance at 1 January	**153,419**	**4,619**	**1,635**	**2,130**	**357**	**162,160**	183,118
Charged/(credited) to the group income statement	**(14,828)**	**2,287**	**2,029**	**982**	**–**	**(9,530)**	122,684
Decrease in value of supporting commitments	**(6,057)**	**–**	**–**	**–**	**–**	**(6,057)**	(5,128)
Utilised in the year	**(9,348)**	**(1,174)**	**(1,923)**	**(1,902)**	**–**	**(14,347)**	(138,514)
Balance at 31 December	**123,186**	**5,732**	**1,741**	**1,210**	**357**	**132,226**	162,160

PROVISION FOR UNDERTAKINGS GIVEN TO INSOLVENT MEMBERS

The Council has given undertakings with financial limits to certain corporate members to use the New Central Fund to discharge the liability of those members where they have unpaid cash calls and do not have the resources to meet those cash calls. The purpose of these undertakings is primarily to allow valid claims made on policies underwritten by those insolvent members to continue to be paid in full. For those corporate members in provisional liquidation, the Council has also provided a supporting commitment, which will ensure that in no circumstance will an insurance creditor receive less than the amount it would have received in a winding-up commencing on the date of the provisional liquidation.

19. PROVISIONS CONTINUED

	2007 £000	2007 £000	2006 £000	2006 £000
Provisions for amounts payable at 1 January		**147,362**		163,885
Undertakings (released)/given in the year		**(14,828)**		114,576
Analysis of paid undertaking by members:				
Blodget and Hazard Limited	**–**		(3,662)	
Cotesworth Capital Ltd	**–**		(17,500)	
Crowe Corporate Capital Limited	**(1,564)**		(2,043)	
Crowe Dedicated Limited	**(2,904)**		–	
Dreason Underwriting Limited	**(92)**		(217)	
Euclidian (No 6) Ltd	**(1,673)**		–	
Grenville Underwriting I/II/III Limited	**–**		(624)	
Kite Dedicated Capital Limited (formerly Goshawk Dedicated (No 2) Limited)	**–**		(69,665)	
Margent Capital Management	**(767)**		–	
Shrewsbury Underwriting Capital (Bermuda) Limited and Shrewsbury Underwriting Capital Limited	**–**		(29,871)	
Riverside Corporate Underwriters	**(225)**		(4,500)	
SOC Corporate Member No.1 Limited	**(945)**		(1,419)	
SOC Corporate Member No.3 Limited	**(783)**		–	
Winford Company Limited	**(27)**		(133)	
Other corporate members	**(368)**		(1,465)	
Paid during the year		**(9,348)**		(131,099)
Provisions for amounts payable at 31 December		**123,186**		147,362
Supporting commitments at 31 December		**–**		6,057
Undertakings given to insolvent members at 31 December		**123,186**		153,419

The aggregate amount of all undertakings (excluding the supporting commitments) given by the Council at 31 December 2007 was £1.2bn of which £1.1bn had been paid by that date.

LIMITED FINANCIAL ASSISTANCE AGREEMENTS (LFAA)

The first LFAA were provided to private members in 2005, to meet their outstanding underwriting liabilities. Further LFAA's have been provided in 2007. Assistance is provided to individuals who are reliant on their Funds at Lloyd's (FAL) either because it is in the form of a bank guarantee secured on their sole residence or because they are reliant on the income generated by their FAL. All costs are funded by the New Central Fund.

INCOME SUPPORT SCHEMES

HARDSHIP INCOME TOP-UP SCHEME

The Hardship Scheme was created in 1989 to assist private members who had reduced means as a result of high underwriting losses. Members in the Scheme are eligible to receive ex-gratia top-up income payments from Lloyd's by virtue of having a Hardship Trust Fund (HTF) or having been awarded litigation recoveries used in 'Reconstruction and Renewal' to pay Equitas premiums. The Hardship Scheme is permanent and non-discretionary, but the granting of Hardship Income Top-up payments is at Lloyd's discretion. All costs are currently funded by the 'Old' Central Fund.

INCOME AND HOUSING SUPPORT SCHEME (IHSS SCHEME)

The IHSS Scheme was established in 1996 to provide financial assistance to private members who accepted the 'Reconstruction and Renewal' Settlement offer, to ensure that their housing and income requirements were maintained at a reasonable level. The payments under the scheme are discretionary and are currently funded by the 'Old' Central Fund.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

19. PROVISIONS CONTINUED

LONG-TERM INCENTIVE PLAN (LTIP)

The Society operates a Long-term Incentive Plan for executive directors and senior employees that is related to the results of the Lloyd's market. Details of the plan, and changes effective from 1 January 2008 following the introduction of the Lloyd's Performance Plan, are outlined in the report of the Nominations, Appointments and Compensation Committee on pages 94 to 96. The provision, including employers' National Insurance, for estimated contribution amounts due in respect of the plan is as follows:

	2007 Balance at 1 January £000	2007 (Credited)/ charged in the year £000	2007 Paid in the year £000	2007 Balance at 31 December £000
2004 LTIP	**1,572**	**(216)**	**(1,356)**	**–**
2005 LTIP	**168**	**166**	**(167)**	**167**
2006 LTIP	**390**	**291**	**(324)**	**357**
2007 LTIP	**–**	**686**	**–**	**686**
Total provisions	**2,130**	**927**	**(1,847)**	**1,210**

Included within the charge for the year are National Insurance contributions of £0.1m (2006: £0.2m).

Payments are made over three years commencing in the year following the underwriting year. One-third of the amounts payable are discretionary and based on performance.

OTHER PROVISIONS

Other provisions include amounts provided for obligations arising from the sale of LPSO Limited during 2001 of £0.4m.

20. TRADE AND OTHER PAYABLES

	2007 £000	2006 £000
Due within one year:		
Trade and other creditors	**21,969**	21,974
Taxation and social security	**1,714**	1,777
Arbitration awards	**2,543**	2,710
Contribution to Equitas – Berkshire Hathaway transaction	**18,000**	–
Interest payable on subordinated loan notes and perpetual capital security	**23,793**	3,945
	68,019	30,406

21. FINANCIAL INSTRUMENTS

An explanation of the Society's financial instrument risk management objectives, policies and strategies are set out in the discussion of the Society's financial risk management and treasury policies on pages 110 and 111 of the Financial Review.

FAIR VALUES AND CREDIT RISK

The methods and assumptions used in estimating the fair value of financial instruments are detailed in note 2F on pages 118 and 119.

The fair value of subordinated debt is £1,031.3m (2006: £525.3m) against a carrying value measured at amortised cost of £1,011.8m (2006: £497.4m). All other financial instruments are either held at fair value or at an amount that approximates to fair value.

At the balance sheet date there were no significant concentrations of credit risk. The maximum exposure to credit risk is represented by the carrying value of each financial asset, including derivative financial instruments, in the group balance sheet.

21. FINANCIAL INSTRUMENTS CONTINUED

IMPAIRMENT LOSSES

Trade receivables

The ageing of trade receivables as at 31 December 2007 was as follows:

	2007 Gross £000	2007 Impairment £000	2007 Net £000	2006 Gross £000	2006 Impairment £000	2006 Net £000
Not past due	**16,584**	**–**	**16,584**	2,071	–	2,071
Past due 31–60 days	**73**	**–**	**73**	121	–	121
Past due 61–90 days	**101**	**–**	**101**	9	–	9
Past due 91–120 days	**48**	**(4)**	**44**	121	–	121
More than 120 days	**1,597**	**(1,581)**	**16**	1,712	(1,687)	25
Total	**18,403**	**(1,585)**	**16,818**	4,034	(1,687)	2,347

Receivables of more than 120 days represent amounts due from members no longer underwriting in respect of Society charges.

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

	2007 £000	2006 £000
Balance at 1 January	**1,687**	1,826
Additional allowances during the year charged to the group income statement	**73**	228
Allowances released during the year credited to the group income statement	**(146)**	(279)
Recoveries during the year	**(29)**	(88)
Balance at 31 December	**1,585**	1,687

SENSITIVITY ANALYSIS

Foreign currency exposure

Currency risk is the risk that the sterling value of the Society's assets and liabilities will fluctuate due to changes in foreign exchange rates. As at 31 December 2007, the sensitivity of the Society's surplus before tax, to a 5% reduction in the value of the US dollar and the Euro relative to sterling is approximately a loss of £2m and £1m, respectively. This analysis assumes that all other variables, in particular interest rates, remain constant. In practice the actual results may differ.

Debt securities sensitivities

The value of the Society's investments in debt securities is affected by changes in the level of yields, as determined by financial markets. As at 31 December 2007 a consistent increase of 100 basis points in the yields applicable to all relevant securities would have reduced the surplus before tax by approximately £80m. This analysis assumes that all other variables, in particular foreign currency exchange rates, remain constant. In practice the actual results may differ.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

21. FINANCIAL INSTRUMENTS CONTINUED

Equity price risk

Equity price risk is the risk that the market values of equity investments fall. At 31 December 2007, a 15% fall in the value of all of the Society's equity investments would have reduced the surplus before tax by approximately £30m. This analysis assumes that all other variables, in particular foreign currency exchange rates, remain constant. In practice the actual results may differ.

LIQUIDITY RISK

The table below summarises the maturity profile of the Society's financial liabilities as at 31 December 2007 based on undiscounted contractual cash flows:

As at 31 December 2007	**Carrying amount £000**	**Contractual cash flows £000**	**Within 1 year £000**	**1–2 years £000**	**2–5 years £000**	**More than 5 years £000**
Subordinated loan notes	**516,009**	**(772,105)**	**(33,019)**	**(33,019)**	**(99,058)**	**(607,009)**
Perpetual subordinated capital securities	**495,745**	**(871,050)**	**(37,105)**	**(37,105)**	**(111,315)**	**(685,525)**
Loans funding statutory insurance deposits	**101,562**	**(101,562)**	**(101,562)**	**–**	**–**	**–**
Trade and other payables	**68,019**	**(68,019)**	**(68,019)**	**–**	**–**	**–**
	1,181,355	**(1,812,736)**	**(239,705)**	**(70,124)**	**(210,373)**	**(1,292,534)**

As at 31 December 2006	Carrying amount £000	Contractual cash flows £000	Within 1 year £000	1–2 years £000	2–5 years £000	More than 5 years £000
Subordinated loan notes	497,374	(778,712)	(31,995)	(31,995)	(95,984)	(618,738)
Loans funding statutory insurance deposits	120,812	(120,812)	(120,812)	–	–	–
Trade and other payables	30,406	(30,406)	(30,406)	–	–	–
	648,592	(929,930)	(183,213)	(31,995)	(95,984)	(618,738)

DERIVATIVE FINANCIAL INSTRUMENTS

The Society enters into forward currency contracts to manage exposures to fluctuation of exchange rates and to provide a service to the Lloyd's market.

Analysis of forward currency contracts:	**2007 £000**	2006 £000
Outstanding forward foreign exchange gains	**9,440**	3,500
Outstanding forward foreign exchange losses	**(20,760)**	(2,710)

The fair value and their notional amounts of forward currency contracts, all of which mature within one year, are analysed as follows:

	2007	**2007**	**2007**	**2007**
	Assets		**Liabilities**	
As at 31 December 2007	**Fair value £000**	**Notional £000**	**Fair value £000**	**Notional £000**
Currency Conversion Service (CCS)	**2,282**	**70,132**	**(1,437)**	**(69,287)**
Other forward foreign exchange contracts	**7,158**	**814,604**	**(19,323)**	**(826,769)**
	9,440	**884,736**	**(20,760)**	**(896,056)**

	2006	2006	2006	2006
	Assets		Liabilities	
As at 31 December 2006	Fair value £000	Notional £000	Fair value £000	Notional £000
Currency Conversion Service (CCS)	677	30,280	(839)	(30,442)
Other forward foreign exchange contracts	2,823	406,371	(1,871)	(405,419)
	3,500	436,651	(2,710)	(435,861)

22. RECONCILIATION OF MOVEMENT IN EQUITY

	Accumulated reserve £000	Syndicate loans £000	Revaluation reserve £000	Foreign currency translation reserve £000	Total equity £000
At 1 January 2006	648,008	106,834	9,710	16	764,568
Total recognised income and expense for the year	82,862	–	–	(17)	82,845
Receipt of syndicate loans	–	112,578	–	–	112,578
Payment of syndicate loan interest	(4,365)	–	–	–	(4,365)
Tax on payment of syndicate loan interest	1,310	–	–	–	1,310
Revaluation of syndicate loans	5,852	(5,852)		–	–
At 31 December 2006	733,667	213,560	9,710	(1)	956,936
Total recognised income and expense for the year	**200,342**	**–**	**1,138**	**43**	**201,523**
Receipt of syndicate loans	**–**	**121,107**	**–**	**–**	**121,107**
Repayment of syndicate loans	**–**	**(331,611)**	**–**	**–**	**(331,611)**
Payment of syndicate loan interest	**(13,401)**	**–**	**–**	**–**	**(13,401)**
Tax on payment of syndicate loan interest	**4,020**	**–**	**–**	**–**	**4,020**
Revaluation of syndicate loans	**3,056**	**(3,056)**		**–**	**–**
At 31 December 2007	**927,684**	**–**	**10,848**	**42**	**938,574**

ACCUMULATED RESERVES

	2007 £000	2006 £000
Attributable to:		
Corporation of Lloyd's and non-insurance related subsidiary undertakings	**116,756**	68,941
Central Fund	**768,117**	626,813
Insurance related subsidiary undertakings	**35,307**	33,534
Associates	**7,504**	4,379
	927,684	733,667

SYNDICATE LOANS

Members have been contributing to the Lloyd's Central Fund partly by way of interest-bearing loans from syndicate premiums trust funds (the syndicate loans). The syndicate loans paid interest annually at a rate equal to specified market indices which recorded the performance of short-dated fixed interest securities. Council agreed to the repayment of all outstanding loans together with accrued interest on 31 July 2007.

REVALUATION RESERVE

The revaluation reserve is used to record increases in the fair value of the Lloyd's Collection and decreases to the extent that such decreases relate to the amount previously recognised in equity.

FOREIGN CURRENCY TRANSLATION RESERVE

The foreign currency translation reserve is used to record exchange differences arising from the translation of the financial statements of foreign subsidiary undertakings.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

23. COMMITMENTS

A. CAPITAL EXPENDITURE COMMITMENTS

No contractual commitments exist at 31 December 2007 other than those included within financial statements. The same applied at 31 December 2006.

B. OPERATING LEASE COMMITMENTS

	2007 £000	2006 £000
Non-cancellable operating lease rentals are payable as follows:		
Within one year	**19,257**	18,379
After one year but not more than five years	**74,163**	71,616
More than five years	**152,860**	170,619

Commitments outstanding under the terms of the lease for the Lloyd's 1986 building have been included at the current rental value (£16.8m per annum) to the first break of the lease in 2021. The lease was subject to a rent review in March 2006, the next review will be during 2011. The new Lloyd's Chatham building is included at the current rental value (£0.4m per annum) to the first break in the lease in 2016. The lease will be subject to a rent review in 2011.

Subsidiary undertakings are party to a number of small operating leases mainly for property rental and small machinery. The commitments outstanding have been included at the current rental value (£1.2m per annum) to the first break in the lease. These arrangements do not impose any significant restrictions on the Society; renewals are at the option of each entity that holds the lease.

During the year ended 31 December 2007, £19.1m (2006: £18.3m) was recognised as an expense in the group income statement in respect of operating leases.

24. DISCLOSURE OF RELATED PARTY TRANSACTIONS

The group financial statements include the financial statements of the Society and all of its subsidiary undertakings, the Lloyd's Central Fund and the group's interests in its associates as listed in note 11.

Services provided to Ins-sure Holdings Limited group in the year ended 31 December 2007 included operating systems support and development, premises and other administrative services. The total value of the services provided was £615,000 (2006: £1,227,000). In addition, Ins-sure Holdings Limited group have charged the Society £2,680,000 for services provided in the same year (2006: £1,924,000).

At 31 December 2007, there was a balance of £101,000 (2006: £237,000) owing from Ins-sure Holdings Limited group to the Society. The Society owed £nil to Ins-sure Holdings Limited at the same date (2006: £291,000).

Services provided to Xchanging Claims Services Limited group in the year ended 31 December 2007 included premises and other administrative services. The total value of the services provided was £107,000 (2006: £206,000). In addition, Xchanging Claims Services Limited group have charged the Society £nil for services provided in the same year (2006: £nil).

At 31 December 2007, there was a balance of £5,000 (2006: £12,000) owing from Xchanging Claims Services Limited group to the Society. The Society owed £nil (2006: £nil) to Xchanging Claims Services Limited at the same date.

Transactions with associates are priced on an arm's length basis.

A member of Council, Rupert Atkin, is also a Director of Shrewsbury Underwriting Capital (Bermuda) Limited and Shrewsbury Underwriting Capital Limited. These companies benefit from undertakings given by the Council in 2007 to meet unpaid cash calls. No amounts were paid under these undertakings in 2007.

In the normal course of business, the Society may enter into transactions with Lloyd's market businesses in which members of Council and the Franchise Board may have an interest. Such transactions are on an arm's length basis.

25. CONTINGENT LIABILITIES

A) General average guarantees have been given on behalf of, and secured by, Lloyd's underwriters. It is estimated that the aggregate of the liabilities attaching to these guarantees at 31 December 2007 amounted to £11.9m (31 December 2006: £12.6m).

B) The Society has taken on the responsibilities of some private members under hardship and other agreements. The Society has also given indemnity bonds to Lioncover Insurance Company Limited (Lioncover) and Centrewrite Limited (Centrewrite) respectively against any shortfall in their assets.

In the implementation of 'Reconstruction and Renewal', Names underwriting in respect of 1992 and prior years, Lioncover and Centrewrite were reinsured into Equitas Reinsurance Limited (ERL). ERL retroceded all of its liabilities to Equitas Limited (EL), (ERL and EL are collectively referred to as Equitas). If Equitas were unable to discharge in full the liabilities which it has reinsured, any resulting shortfall in respect of Lioncover or Centrewrite could be met out of both the 'Old' Central Fund and the New Central Fund under the terms of their respective Lloyd's bond. Both the 'Old' Central Fund and the New Central Fund would also be available to meet the claims of policyholders of private members who are party to hardship agreements executed before 4 September 1996, to the extent that such an event resulted in a shortfall. However, unless the members of the Society resolve in a general meeting to make the New Central Fund available, only the 'Old' Central Fund would be available to meet the claims of policyholders of private members who are not party to hardship agreements executed before 4 September 1996.

The Council has determined that any losses resulting from such indemnities will be met by the Lloyd's Central Fund.

The reinsurance of Equitas' reinsurance obligations with National Indemnity Company makes these contingent liabilities significantly less likely to crystallise.

C) Uncollateralised bank guarantees and other arrangements have been entered into by the Society and its subsidiary undertaking, Additional Securities Limited, to provide security in connection with the underwriting activities of the members of Lloyd's in the countries shown:

	2007 £000	2006 £000
Guarantees provided by the Society: USA US$1,500,000 (2006: US $1,500,000)	**754**	766
Guarantees provided by the Society including Additional Securities Limited: Cayman Islands: Letter of credit US$1,250,000 (2006: US $1,250,000)	**628**	639

D) The Society has given indemnities to certain of its subsidiary undertakings, and the directors thereof, in respect of any claims or actions which may be brought against them or any future operating losses incurred by them in connection with the companies' activities. The Society has also given indemnities to and has agreed to cover certain specific costs that may be incurred by members of the Council, Lloyd's Franchise Board, Lloyd's Regulatory Board and Lloyd's Market Board (the latter two boards ceased during 2002) and of their respective sub-committees, the Society staff and also certain individuals and organisations who have been asked to carry out or provide services to the Society or on behalf of, or for the benefit of its members.

E) Fifty one individual members have commenced proceedings alleging that Lloyd's fraudulently misrepresented the effect of Reinsurance to Close. The Society does not accept any liability in respect of this action.

F) A counterclaim alleging fraud by Lloyd's has been filed in the US by one private member, in response to the Society's proceedings seeking recognition of a judgment obtained by the Society in England. The Society does not accept any liability in respect of this claim.

G) In Quebec, proceedings have been issued by Agence Nationale D'Encadrement Du Secteur Financier as the regulator of the Quebec policyholder protection fund, by ninety one alleged insureds and by one intermediary who was offering extended warranty programs to automobile dealers against the Society and other parties arising out of the issue by a coverholder of purported 'policies of insurance' without the authority of a Lloyd's syndicate. The Society does not accept any liability in respect of this action.

H) In Greece proceedings have been issued against the Society alleging a conspiracy to frustrate an insurance claim. The sum claimed is €14m. The Society does not accept any liability in respect of this action.

In respect of all contingent liabilities disclosed as at 31 December 2007, no provision has been made in the Society financial statements as the Society does not accept any liability in respect of any of the claims.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2007

26. REINSURANCE OF EQUITAS' REINSURANCE OBLIGATIONS WITH NATIONAL INDEMNITY COMPANY

On 10 November 2006, Equitas Holdings Limited and Equitas Limited (EL) (see note 25B) entered into a retrocession and run-off contract with a Berkshire Hathaway group undertaking, National Indemnity Company (NICO), becoming effective on 27 March 2007 by which NICO has provided to EL retrocession cover up to a limit of US$14bn (EL's net undiscounted claims reserves as at 31 March 2006 plus US$5.7bn) less adjustments for claims payments between 1 April 2006 and the date when the transaction became effective. The premium for that retrocession was all of EL's existing assets (including its residual beneficial interest in the Equitas American Trust Fund) less £172m plus a contribution of £72m from Lloyd's, which was paid on 27 March 2007 following approval by Lloyd's members at the Extraordinary General Meeting held on 22 February 2007. This Phase 1 of the transaction has provided substantial additional retrocessional cover for Equitas, and thus for the Society's subsidiary undertaking, Lioncover, which as at 31 December 2007 recognises a reinsurance asset due from ERL of £387m (see note 13).

The Society's contingent liabilities in respect of responsibilities arising from the reinsurance of liabilities into ERL as part of the implementation of 'Reconstruction and Renewal' as described in note 25B are now also considerably less likely to crystallise.

Phase 2 of the transaction involves the transfer of Equitas-reinsured members' obligations to policyholders to another company, which will be EL, Equitas Reinsurance Limited or a specially-created insurance company. This transfer of business is required to be sanctioned by the High Court under Part VII of the Financial Services and Markets Act 2000. Provided the transfer is completed by 31 December 2009, EL has the option to purchase up to US$1.3bn of additional reinsurance from NICO at a cost of £40m. A further £18m is payable by the Society, subject to approval by the Council in 2009, before 31 December 2009. The latest date for this payment in the event that the insurance business transfer does not take place has yet to be agreed. The option to purchase the additional reinsurance cover will not be available if EL's net undiscounted reserves (inclusive of IBNR) have deteriorated by more than US$2bn since 31 March 2006.

The Society has accounted for its total contribution of £90m in the group financial statements as an expense in the group income statement in 2007. As part of Phase 1 £50m was payable by Equitas as a return premium to reinsureds. The Society has accounted for that part of the return premium due to it in the group financial statements.

FOUR YEAR SUMMARY

	2007 £000	2006 £000	2005 £000	2004 £000
Operating income	**177,853**	171,498	162,353	169,166
Central Fund contributions	**168,346**	152,226	70,077	190,657
General insurance net premium income	**2,046**	2,834	2,769	3,428
Other group income	**81,478**	23,477	18,637	28,979
Total income	**429,723**	350,035	253,836	392,230
Central Fund claims and provisions released/(incurred)	**18,208**	(115,735)	(223,889)	(125,540)
Contribution to Equitas – Berkshire Hathaway transaction	**(90,000)**	–	–	–
Gross insurance claims	**16,330**	(55,461)	(30,039)	(47,735)
Insurance claims recoverable from reinsurers	**(17,041)**	56,804	29,844	52,053
Other group operating expenses:				
Employment (including pension costs)	**(82,752)**	(72,996)	(72,201)	(68,415)
Premises	**(35,371)**	(34,629)	(32,074)	(31,668)
Legal and professional	**(16,580)**	(18,442)	(21,596)	(22,768)
System and communications	**(19,293)**	(20,394)	(23,608)	(22,604)
Other	**(33,870)**	(24,334)	(22,618)	(27,961)
Total other group operating expenses	**(187,866)**	(170,795)	(172,097)	(173,416)
Operating surplus/(deficit)	**169,354**	64,848	(142,345)	97,592
Profit on sale of Lloyd's buildings	**–**	–	–	23,638
Surplus/(deficit) before finance, associates and tax	**169,354**	64,848	(142,345)	121,230
Finance costs	**(53,752)**	(32,921)	(39,951)	(4,547)
Finance income	**128,468**	52,942	129,033	45,875
Unrealised exchange (losses)/gains on borrowings	**(18,059)**	3,842	6,298	(2,630)
Share of profits of associates	**4,395**	1,867	2,006	1,872
Surplus/(deficit) before tax	**230,406**	90,578	(44,959)	161,800
Tax (charge)/credit	**(65,994)**	(7,012)	17,343	(38,959)
Surplus/(deficit) for the year	**164,412**	83,566	(27,616)	122,841

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 The accident year ratio is calculated as expenses and 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.

Calendar year ratio This is the combined ratio (see below) and is the sum of the accident year ratio (see above) and the prior years' reserve movements (see below).

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.

Capacity In relation to a member, it is the maximum amount of insurance premiums (gross of reinsurance but net of brokerage) which a member can accept. In relation to a syndicate it is the aggregate of each member's capacity allocated to that syndicate.

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.

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 United Kingdom 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.

Financial Services Authority (FSA) The body that regulates the financial services industry in the UK.

Franchise The arrangements that permit managing agents and members to conduct business in the Lloyd's market, and maximise the benefits from the Lloyd's brand, a common rating, mutual security and licences to conduct business around the world.

Franchise Board The board established by the Council, which is responsible for managing the Franchise.

Franchise goal To create and maintain a commercial environment at Lloyd's in which the long-term return to all capital providers is maximised.

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.

GWP (Gross Written Premiums) Written insurance premiums, gross of reinsurance and acquisition costs.

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.

Managing agent An underwriting agent responsible for managing a syndicate.

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

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 as a proportion of net premiums earned during the year.

Realistic Disaster Scenarios (RDS) A series of scenarios, both natural and man-made, which are used to model the market's exposure 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.

Special Purpose Syndicate (SPS) 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 members that have separate ownership and control to the syndicate's managing agent.

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.

Tier 1 capital The core measure of an insurer's financial strength from the viewpoint of the FSA. It consists of the most reliable and liquid assets. The perpetual securities issued in 2007 quality as tier 1 capital as the proceeds of the debt issue are fully paid and immediately available; debt holders are sub-ordinate to payment of lines.

Traditional Syndicate A syndicate whose members underwrite insurance business at Lloyd's for the current year of account and which is neither an SPS syndicate or an RITC syndicate.

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 at the end of 36 months.

FIDENTIA

Since merchants first met to insure their ships at Edward Lloyd's coffee shop over 300 years ago, nearly every aspect of the way we do business has changed. But one constant is the bold confidence proclaimed by our motto, reflected in both our unique appetite for risk and our worldwide reputation for settling valid claims.

The cover and text pages of this report are printed on Revive 50:50 Silk, a recycled paper containing 50% recovered waste, 50% virgin fibre and is certified as an FSC mixed sources grade. Revive 50:50 is manufactured to the certified environmental management system ISO 14001.
Designed by Radley Yeldar. Printed by Midas Press. Lloyd's is a registered trademark of the Society of Lloyd's.

Lloyd's One Lime Street London EC3M 7HA Telephone +44 (0)20 7327 1000 Fax +44 (0)20 7626 2389 www.lloyds.com