Market Bulletin

LLOYD'S

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FROM:	General Manager, LPSO
LOCATION:	CH/L4
EXTENSION:	2113
DATE:	21 December 1998
REFERENCE:	Y1050
SUBJECT:	REINSURANCE TO CLOSE (RITC)
ACTION POINTS:	Note revised LPSO procedures and requirements for RITC contracts, especially "third party" RITC.
DEADLINE:	Effective immediately

Over the past eighteen months, there has been significant examination and development of the methods and requirements for handling reinsurance to close (RITC). This includes the emergence of syndicates willing to write RITC contracts on a commercial, third party basis for orphan syndicates.

During 1998, LPSO has been working closely with other business units and market practitioners to ensure operational matters relating to RITC are given due consideration and that practice and procedure is developed and applied accordingly. Attachment 1 to this bulletin is intended to provide a comprehensive summary of RITC matters insofar as they relate to LPSO intervention. It is hoped that it will serve as a useful reference document in relation to next year's closure of the 1996 account. More immediately, it should prove useful to those syndicates that have not yet closed their 1995 account.

This bulletin has been sent to all active underwriters, managing agents and Lloyd's brokers. Any questions or enquiries should be directed to Deirdre Matthews or Steve Constantine of LCO/LPSO Technical Services, on Lloyd's extensions 2535 or 2351 respectively.

Michael Collins

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REINSURANCE TO CLOSE - LPSO PROCEDURES

1 The traditional role of LPSO

1.1 RITC Premium Processing (non third Party RITC)

LPSO does not centrally record or process RITC premiums via central settlement where the reinsuring and reinsured syndicate are treated as the same syndicate for premium income monitoring purposes under the Syndicate Premium Income Byelaw by Underwriting Agents Department. The LPSO database and statistical reports generated from this database do not include these transactions.

1.2 RITC contract wordings

Since 9 December 1985 (as per the RITC Byelaw [no. 6 of 1985]), RITC contracts have been required to be evidenced in writing and presented to LPSO. The onus is upon a managing agent to present contract wordings to LPSO for signing within twelve months of the closure of a given year of account. For example, contract wordings relating to the 1995 account RITC should be signed by LPSO before the end of 1998. There is currently no standard form of RITC contract wording for general use. LPSO sign, seal and date RITC contract wordings.

The Regulatory bulletin (125/97) "Reinsurance to Close" dated 29 December 1997, advised the RITC Contract Requirements 1997, requiring all RITC contract wordings underwritten by members of a syndicate to include certain mandatory terms. Further details follow later in this paper.

RITC wordings should now be marked for the attention of

Business Support
LCO/LPSO Technical Services

and presented to the London Customer Liaison Office, 86/328, or sent direct to Gun Wharf, Chatham.

1.3 Central settlement and advice of post RITC run-off transactions

If the reinsuring syndicate number is different to the reinsured syndicate number and Underwriting Agents Department (UAD) have agreed that the contract can be classed as non third party RITC, it is possible to arrange for central accounting settlement of any run-off transactions to be directed to the bank account of the reinsuring syndicate (and tore-route USM/SCM advising messages to the reinsuring syndicate's mailbox), even though LPSO and LCO processing of such transactions will retain the original, reinsured syndicate number and year of account. This feature is only available where RITC is ceded to ~ reinsuring syndicate number.

2 Third Party RITC (also known as Commercial RITC)

Third party RITC contracts have evolved to cater for RITC of orphan syndicates. These are defined as RITC contracts where the year of account of a syndicate (the reinsured syndicate) is reinsured into the later year of account of a different syndicate (the reinsuring syndicate). For example, RITC of the 1995 account for syndicate X being reinsured into the 1998 account of syndicate Y. In such cases, the premium income needs to be allocated to the later year of account of the reinsuring syndicate.

A similar arrangement has existed in the form of the established ‘arms length’ contracts. Unlike conventional contracts, which do not require signing through LPSO, the premium for third party RITC must be included in central Premium Income Monitoring.

2.1 Inward Third Party RITC premium processing

2.1.1 In order for LPSO to process third party RITC contracts, the RITC slip and any related documents should be presented to LPSO for processing, allocation of a signing number and date, recording of the contract wording, and, if brokers and/or ceding/reinsuring syndicates elect to settle the RITC premium through LPSO, the settlement of the RITC premium. Whether or not LPSO settle the RITC premium between brokers &/or ceding/reinsurings syndicate(s) is a decision for those parties. It may be most appropriate to transact the premium by cheque payment, outside of central accounting, although it will still be necessary to process a ‘non-cash’ entry through LPSO.

2.1.2 Experience to-date indicates that in some, but not all, cases, a Lloyd’s broker is involved in the RITC contract negotiations. If a Lloyd’s broker is involved, LPSO will record the inward RITC premium as a debit to the Lloyd’s broker number and a credit to the reinsuring syndicate(s). If the RITC has been arranged without a broker, the reinsuring syndicate (or agency) will need to operate a dummy broker number. The inward RITC premium will be recorded by LPSO against this dummy broker number and the reinsuring syndicate(s).

2.1.3 Subsequent ‘run-off additional premium, return premium, claim and claim refund transactions (ie post RITC) will continue to be processed to the reinsured syndicate number using the original slip documentation, thereby retaining original risk coding etc. Managing agents may elect to direct USM/SCM transaction advices and central settlement to the mailbox and bank account(s) of the reinsuring syndicate (refer section 1.3 also).

Alternatively, managing agents may consider an audit trail is better maintained and premium income more effectively monitored, by processing run-off transactions, to the RITC slip and therefore the year of account into which liabilities have been reinsured.

2.1.4 Syndicates should also note that transactions processed against the RITC slip will attract the TC risk code and will not retain the coding allocated to the original slips and premiums. (Also refer 2. 1.3).

2.1.5 Settlement of post RITC run-off transactions cannot be made to multiple reinsuring syndicates, unless the run-off transactions are processed against the RITC slip (refer 2. 1.3). This situation is most likely to occur where the reinsuring syndicates are a corporate parallel split stamp.

2.2 Outward Third Party RITC premium processing

Where a Lloyd's broker is involved in the RITC, a 'premium debit' transaction should be processed through Lloyd's Outward Reinsurance System (LORS). This will be either a 'paid by cheque' or central settlement transaction, debiting the reinsured syndicate, as required.

Where there is no Lloyd's broker involved, the reinsured syndicate will need to create an equivalent LORS transaction to debit the reinsured syndicate and credit the dummy broker number account against which the inward RITC premium is to be recorded. Again, this will be either a 'paid by cheque' or central settlement transaction.

2.3 Risk Codes for inward and outward Third Party RITC transactions

Regulatory bulletin (066/97) "The Risk Coding System" dated 2 July 1997, introduced risk code 'TC' (effective same date) which should be applied to all inward transactions, whether 'paid by cheque' or central settlement. This eliminates the need to allocate RITC premium against more specific code(s) and also isolates RITC premiums within central reporting. RITC premiums are, of course, exempt from the premium charge levied as part of Lloyd's reconstruction and renewal programme.

The same bulletin also made reference to the need for managing agents to maintain details by risk code of the risks being reinsured. Any questions relating to this section should be referred to Keith Harris, Policy department, Lloyd's extension 6147.

3 New requirement for mandatory terms in RITC contract wording

Regulatory bulletin (125/97) "Reinsurance to Close" dated 29 December 1997, advised the RITC Contract Requirements 1997. Effective 16 December 1997, all RITC contract wordings underwritten by members of a syndicate must include certain mandatory terms. These terms were included in the aforementioned bulletin and apply to all RITC contract wordings. They are enclosed again for information as Attachment 2. Whilst the onus is upon the managing agent to ensure contract wordings comply with these requirements, LPSO will check to ensure that contract wordings contain the mandatory terms. Work is underway to provide a model wording for use by managing agents. More information about this will follow under separate cover.

4 RITC involving more than one reinsured syndicate

There is no reason why multiple syndicates cannot reinsure to close into one syndicate, provided the RITC contract complies with the RITC Requirements 1997. Where incidentals or merging of syndicates are involved, one contract is acceptable, provided the incidental or merging reinsured syndicate numbers are listed in the schedule. In all other circumstances, it is recommended to have one contract per syndicate number, so as to minimise any uncertainty and achieve absolute clarity as to where the run-off obligations lie.

5 RITC 1995 (and later) account

There are specific requirements relating to closure of the 1995 and subsequent years of account for US dollar business arising from the amendment to the US Trust Fund structure, effective 1 August 1995. More detail is available in market bulletin (Y734), dated 17 November 1997, " 1995 Year of Account Regulatory Funding Requirements, Reinsurance to Close and Profit Distribution".

5.1 Trust Fund Arrangements

Reinsuring syndicates must have trust funds to mirror those of the syndicates who they are reinsuring. Agents are reminded of the need to verify that the correct trust fund structure is in place to support the new US dollar liabilities assumed by the reinsuring syndicates, ie that LATFs, US Situs Credit for Reinsurance and US Situs Surplus Lines Trust Funds exist for any syndicate year of account which assumes such 1995 liabilities through the RITC.

Any managing agent which has not established such arrangements should contact the North America Unit, Lloyd's extension 6234 as a matter of urgency to discuss their syndicate's circumstances.

These arrangements should continue on subsequent RITC years. Managing agents should consider this when agreeing requirements for future years trust deeds and accounts.

5.2 Third Party RITC slips

Slips presented to LPSO evidencing third party RITC contracts should show:

a) risk code 'TC' and whether the RITC premium requires central settlement or non-cash processing,

b) a breakdown of the US dollar RITC premium between pre and post 1 August 1995 liabilities, in order that the relevant trust funds will be funded appropriately. Separate signing numbers and dates will be allocated to the two US dollar transactions. This breakdown will need to continue on subsequent years of account being reinsured to close for as long as the LATF exists, refer section 5.1.

c) the US Classification heading on panel 2 completed as 'Non Regulated', irrespective of breakdown of premium. For the post 1 August 1995 liabilities' RITC premium, the 'Non Regulated' classification will attract the appropriate FIL code to then trigger the correct trust fund code.

5.3 Central Settlement Bank Accounts

Market bulletin (Y734), dated 17 November 1997, 'r 1995 Year of Account Regulatory Funding Requirements, Reinsurance to Close and Profit Distribution", advised that the NYID has indicated that assets needed to support LATF liabilities should be retained in LATFs in the US. Syndicates formed in 1996 or later intending to accept RITC liabilities will need to open an LATF account.

5.4 Inception Date Allocation (IDA) and the 1995 transition year of account

When IDA was introduced, 1995 was identified as the transitional year. All premiums presented to LPSO in 1995 were signed to the 1995 account irrespective of inception date. Additionally, any subsequent late signings of premiums for risks incepting prior to 1995 have been allocated to the 1995 account. In accordance with the Syndicate Accounting Byelaw, from 1 January 1996, LPSO allocated risks to the years of account in accordance with their inception dates. Syndicates are reminded that liabilities relating to risks incepting in 1995, but not yet processed by LPSO, will be signed to the 1995 account and should be handled through the RITC. Any queries relating to this section should be referred to Keith Harris, Policy department, Lloyd's extension 6147.

6 Summary of contacts for advice on RITC processing

Topic	Contact
Allocation and use of a dummy broker number for inward / outward third party RITC processing. Opening LATF bank accounts for 1996 and later years. Redirection of central settlement for post RITC run-off transactions from the reinsured syndicate account/years of account to a reinsuring syndicate account/years of account. Processing and signing of RITC contracts.	Deirdre Matthews Steve Constantine Business Support team LCO/LPSO Technical Services Lloyd's extension 2535 or 2351
Inception Date Allocation (IDA) Risk Codes	Keith Harris, Policy department, Regulatory Lloyd's extension 6147.
Trust Fund Arrangements	North America Unit Lloyd's extension 6234.
Authority for transfer of assets/arms length RITC.	Authorisation department, Regulatory Refer to individual case officers.

REINSURANCE TO CLOSE CONTRACT REQUIREMENTS 1997

In exercise of the Council's powers under paragraph 2(3) of the Syndicate Accounting Byelaw (No. 18 of 1994) the Lloyd's Regulatory Board hereby makes the following requirements.

1. Citation

These requirements may be cited as the Reinsurance to Close Contract Requirements 1997.

2. Mandatory terms in contracts

Without prejudice to sub-paragraph (a) of the definition of "reinsurance to close" in paragraph 1 of Schedule 1 to the Syndicate Accounting Byelaw (No. 18 of 1994) or to the Parallel Syndicates (Reinsurance to Close) Requirements 1997, every contract of reinsurance to close underwritten by members of a syndicate shall, unless the Lloyd's Regulatory Board otherwise agrees (whether generally or in relation to a particular case) include express terms to the following effect -

(a) the reinsuring members unconditionally agree to indemnify the reinsured members, without limit as to time or amount, in respect of the net amount of all known or unknown losses, claims, refunds, reinsurance premiums, outgoings, expenses and other liabilities (including extra-contractual obligations for punitive or penal damages) arising in relation to the underwriting business of the syndicate for the reinsured year of account (and earlier years of account of the same or any other syndicate reinsured to close into that year of account) (the "underwriting business") after taking account of all amounts recoverable by the reinsured members under syndicate reinsurances in respect of those liabilities and actually recovered on or after the inception date of the contract;

(b) notwithstanding that the indemnity under the contract is against liabilities net of syndicate reinsurance recoveries or that the ultimate net liability of the reinsuring members may not yet have been ascertained, the reinsuring members shall discharge or procure the discharge of the liabilities of the reinsured members;

(c) either

(i) the rights to receive all premiums, recoveries and other monies recoverable at any time in connection with the insurance business of the reinsured members are assigned to the reinsuring members by the contract or are to be assigned on their subsequent request; or

(ii) the reinsuring members are authorised by the reinsured members to collect on behalf of the reinsured members the proceeds of all such rights and retain them for their own benefit so far as they are not applied in discharge of the liabilities of the reinsured members;

(d) the reinsuring members are required and fully, irrevocably and exclusively authorised on behalf of the reinsured members to conduct the underwriting business, and authorised to sub-delegate that authority to the reinsuring members' managing agent and to any person underwriting any reinsurance to close of the reinsuring members and to permit the further sub-delegation of the whole or part of that authority in either case; and

(e) the contract shall not be cancelled or avoided for any reason, including mistake, non-disclosure or misrepresentation (whether innocent or not).

3. Multi-reinsurer contracts

(1) No contract of reinsurance to close may be underwritten by more than one syndicate except -

(a) in the case of a contract to which the Parallel Syndicates (Reinsurance to Close) Requirements 1997 apply;

(b) in the case of a contract to which sub-paragraph (3) of this paragraph applies; or

(c) where the Lloyd's Regulatory Board is satisfied that it is not practicable for the contract to be underwritten by a single syndicate only and that the contract should be permitted to be underwritten by more than one syndicate and grants its consent.

(2) Consent granted under sub-paragraph (1)(c) may be subject to such conditions as the Lloyd's Regulatory Board thinks fit.

(3) Where, under any approval granted under Part H of the Membership and Underwriting Requirements (Corporate Member), the same individual is permitted to act as underwriter for two syndicates managed by the same managing agent, one of which consists only of a single corporate member and the other of which includes individual members, both syndicates may together underwrite a reinsurance to close of another syndicate in the proportions borne by their respective syndicate allocated capacities for the year of account to which the reinsurance to close contract is allocated.

(4) Any reinsurance to close contract underwritten under sub-paragagh (3) shall require that the authority thereby conferred on both syndicates as constituted for the reinsuring year of account to conduct the underwriting business reinsured under the contract shall at all times thereafter be delegated to the same managing agent for both syndicates.

(5) Save to the extent that, in accordance with this paragraph, it is underwritten by more than one syndicate, any contract of reinsurance to close permitted by or under this paragraph 3 shall contain provisions so as to satisfy sub-paragraph (a) of the definition of “reinsurance to close” in paragraph 1 of Schedule 1 to the Syndicate Accounting Byelaw (No. 18 of 1994), modified, if necessary, to comply with sub-paragraph (e) of that paragraph.

4. Commencement

These requirements shall come into force on [ ].