LLOYD'S

ANNUAL REPORT 2008

RESILIENCE IN TESTING TIMES

LLOYD'S ACCEPTS BUSINESS FROM OVER 200 COUNTRIES AND TERRITORIES WORLDWIDE.

OUR 80 LICENCES, SUPPORTED BY A NETWORK OF LOCAL OFFICES, ENSURE ACCESS TO INSURANCE MARKETS LARGE AND SMALL.

Key to map

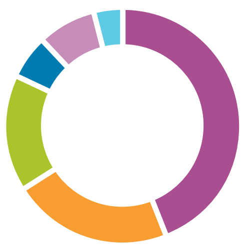
- US & Canada
- United Kingdom
- Europe
- Other Americas
- Central Asia & Asia Pacific
- Rest of the World

Lloyd's total business by class

Reinsurance	35%
Property	22%
Casualty	21%
Marine	8%
Energy	6%
Motor	5%
Aviation	3%

Lloyd's total business by region

US & Canada	44%
United Kingdom	22%
Europe	16%
Other Americas	6%
Central Asia & Asia Pacific	8%
Rest of the World	4%



For more information on Lloyd's international reach please see page 27.

CLASS OF BUSINESS	TOTAL BUSINESS BY CLASS	TOTAL BUSINESS BY REGION* US & CANADA 44%	OTHER AMERICAS 6%	UNITED KINGDOM 22%
REINSURANCE More information on page 61.	35%	30%	77%	27%
PROPERTY More information on page 62.	22%	30%	8%	19%
CASUALTY More information on page 63.	21%	21%	8%	24%
MARINE More information on page 64.	8%	5%	4%	6%
ENERGY More information on page 65.	6%	10%	1%	3%
MOTOR More information on page 66.	5%	1%	1%	20%
AVIATION More information on page 67.	3%	3%	1%	1%

All figures as at 31 December 2008

*Geographical split is based on Xchanging Ins-sure Services data, as at 31 December 2008

EUROPE 16%	CENTRAL ASIA & ASIA PACIFIC 8%	REST OF THE WORLD 4%
35%	44%	58%
16%	15%	7%
20%	26%	14%
18%	7%	9%
6%	5%	3%
1%	1%	2%
4%	2%	7%

Lloyd's is well placed to face the challenges ahead. Here's why…

Through the past year's financial turmoil, Lloyd's has stood firm. Our ability to cover complex risks in such an unstable climate reflects the strengths outlined below, which are described in more detail throughout this report.

OUR UNDERLYING CAPABILITIES

AGILITY
Lloyd's entrepreneurial approach is founded on its collective experience, expertise and appetite for risk. These enable Lloyd's underwriters to adapt quickly to new, unusual and emerging risks.

More information on pages 8-9.

STRENGTH
The Lloyd's market has been built, and tested, to withstand extreme demands – such as the need to finance rapid reconstruction after major catastrophes.

More information on pages 20-21.

EXPERTISE
We constantly monitor, measure and anticipate risk – and refine the market's response capability – so that Lloyd's underwriters can assess evolving challenges and be prepared to address them.

More information on pages 28-29.

FLEXIBILITY
As risks change, Lloyd's is structured to respond flexibly. Our resilience comes from constantly reshaping ourself, and the Lloyd's platform provides security and rigour without excessive rigidity.

More information on pages 38-39.

STABILITY
Lloyd's maintains a disciplined approach to the insurance cycle. Writing for profit, rather than market share, helps to keep the Lloyd's market and its participants stable and profitable.

More information on pages 48-49.

ROBUST
IN FACING THE FUTURE

It's in testing times that businesses show their mettle. In a year when the robustness of many financial institutions was severely tested, Lloyd's maintained its financial strength. At the year-end we had our strongest ever Central Fund, and contribution rates eased to 0.5%. Mutuality is at its lowest cost to members for a decade.

Inevitably, pre-tax profit was lower, down 51% to £1,899m which is, nonetheless, the third most profitable year the market has produced since the introduction of annual accounting in 2001. This lower profit reflected weakening market conditions, an increase in catastrophe events after a period of unusually low claims, and exceptionally challenging financial conditions. But in a year of turbulence for the financial markets, the most important achievement was that Lloyd's financial strength remained virtually unimpaired.

This has not happened by chance. In extreme conditions, Lloyd's core attributes come to the fore. We have the agility to adapt to changing conditions, the financial strength to withstand turbulence, the expertise to address an evolving risk landscape, the flexibility to meet customers' needs worldwide, and the stability that comes from disciplined underwriting.

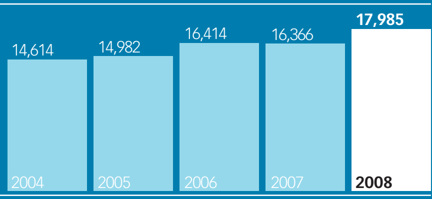
UNDERPINNED BY THESE STRENGTHS, LLOYD'S REMAINS WELL PLACED TO FACE THE CHALLENGES AHEAD.

2008 FINANCIAL HIGHLIGHTS

- Lloyd's achieved a profit before tax of £1,899m (2007: £3,846m) and a combined ratio of 91.3% (2007: 84.0%). This was a solid performance during an exceptionally turbulent year for the financial sector. Higher levels of catastrophes and attritional claims were partially offset by currency movements and prior year releases.
- Return on investments of 2.5% (2007: 5.6%) benefited from a conservative investment strategy.
- Surplus on prior years of £1,265m (2007: £856m) based on strong reserves.
- Central assets increased further to £2,072m (2007: £1,951m).

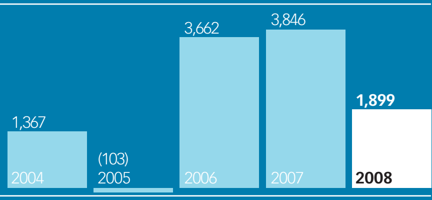
Gross written premium*
(£m)

£17,985m



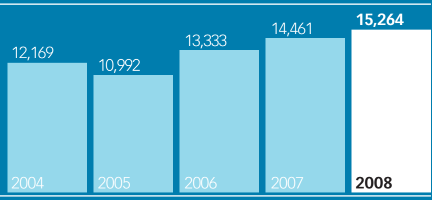
Profit/(loss) before tax
(£m)

£1,899m



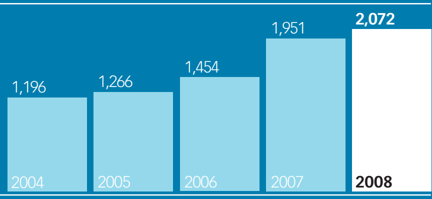
Capital, reserves and subordinated debt and securities
(£m)

£15,264m



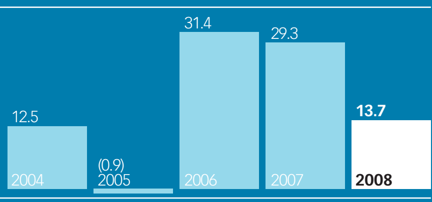
Central assets*
(£m)

£2,072m



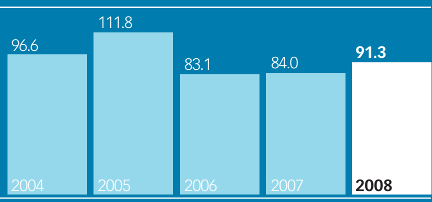
Return on capital
(%)

13.7%



Combined ratio*
(%)

91.3%



*See Glossary on page 140.

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

2008 BUSINESS HIGHLIGHTS

- A.M. Best, Fitch Ratings and Standard & Poor's affirmed their Lloyd's security ratings of A (Excellent), A+ (Strong) and A+ (Strong) respectively.
- New trading licences obtained in Brazil – where Lloyd's was the first 'Admitted' reinsurer – Poland and Austria.
- By the end of 2008, over 90% of in-scope claims and 96% of original premiums were processed electronically through the Electronic Claims File and Accounting & Settlement repositories.
- Lloyd's successfully lobbied for the inclusion of letters of credit in the EU's Solvency II framework.
- Lloyd's governance arrangements have been modernised and access to the market widened following the passing of the Legislative Reform Order.
- The US regulatory authorities are considering a new framework that, when implemented, will reduce US collateral requirements necessary to conduct reinsurance business.
- HM Revenue & Customs agreed to reduce the tax burden for corporate members by introducing tax relief in the form of a Claims Equalisation Reserve.

STRATEGY

VISION
OUR VISION IS TO BE THE PLATFORM OF CHOICE

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.

STRATEGIC PRIORITIES:

- Managing the cycle
- Market access
- Operating environment

For more information on Lloyd's strategy see page 30.

BENEFITS OF OPERATING AT LLOYD'S

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.

CONTENTS

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.

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

WELL PLACED TO FACE THE CHALLENGES AHEAD.

Amidst the unprecedented slump in the world economy, Lloyd's remains in good shape. This has been reflected in our full year results. We have reported a profit of £1,899m and a combined ratio of 91.3%. Albeit that our profits have inevitably been impacted by lower insurance rates, natural catastrophes and a reduction in investment income and offset by currency movements and prior year surpluses.

Our conservative investment strategy and sound underwriting performance have meant that our capital remains intact. Our solvency position continues to strengthen, with limited draw downs on our Central Fund to meet legacy claims, and no new member insolvencies since 2003.

At the same time it is to be noted that the rapid depreciation in sterling in the last four months of 2008 against the dollar, and other major currencies, has also had a significant impact on our results. Lloyd's holds a major proportion of its assets in the currencies in which it transacts business. The decline in the value of sterling means that profits generated in foreign currency are higher when converted back to sterling.

These results underline the importance which we have attached to risk management and underwriting discipline. Our focus on these core elements has been fundamental to the market's resilience and it will remain so as we look to the opportunities and the challenges the future brings. It was important that the market learnt the lessons of the past – pulling back from providing wide insurance cover for financial institutions in the wake of the Enron and WorldCom scandals. As a result, the impact of the sub prime crisis on the market is within the normal course of business.

We cannot of course expect to escape other financial and recessionary trends. We are already taking a long-term view of the potential issues that may arise from the fall in the value of sterling and are working with businesses to assess the impact on capital requirements to support our overseas business. We are also likely to see a rise in claims frequency as the recession starts to bite.

The challenges of the current economic conditions will, however, provide opportunities for insurers. Insurance is largely a non-discretionary product, and while asset values will fall, businesses and individuals will still need to buy cover for their risks. In fact, some argue that the demand for insurance will be even greater as businesses seek to protect their assets and shareholders. Our subscription model, which is underpinned by the concept of spreading risk, will continue to be fundamental in meeting our customers' needs. Less surplus capital in the industry and a low investment return outlook should also improve underwriting discipline, helping to improve market conditions.

Ultimately, the long-term trend in profitability for the industry is not linked to the economic cycle. Statistics show that the industry did better during the Great Depression than for most of the boom years of the 1980s. However, as a sector we are still vulnerable to the vagaries of the underwriting cycle.

MARKET CONDITIONS

The recent run of calm summers ended in 2008 as Hurricanes Ike and Gustav roared into the Gulf of Mexico destroying hundreds of coastal homes and surging inland. Together these storms are projected to produce net claims for the Lloyd's market of £1,430m ($2,574m).

The absence of major catastrophes in the last two years has, as always, been a double edged sword for the industry – reducing the volume of claims to generate good underwriting figures but also forcing down rates and adding to the already soft market environment. In the wake of Hurricane Ike and in light of the current economic conditions, some businesses are calling the bottom of the cycle, although it is too early to say if prices are improving outside catastrophe-exposed classes.

Hurricane Ike and the prevailing economic crisis have demonstrated only too well that risks continue to pose challenges for the market and we need to remain adept at meeting them, utilising our expertise and flexibility. Any upturn in the market should not detract from the continuing need to exercise underwriting discipline.

THE REGULATORY AND GLOBAL LANDSCAPE

Like the wider economy the regulatory landscape has also felt the force of change. Despite this, Lloyd's lobbying efforts have helped to deliver progress for the market in a number of areas, both in Europe and North America:

- → Lobbying for the inclusion of letters of credit in the Solvency II Framework.
- → The US regulatory authorities considering a new framework that would reduce collateral requirements for non-US based reinsurers.
- → The UK Government agreeing to reduce the tax burden for corporate members by introducing tax relief in the form of a Claims Equalisation Reserve, finally bringing parity in the tax treatment of reserves with other UK insurance companies.

One of the consequences of the financial crisis has been to increase the political pressures around the world for more regulation. It is now more important than ever that Lloyd's continues to take part in these debates, offering a voice of experience and reason.

Closer to home we undertook to modernise our governance arrangements through a Legislative Reform Order, which, over the long-term, will also widen access to the market, helping Lloyd's to compete on an equal footing with our competitors. We are most grateful to HM Treasury for their help in achieving its successful passage through both Houses of Parliament.

SUMMARY

Sound risk management, effective oversight and management focus are the fundamentals that have supported Lloyd's well in recent years.

We have undergone a remarkable transformation but have always stuck to our core offering – devising innovative and tailored solutions for complex risks. There is no greater ambition for us than to be the world's leading insurance market.

We stand ready to continue our role in supporting the world's economy and its businesses – providing insight so that they can have the foresight to manage tomorrow's risks.

At Lloyd's we have the capital, risk appetite and expertise to help to shoulder the risks of the world. As a subscription market built on the concept of sharing risk, we also have the strength and flexibility that can only come from a marketplace of over 50 individual businesses and a 321-year history.

I would like to end by thanking all of those within the Corporation and market who have contributed to Lloyd's success over the last year. Richard Ward and his team within the Corporation have shown great leadership and the market has continued to demonstrate its professional approach, skills and attributes that have made it world famous.

I must also pay tribute to Bill Knight and Peter Morgan for their outstanding contributions during their nine years on Council and to Edward Creasy, Roy Brown and Stephen Hodge for their hard work and important contribution since the Franchise Board's inception. I look forward to working with the new members of both bodies.

PETER LEVENE
Chairman
23 March 2009

BEHIND THE ICONIC GLASS LIFTS AND STEEL DUCTS IS ONE OF THE WORLD'S MOST DYNAMIC ORGANISATIONS.

Lloyd's is the world's leading specialist insurance market, conducting business in over 200 countries and territories worldwide – and is often the first to insure new, unusual or complex risks. We bring together an outstanding concentration of specialist expertise and talent, backed by excellent financial ratings which cover the whole market.

Lloyd's began over 300 years ago in Edward Lloyd's coffee house – a place where shipowners 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.

To this day, Lloyd's remains a dynamic, innovative market where individuals meet face-to-face. 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 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.

We continue our steady expansion into overseas markets to build our platform for the future. A major priority has been and continues to be managing performance throughout the cycle. Although our resolve has been tested over the past 12 months, our disciplined approach to underwriting and our conservative investment mix have ensured that we maintain our strong competitive position.

ABOUT LLOYD'S MANAGING AGENTS

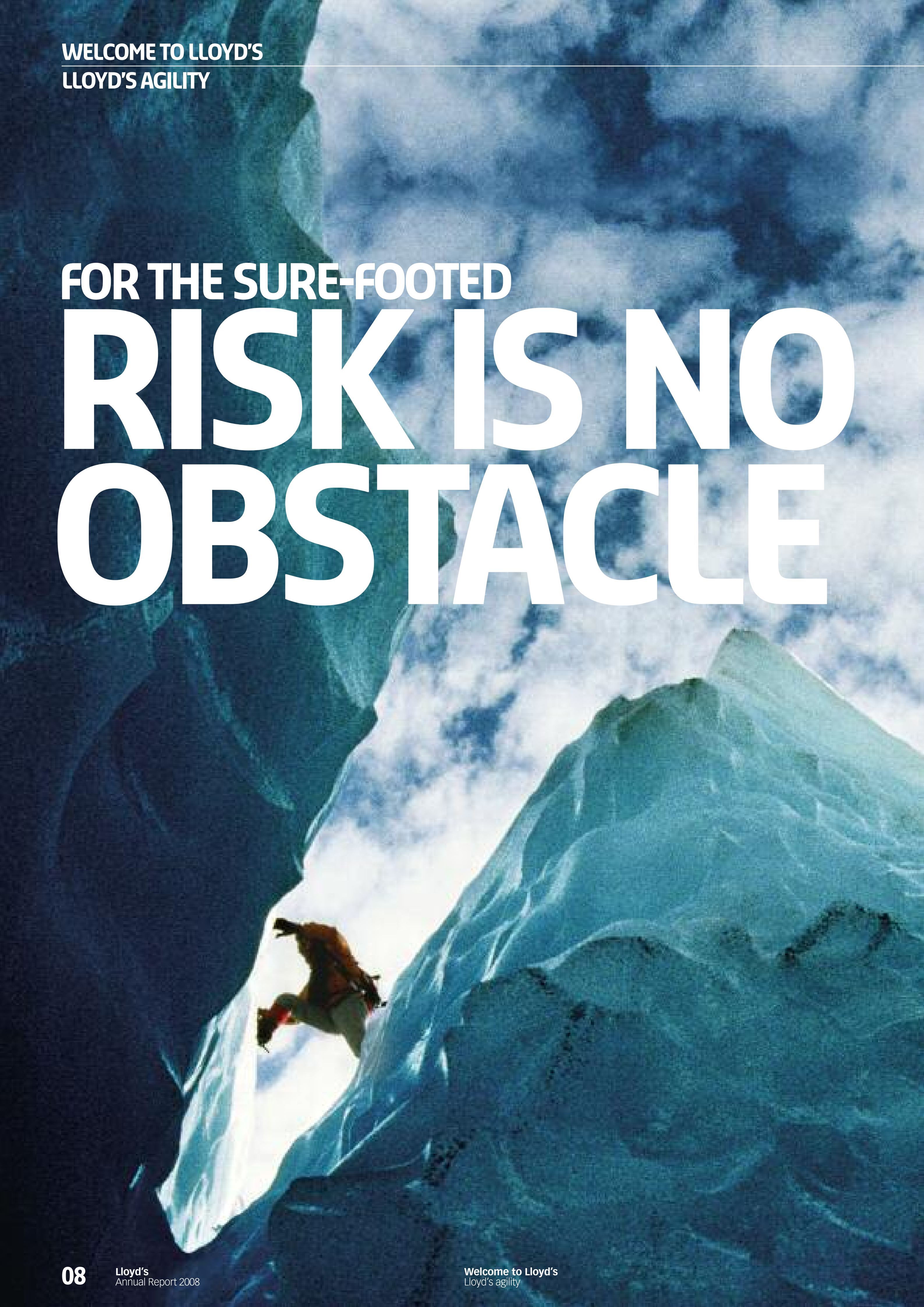
As at 31 December 2008, the Lloyd's market was home to 51 managing agents, shown below, and 80 syndicates. However, more important than sheer size is the breadth and depth of specialist broking and underwriting expertise, brought together under one roof at Lloyd's.

More information on managing agents and syndicates on page 10.

For information on Syndicate GWP see page 138.

CATLIN
HARDY
AEGIS London
CAPITA
HISCOX
AMLIN
Watkins Syndicate
FARADAY
Chaucer
HCC Underwriting Agency Ltd
Brit Insurance
STARR UNDERWRITING
MARKEL INTERNATIONAL
XL INSURANCE
ATRIUM
Pembroke Managing Agency
spectrum
HERITAGE
ADVENT
ARK
SHELBOURNE SYNDICATE SERVICES
NEWLINE
Marketform
CANOPIUS
Beaufort
OMEGA
Liberty Syndicates
CATHEDRAL
SPORTSCOVER UNDERWRITING LTD
ASPEN
Argenta
equity
TALBOT UNDERWRITING
Whittington
beazley
Sagicor AT LLOYD'S
Navigators
ACE
QBE
Novae
TRAVELERS
Kiln
MAP underwriting at Lloyd's
KGM
JUBILEE
MARLBOROUGH
Max at Lloyd's
S.A Meacock & Company Limited
Mitsui Sumitomo Insurance Group MSIG
RITC Syndicate Management Limited

FOR THE SURE-FOOTED
RISK IS NO OBSTACLE



For most businesses, risk is a threat. For Lloyd's, it's also an opportunity, because risk is our business.

Lloyd's exists to anticipate, understand and manage it. There is nothing reckless about this appetite for risk. It is based on research and analysis, experience and expertise, and a shared culture of practical common sense. It is the product of over 300 years' adaptation and innovation to meet customers' evolving needs.

That is what enables Lloyd's underwriters to work in such an entrepreneurial way. They can adapt quickly to new and emerging risks. They have a reputation for considering risks that others can't or won't accept. They provide creative solutions for end clients with unusual or hard-to-meet needs.

AN AGILE MARKET WHERE CAPITAL AND EXPERTISE JOIN TO COVER RISK WORLDWIDE.

Lloyd's is not an insurance company; it is a partially mutualised market where members 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.

SYNDICATES
WRITING THE INSURANCE

As at 31 December 2008, there were 80 syndicates at Lloyd's. They 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 our business is conducted in the Underwriting Room at One Lime Street, London, where most of the syndicates have a presence. Here, detailed negotiations take place regarding the risks brokers wish to place at Lloyd's on behalf of their clients. Most of these placements involve face-to-face negotiations, but work is under way to enhance the supporting business processes and electronic infrastructure. Some syndicates specialise in underwriting a certain class of insurance, while others write a range of classes. Having direct access to this concentration of underwriting skill gives us our excellent reputation for expertise, innovation and quick decision-making.

MANAGING AGENTS
MANAGING THE SYNDICATES

A managing agent is a company set up to manage one or more syndicates on behalf of the members who provide the capital. It employs the underwriters and handles the day-to-day running of the syndicate's infrastructure and operations. 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. For other syndicates, the capital is provided by a 'spread' of different members, who may include both individuals and corporate groups, and the managing agent may be separately owned and managed. Managing agents are also responsible for investing the syndicates' funds.

Together, the syndicates underwriting at Lloyd's form one of the world's largest specialist commercial insurance and reinsurance markets. As at 31 December 2008, there were 51 managing agents.

A list of managing agents and the syndicates they manage can be found on page 138.

How we work

		Corporation of Lloyd's		
Policyholders	Brokers Service companies	Syndicates	Managing agents	Members
Business flow				Capital provision
Risk Clients have risks that need to be insured or reinsured. They will discuss their needs with a broker.	**Distribution** Brokers: provide advice to clients, negotiate terms with underwriters and service the business during the life of the policy. 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.	**Underwriting** 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.	**Management** Managing agents provide management and other services to syndicates. They employ underwriting and support staff and provide the business infrastructure.	**Capital provision** Capital providers, called members, are the risk carriers. They support one, or a number of syndicates.

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 members' underwriting liabilities. The diverse sources of capital in 2008 are shown below.

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 34.

CORPORATION OF LLOYD'S
SUPPORTING THE MARKET

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

See page 15 for more detail on the governance of Lloyd's.

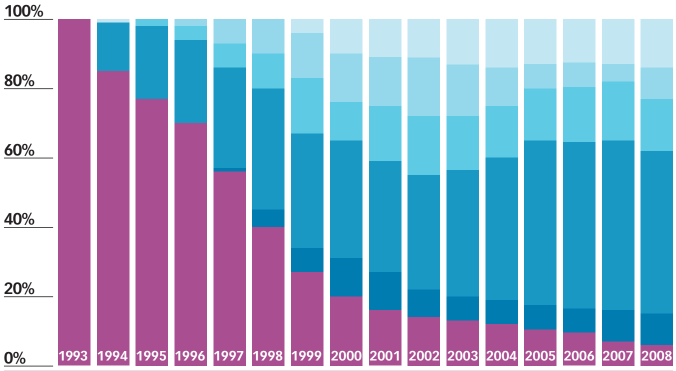
The Corporation (including its subsidiaries) had 851 employees worldwide, as at 31 December 2008.

More information can be found in People Strategy on page 44.

As well as providing cost-effective services fundamental 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:

- → Setting the level of capital that Lloyd's members must provide to support their proposed underwriting.
- → Overseeing the market's business activities 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 managing agents of underperforming syndicates to improve performance and intervening directly if stronger action is required.
- → Managing financial and regulatory reporting for the market, including the production of its results and Financial Services Authority (FSA) return.
- → Managing and developing Lloyd's global network of licences and the Lloyd's brand.

Sources of capital by type and location



	2008
Worldwide insurance industry	14%
Bermudian insurance industry	9%
US insurance industry	15%
UK insurance industry and other corporate	47%
Individual members (limited liability)	9%
Individual members (unlimited liability)	6%

STABILITY UNDERPINNED BY A STRONG CAPITAL STRUCTURE.

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 levels 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 the relevant 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 available, subject to Council approval, to meet any member's insurance liabilities.

Further information on 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 premium trust funds, and are the first resource for paying policyholder claims from 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 for future liabilities of each syndicate are subject to annual independent audit and actuarial review.

SECOND LINK
MEMBERS' FUNDS AT LLOYD'S

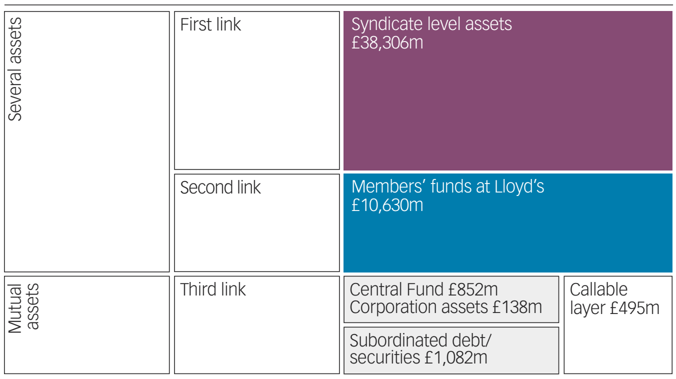
Each member, whether corporate or individual, must provide capital to support its underwriting at Lloyd's. In accordance with the FSA regime, each syndicate produces an Individual Capital Assessment (ICA) stating how much capital it requires to cover its underlying business risks at a 99.5% confidence level.

The Corporation reviews each syndicate's ICA to assess the adequacy of the proposed capital level. When agreed, each ICA is then 'uplifted' (by 35% for 2008) to ensure extra capital is in place to support Lloyd's ratings and financial strength. This uplifted ICA, known as the syndicate's Economic Capital Assessment, is used to determine the level of capital required by the syndicate's members 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.

> "In these uncertain times worldwide, there is a concern as to any company's security, whether it be an insurer or otherwise. Lloyd's provides a more secure platform than many and remains a key participant within our insurance programme."

Ken Williamson
Insurance Manager, Kier Group plc
Kier Group is a leading construction, development and service group specialising in building and civil engineering, support services, private house building, property development and the Private Finance Initiative.

Chain of security



All figures as at 31 December 2008.

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 other 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 members' desire for cost-effective mutuality of capital. In particular, the Corporation's sophisticated modelling tests each member's underwriting portfolio against a number of scenarios and a range of forecasts of market conditions. The Corporation's target for unencumbered central assets is a minimum of £1.7bn. Members' contributions to the Central Fund remain at 0.5% of gross written premiums for 2009. The Council of Lloyd's regularly reviews the central assets target and the level of contributions in light of the current financial position and forecast 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 the statutory solvency position of the Society of Lloyd's and reports this to the FSA. As at 31 December 2008, the Society had an estimated solvency surplus of £2,475m.

LLOYD'S RATINGS

The world's three leading insurance rating agencies recognise Lloyd's strengths and robust capitalisation. The Lloyd's financial strength ratings apply to every policy issued by every syndicate at Lloyd's since 1993.

In 2008, all three rating agencies affirmed Lloyd's ratings, reinforcing our resilience and the financial strength of the market.

FITCH RATINGS: A+ (Strong), Stable Outlook
STANDARD & POOR'S: A+ (Strong), Stable Outlook
A.M. BEST: A (Excellent), Stable Outlook

"Lloyd's has a strong competitive position in the global insurance market and benefits from its reputation for innovative and flexible underwriting. Its competitive strength derives from its marketplace structure that fosters the development of strong specialist underwriting skills."

A.M. Best, July 2008

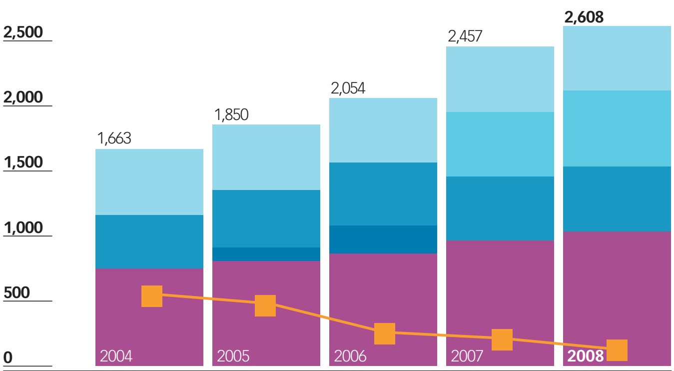
Enhancing the market's performance and credit ratings

The strategic objective of working with managing agents to ensure they are effectively managing the insurance cycle across the market is a vital part of protecting Lloyd's Central Fund. To support this objective, the Franchise Performance Directorate (FPD) launched its Performance Management Data project in 2008. This enables FPD to collect underwriting data from managing agents at risk level, allowing for more accurate monitoring of syndicates' performance against their approved business plans. By collecting more robust and accurate information, FPD will be better positioned to take decisive action if there are performance concerns about particular syndicates or managing agents.

The project has been recognised as an important factor in Lloyd's future credit ratings. Standard & Poor's September 2008 assessment of the Lloyd's market reported: "A project is currently under way to improve the granularity of the underwriting data the FPD is able to access for monitoring purposes. If successfully implemented, Standard & Poor's believes this project will further enhance FPD's ability to oversee the market's underwriting performance, which will be a key focus over the rating horizon."

Managing agents make their first data submissions in April 2009.

Corporation & Central Fund net assets†
(£m)



£m	2008
Corporation & Central Fund net assets	1,031
Syndicate loans	–
Callable layer	495
Subordinated debt issued 2004	586
Subordinated perpetual securities issued 2007	496
Solvency deficits	133

† The aggregate value of central assets of the Corporation for solvency purposes at 31 December 2008, excluding the subordinated debt liabilities, including the callable layer.

A RANGE OF RISK APPETITES, WITH EACH AREA OF POTENTIAL RISK EXPERTLY ASSESSED.

MANAGING INSURANCE RISK AT LLOYD'S

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

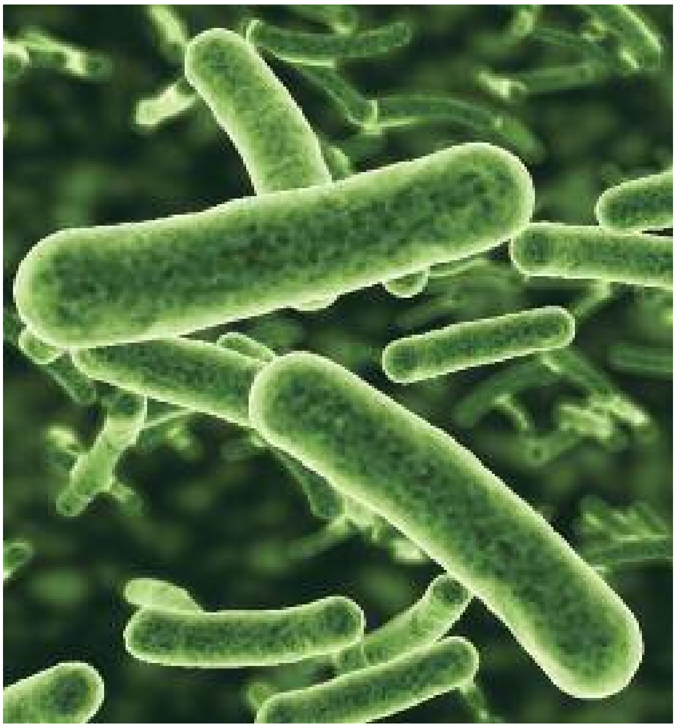
- → Setting guidelines for catastrophe exposure and reinsurance usage.
- → Devising Realistic Disaster Scenarios to assist in the measurement and management of catastrophe exposures at syndicate and market level.
- → Reviewing business plans and determining appropriate capital requirements.
- → Establishing and monitoring underwriting standards, including claims and exposure management principles.
- → From April 2009, the Performance Management Data project will enhance monitoring of syndicates' performance against approved business plans.

For more information on the Performance Management Data project please see the case study on page 13.

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



Pandemics: preparing for the next outbreak

Pandemics have tended to break out every 30-50 years. It's prudent to assume that the world will see another one – but it would be unwise to assume that this will necessarily repeat the patterns of the past.

In April 2008, the Corporation joined with XL Capital to host a conference on managing the threat of the next pandemic. Speakers from the Metropolitan Police, the Fire Service and the Department of Health came together to discuss their preparations for a pandemic outbreak, and provide guidance for the financial services and insurance world.

The Lloyd's Emerging Risks team followed-up with a report into the possible insurance impacts of a major pandemic. There are many reasons to hope that the world is better prepared, including the availability of new anti-viral drugs and global coordination by the World Health Organisation. But there are also reasons for concern, including the growth of urbanisation and global travel.

Economic impacts in today's interconnected world are likely to be severe and could have knock-on effects for insurers: in today's litigious world, legal actions against businesses shown to be unprepared could lead to claims against liability policies. This type of event, among others, could have a substantial impact on the (re)insurance industry. The conference provided a timely reminder of the importance of robust disaster planning including catastrophe and systemic risk management, and the Emerging Risks team's own close monitoring through its Realistic Disaster Scenario framework.

A STRUCTURED APPROACH TO GOVERNANCE AND REGULATION.

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.

The members of the Council and Franchise Board are listed on pages 16 and 17.

Further details on the roles of the Council, Franchise Board and their respective committees can be found on pages 86 to 88.

The day-to-day powers and functions of the Council and Franchise Board are exercised by the Corporation's Executive Team, consisting of the CEO and directors of the Corporation.

In November 2008, Parliament approved a Legislative Reform Order to amend the Lloyd's Act 1982.

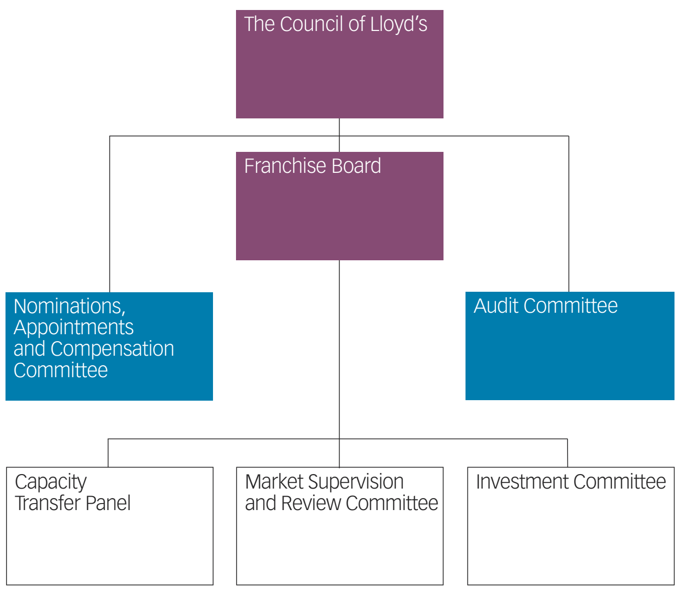
For more details of the Legislative Reform Order see page 86.

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, licences and reputation are protected.

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

For more information on corporate governance see page 86 to 88.

Principal committees of Lloyd's



GOVERNANCE
THE COUNCIL OF LLOYD'S

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 a member of the House of Lords Select Committee on Economic Affairs. 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 moved to the Lloyd's market in 1993 to help facilitate the introduction of corporate capital. He is a former Chairman of the Lloyd's Market Association Market Processes Committee.

04 **DR ANDREAS PRINDL CBE***†
Deputy Chairman of Lloyd's
(Nominated member)
Andreas Prindl worked for Morgan Guaranty in New York, Frankfurt, London and as General Manager in Tokyo and then set up Nomura Bank International, which he chaired. He was appointed CBE for his contributions to financial services education in Britain and Eastern Europe.

Council as at 23 March 2009
* Member of Audit Committee
† Member of Nominations, Appointments and Compensation Committee

05 **GRAHAM WHITE†**
Deputy Chairman of Lloyd's
(Working member)
Graham White is Managing Director of Argenta Private Capital Ltd and 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. He is Chairman of Lloyd's Charities Trust.

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 2007. 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 **MICHAEL DEENY**
(External member)
Michael Deeny is a chartered accountant and Chairman of the Association of Lloyd's Members. His career has principally been in the music industry, where he promoted U2, Bruce Springsteen, Nirvana and Luciano Pavarotti amongst others. He underwrites through a Limited Liability Partnership and is Deputy Chairman of the Equitas Trust.

08 **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 ten years. She was responsible for risk management in the assurance and advisory practice, prior to her retirement in 2003.

09 **SIR ROBERT FINCH†**
(Nominated member)
Sir Robert Finch qualified as a solicitor in 1969 when he joined Linklaters, becoming Partner in 1974 and Head of Real Estate in 1997. He retired in 2005 to take the Chairmanship of Liberty International plc for three years. He became Chairman of the Royal Brompton and Harefield Hospital in January 2009. He is a director of FF&P Russia, served as a Church Commissioner from 2003 to 2008 and was Lord Mayor of London for the year 2003/04.

10 **CHRISTOPHER HARMAN**
(Working member)
Christopher Harman 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 was the founder member and Deputy Chairman of Harman, Wicks & Swayne Ltd, which is now part of Jardine Lloyd Thompson Reinsurance Brokers Ltd. He has been an unlimited Name since 1979.

11 **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.

12 **MARTIN HUDSON**
Representative of Aprilgrange Limited
(External member)
Martin Hudson is the International Chief Executive Officer for The Travelers Cos. In this role he leads businesses in the UK, Ireland and Canada in addition to the Travelers Lloyd's managing agency. He has worked for Travelers, and St Paul Cos prior to the merger of those two companies, since 1980. He began his career in Lloyd's in 1977.

13 **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.

14 **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, The Atlantic Council and the Smithsonian Museum of American History.

15 **ALAN LOVELL†**
(External member)
Alan Lovell is Chief Executive of Infinis Limited, the UK's second largest producer of renewable energy, 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).

16 **NICHOLAS MARSH**
(Working member)
Nick 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.

17 **BARBARA MERRY**
Representative of Hardy Underwriting Limited (External member)
Barbara Merry is the Chief Executive Officer of the Hardy Group. She is a chartered accountant and has worked in the Lloyd's community since 1985, spending 14 years in the Corporation of Lloyd's, then as MD of another managing agent, before taking on her current role at Hardy.

18 **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.

GOVERNANCE
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 **NICHOLAS 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 a member of the Lloyd's Market Association Board and Chairman of the Lloyd's Community Programme Management Board.

04 **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).

05 **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 of ACE Bermuda. He has over 25 years of insurance industry experience. He is a member of the Lloyd's Market Association (LMA) Board and was Chairman of the LMA from January 2006 to June 2007.

06 **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.

07 **DIPESH SHAH OBE**
Dipesh Shah is a non-executive director of Thames Water and Kemble Water Group of Companies, Babcock International Group plc, and JKX Oil and Gas plc. He is the Chairman of the Remuneration Committee at Babcock and JKX. He is a former Chairman of Viridian Group plc and Hg Capital Renewable Power Partners LLP amongst others, and a former Chief Executive Officer of the UK Atomic Energy Authority and of various businesses within BP Group.

08 **DAVID SHIPLEY***
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. He was a member of the Council from February 2003 to January 2009.

09 **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.

10 **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 23 March 2009
* Member of Audit Committee

MOVING FORWARD WITH CLARITY AND AMBITION.

In these testing times, having a strategy that is clear and understood is crucial. Indeed it will be those businesses with clarity of vision and purpose that will stand the best chance of success.

Our rolling Strategic Plan, reviewed and tested on an annual basis, supports our aim to be the platform of choice for insurance and reinsurance buyers and sellers to access and trade specialist property and casualty risks.

Over the course of 2008, we have moved further towards this goal. Highlights include:

→ A.M. Best, Standard & Poor's and Fitch Ratings affirmed their Lloyd's security ratings of A (Excellent), A+ (Strong) and A+ (Strong) respectively.
→ A new syndicate ICA benchmarking tool delivered to replace the Risk Based Capital model as part of a wider Capital Systems Upgrade programme.
→ The launch of the Performance Management Data project which will improve the level and quality of individual risk data available from managing agents and support our strategic objectives to ensure that the market manages the cycle more effectively.
→ The Corporation and market worked together to implement the Claims Change programme, specifically the development of a claims segmentation programme, which over the next few years will deliver significant benefits to our customers through a better claims service.
→ Significant progress made in the drive to modernise the market – the functionality of the Electronic Claims File and Accounting & Settlement repositories enhanced, and their usage increased to over 90% of in-scope claims and 96% of original premiums; a new project (the Lloyd's Information Project) to streamline data capture and management started; and IBM chosen to run the pilot for the Lloyd's Exchange, a new information hub service.
→ The overseas office and trading network reviewed and restructured, and a number of new appointments made to improve our presence in key territories. In addition, new trading licences were obtained in Brazil, Poland and Austria.

From a solid base, we are seeking to further improve our competitive position and create a truly modern and sustainable marketplace. The priorities for 2009 are:

1. PERFORMANCE MANAGEMENT DATA – To collect robust and accurate risk level information in order that we can better monitor the performance of syndicates relative to their business plans and are well placed to take decisive action where there are prudential concerns. This will enhance the performance framework that has been in place since 2003 and will further help reduce the risk of a call on the central fund, in turn protecting policyholders.

2. CLAIMS STRATEGY – We will work with the market to improve the claims service to our customers, seeking to make it faster, more effective and competitive. In addition to introducing claims segmentation in the spring, we are looking more strategically at the future of claims management via the Claims Business Requirements Project.

3. E-ACCOUNTING AND INFORMATION PROJECT – Our aim is for the market to be supported by straight through processing. The use of Accounting & Settlement and Electronic Claims File has risen dramatically in the last two years and we are continuing to ensure that both processes are embedded in day to day market operations.

The Lloyd's Information Project will look at how reporting information is gathered in the market, allowing businesses more flexibility in how they collect and report information and cutting out unnecessary collation. By enabling choice in how information is provided to Lloyd's, we will improve efficiency and reduce costs.

4. LLOYD'S EXCHANGE – The Lloyd's Exchange will give market participants the ability to communicate with one another by a simple connection that imports and polices the core ACORD standards to the market. The tool is not designed to change the established way in which business is placed, but to support the electronic exchange of information in a standardised form and supplement the 'face-to-face' process that is integral to Lloyd's.

5. SOLVENCY II – Solvency II will establish new and demanding capital requirements, risk management and disclosure standards for EU insurers and reinsurers, harmonising capital setting and supervision across the EU. Planning for Solvency II's implementation is a key priority for Lloyd's in 2009.

6. EMPLOYER OF CHOICE – We continue to improve the skills of the Corporation staff and embed the right performance culture across the organisation through access to world class training and the Leadership Development Programme, which is developing future leaders within the Corporation and the market. We will also seek to continue to recruit the best talent to the market through the award winning Graduate Programme.

SUMMARY

This is an ambitious agenda, but as we move into 2009 it is more important than ever that we continue to improve our service to our customers, enhance our partnership with the market and continue to monitor the shifting global landscape so we are prepared to take advantage of opportunities as they arise.

The following section sets out in more detail how we will do that.

RICHARD WARD
Chief Executive Officer
23 March 2009

IN AN UNCERTAIN WORLD WE OFFER SUPPORT YOU CAN RELY ON

Lloyd's is famous for meeting its claims commitments.

The Lloyd's market has been built, and tested, to withstand extreme demands – such as the need to finance rapid reconstruction after major catastrophes.

Our subscription market enables large and complex risks to be shared between market participants. And its unique capital structure provides excellent financial security to policyholders.

Ratings agencies A.M. Best, Fitch Ratings and Standard & Poor's recognise this and confirmed their ratings in 2008.

Sharing and spreading risk enables Lloyd's syndicates to give clients a more innovative and tailored service – and to uphold the market's reputation for reliability in a changing, sometimes chaotic world.

IN AN UNCERTAIN WORLD, LLOYD'S IS STILL REACHING NEW MARKETS.

"We hugely value our relationship with the Lloyd's market, which has been built over the last 25 years. It is the market's ability to understand our cyclical business, to create both direct and reinsurance products to protect our diverse and evolving operations, that makes Lloyd's such an important partner to us."

Jill Clair
Director of Risk Management, Pulte Homes, Inc.
Pulte Homes, Inc. is America's most diversified homebuilder with operations spanning 27 states and 52 markets.

THE WORLD HAS CHANGED

The collapse of confidence in the banking system and the economic turmoil are events from which no industry is immune. The substantial markdown in equity values has impacted balance sheets while capital-raising has become more difficult. Profitability is being affected by falling investment returns, making prudent underwriting even more crucial. The global recession will also have an effect on the claims environment. These are uncertain times for the insurance industry, but Lloyd's remains well-placed to meet these challenges.

A DETERIORATING CLAIMS ENVIRONMENT

After two relatively benign years, 2008 saw the return of significant catastrophe and large risk losses. Hurricanes Ike and Gustav proved more costly than many insurers and modelling agencies first anticipated. Once again, the energy market was hit disproportionately hard. Aside from the increase in severity of losses, 2008 also witnessed an increase in attritional claims frequency. This is a trend that is expected to quicken due to the economic downturn.

The full impact of the recession is beginning to materialise in 2009 and will continue through to 2010.

An acceleration of claims has been predicted extensively although the industry's response to this deteriorating risk environment, for example through more prudent risk pricing, has been mixed so far.

PRUDENT CYCLE MANAGEMENT REMAINS KEY

Softening premium rates and/or policy terms were the norm across most lines of business during 2008 with market conditions near, or at, the bottom of the insurance cycle. In the wake of the financial turmoil, by the end of the year several commentators were hopeful for a rapid improvement in fortunes during 2009. In practice, however, the January renewal season did not herald the sea-change in rates across the board that had been hoped for, and a level of uncertainty still persists in many lines.

Reinsurance rates are showing signs of improvement in the wake of increasing demand as some insurers, facing new capital pressures, seek greater reinsurance coverage. Elsewhere, the hurricanes are expected to have a positive impact on rates in the energy market in 2009.

The aviation market began to stabilise by the end of 2008. Some major accounts showed modest rate increases, although the global economic situation is having a depressing affect on demand as some airlines reduce their fleets.

SOME GOOD NEWS FOR THE SUBSCRIPTION MARKET

The recent financial turmoil has further reinforced the advantages to insureds of spreading their risk cover through the subscription market. This trend should be particularly beneficial to the Lloyd's market, where efficient syndication of risk can be achieved.

RECAPITALISATION

The decline in asset values, poor investment returns and falling underwriting returns, all arising from the economic downturn, are having an effect on capital requirements. A real or perceived weakening capital position that is believed to be spreading from the banking industry to the insurance sector has led to some insurers looking to raise new equity to increase confidence and safeguard themselves against the uncertain times ahead. A further worrying trend has been the falling sterling exchange rate that may raise issues for global insurers with a sterling capital base but who pay a large proportion of claims in other currencies.

The diversity of capital providers at Lloyd's has been described on page 11. In addition to traditional capital markets, there is a flexible supply of private capital that may be available to businesses to finance their underwriting operations.

UNCERTAIN TIMES AHEAD

The general prognosis for the global insurance industry is that a period of uncertainty will persist while the consequences of the traumatic events of 2008 continue to play themselves out. At such times, maintaining financial strength and prudent cycle management are key priorities for insurers.

GLOBAL ECONOMIC AND ENVIRONMENTAL TRENDS

Global economic and financial conditions deteriorated rapidly in 2008. The crisis that started as a credit crunch led to a string of high profile failures in the financial sector and a tightening of the money and credit markets around the globe.

The severity of the financial crisis and its impact on the wider economy prompted governments from the largest economies to fund rescue and stabilisation measures on an unprecedented scale. In addition, efforts to stimulate economic activity and avoid a prolonged recession are leading to higher levels of public spending and intervention in economies around the world.

The global economic slowdown has already increased claims frequency and costs. Looking ahead, recession in key developed economies and slower growth in emerging economies could reduce demand for insurance. Volatile and modest investment returns will also impact performance, further emphasising the need for prudent underwriting discipline.

The world is becoming a riskier place, in a number of ways:

- → The effects of climate change are already being observed. There is evidence of rising sea levels in many areas of the planet and coastal flooding is an increasing threat.
- → Natural and man-made disasters are increasing in frequency and severity.
- → The more litigious environment is creating a greater risk of liability exposure.
- → Technology and innovation are advancing so fast that companies may find it difficult to keep pace with the legal implications. For example, the risks posed by nanotechnology remain largely unforeseeable and unquantifiable.

These developments present threats but also opportunities for the Lloyd's market. For example, more frequent disasters highlight the importance of insurance and reinforce Lloyd's role as a specialist insurance provider.

Paying hurricane claims even faster

Catastrophes such as hurricanes pose the ultimate test of whether an insurer can deliver its core client promise to pay promptly. The sheer number and wide-ranging nature of claims present formidable logistical challenges if they are to be investigated, evaluated and settled in a timeframe acceptable to clients whose lives and businesses may have been devastated.

Lloyd's was widely praised for its performance in resolving claims arising from Hurricanes Katrina, Rita and Wilma in 2005. In late summer 2008 we were tested again, as the Gulf of Mexico was hit by Hurricanes Gustav and Ike – two of the most ferocious hurricanes ever recorded in that region. They provided our first real opportunity to respond to a large-scale catastrophe since introducing our Claims Management Principles and implementing Electronic Claim Files.

Over comparable timescales, analysis of our claims data shows that we have paid twice as many of the claims from Gustav and Ike as we did with the 2005 claims. This demonstrates how our continuing commitment to drive up performance standards can help improve our service to clients.

BUSINESS ENVIRONMENT
INSURANCE TRENDS CONTINUED

New tax regime enhances Lloyd's competitiveness

For any financial centre, its tax regime is an important element of its overall competitiveness. In March 2006, the UK Government announced its intention to strengthen London's position as the world's leading international financial centre. Since then, the Corporation has been lobbying the Government to establish conditions in which Lloyd's can continue to compete globally against new businesses operating in jurisdictions such as Bermuda and Ireland with more favourable tax regimes.

In its November 2008 Pre-Budget Report, the Government announced that it will bring the tax treatment of Lloyd's corporate members' technical reserves into line with that of general insurers by introducing a claims equalisation reserve for tax purposes only. Little detail is available at present on precisely how this will work, except that it will replicate as closely as possible the rules for general insurers – allowing amounts to be transferred into the Claims Equalisation Reserve in profitable years and released when an 'abnormal loss' occurs. The effect is to reduce the volatility of the tax result. This means that Lloyd's will not be required to recognise the Lloyd's Claims Equalisation Reserve for solvency purposes and Lloyd's solvency calculation and levels of capital will, therefore, be unaffected.

The new regime is expected to apply to profits arising in the year ended 31 December 2008. During 2009 the Corporation will be working closely with HM Treasury and HM Revenue & Customs on the detail of the regime, as well as discussing other issues that could impact on Lloyd's competitive position.

EMERGING MARKETS AND INTERNATIONAL AND REGIONAL TRADING CENTRES

In 1998, the GDP of the G7 countries represented 50% of world GDP; by 2008 this had fallen to 42%. Clearly, emerging markets present new opportunities for the insurance industry – but also challenges as to how best to access them. The Corporation continues to work closely with the market to examine how Lloyd's can best develop presences in the Middle East, South America and Eastern Europe.

See page 27 for more information on Lloyd's international reach.

DISTRIBUTION

As local insurance markets develop and cost pressures drive brokers and insurers to seek more cost-effective distribution channels, complex commercial insurance business will increasingly tend to stay in local markets that can develop their underwriting capabilities. Together with changes in brokers' business models – for example, consolidation or the development of regional insurance hubs – this could change the way in which business flows to the Lloyd's market.

Changes to the Lloyd's Act 1982 through the Legislative Reform Order now enable non-Lloyd's brokers to deal directly with managing agents. New arrangements are in place to ensure that minimum standards apply to all brokers placing business directly in the market.

The Franchise Board has agreed a distribution strategy to enable the Lloyd's market to adapt and continue conducting business through diverse distribution channels. The London market and the close relationships between managing agents and Lloyd's brokers will continue to be at the core of the distribution strategy, which is focused on:

- Delivering simple, cost-effective controlled access to the Lloyd's market.
- Applying the same minimum prudential standards for both Lloyd's and non-Lloyd's brokers dealing directly with the market.
- Identifying market development opportunities in co-operation with managing agents and brokers.
- Providing relationship management support for brokers and coverholders.
- Enhancing the attractiveness of Lloyd's overseas trading centres.

TAX

The UK tax regime is making it increasingly difficult for the Lloyd's market to compete with insurers and reinsurers in other jurisdictions. The Corporation has been discussing tax-deductible claims equalisation reserves with the Government for some time, and in his Pre-Budget Report the Chancellor of the Exchequer in November 2008 announced the Government's intention to introduce a claims equalisation reserve for Lloyd's members. We welcome this, as it enhances our ability to compete globally.

The Corporation is now discussing the details with the Treasury. It also continues to lobby on other ways to improve the competitiveness of the UK tax regime, including a reduction in the rate of corporation tax.

More information on claims equalisation reserves can be found in the case study, left.

ONGOING REGULATORY CHANGE

The insurance industry will experience significant regulatory change in the coming years as a result of legislative initiatives at global, regional and national level.

At a global level, the International Association of Insurance Supervisors (IAIS) continues to produce global standards, principles and guidance on a wide range of regulatory issues such as reinsurance, solvency, mutual recognition of different regulatory regimes and corporate governance. These initiatives should lead to greater convergence of national regulatory rules and a reduction in conflicting and duplicative laws for insurers and reinsurers trading internationally.

The EU continues to be very active in considering initiatives affecting insurance – the most significant being the proposed Solvency II directive. This seeks to create a harmonised, risk-based approach to supervision and capital requirements in the EU. It is also likely to have a substantial influence on the IAIS's work on global standards.

The detailed content of the Solvency II regime, which is scheduled to be implemented throughout the EU by October 2012, is still being developed and discussed. The Franchise Board supports the Solvency II objectives and, in close cooperation with managing agents, will work to ensure that the market is ready for implementation. Increased market engagement on the detail of Solvency II is a key priority.

In the US, the National Association of Insurance Commissioners (NAIC) has put forward its Reinsurance Regulatory Modernisation Framework Proposal for full adoption. If implemented, this will significantly relieve the current onerous collateral requirements applying to non-US reinsurers. The NAIC is likely to seek a federal mechanism to ensure uniform implementation across all states, and Lloyd's continues to lobby for regulatory reform both at the NAIC and in Washington.

At a national level the recently published Turner review and accompanying FSA discussion paper on "a regulatory response to the global banking crisis" signals the FSA's intent to introduce a much more intrusive regulatory approach to its UK supervised firms, not just those in the banking sector, and also raises wider issues about steps the international community needs to take to raise regulatory standards, supervisory approaches and international cooperation and coordination.

The UK Law Commission's work on the modernisation of insurance contract law will also have an impact on the industry. Working with the Lloyd's Market Association, the Corporation will continue to review and comment on the Law Commission's proposals.

The turmoil in the financial markets may prompt some politicians and regulators to make a case for more national, protectionist policies. This could threaten the trend towards greater harmony of insurance regulation. Lloyd's will continue to argue for close co-operation between regulators to foster a common approach that reflects the global nature of the insurance industry.

Operational improvements boost customer satisfaction

It takes time to change the market but modernisation is crucial to ensuring Lloyd's remains the platform of choice. In 2008 good progress was made on several important change projects.

Contract Certainty is now embedded as part of the underwriting process and customer feedback is more positive. The annual Customer Satisfaction Survey, covering brokers, coverholders and policyholders, was launched in 2005. By 2008, it showed a 40% improvement in satisfaction with speed of contract documentation. Performance was maintained throughout 2008, and the number of outstanding legacy policies continued to reduce. By the year end, fewer than 12.5% remained outstanding, against a target of under 20%.

The proportion of new in-scope claims using Electronic Claims Files in the market is now consistently above 90%. A process for handling legacy claims – originally paper based and currently out of scope – has been agreed and will increase the number of claims being dealt with electronically. Since the system was introduced, customer satisfaction with claims settlement has been consistently and significantly above pre-introduction levels.

Since mid 2008 over 90% of original premiums have been constantly processed electronically via Accounting and Settlement, and this is an important first step in modernising the flow of money in the market. The next step is the Lloyd's Information Project, which will provide choice of operating model, enabling faster movement of cash and more efficient reporting.

In 2009 we begin a pilot of the Lloyd's Exchange. This will give market brokers and managing agents a simple, standardised electronic messaging exchange, replacing the multiple communication platforms currently in use and ensuring a single standard for information transfer.

BUSINESS ENVIRONMENT
INSURANCE TRENDS CONTINUED

CONVERGENCE OF CAPITAL MARKETS AND INSURANCE MARKETS

Before the dislocation in the financial markets, banks were showing some strategic interest in developing insurance risk as an asset class. There was also the possibility that significant players in the capital markets could seek to participate in the (re)insurance markets. While recent events have probably brought about a reappraisal on the part of the capital markets, the Corporation will continue to monitor financial institutions' strategies for the (re)insurance markets. The use of capital market risk transfer products continues to attract interest from specialist capital market investors and reinsurers alike, including some Lloyd's businesses, although the uptake has not been significant in 2008.

MARKET OPERATING ENVIRONMENT

As part of a global industry, Lloyd's must stay comparable to other markets in terms of the ease, time and cost of doing business. Progress has been made to improve process efficiency and work will continue to build on the market's achievements in delivering a streamlined, flexible, technology-backed operating model that attracts business to Lloyd's.

The Corporation is sponsoring a new service, the Lloyd's Exchange, which will allow market participants to transfer risk information using electronic messaging standards. This will be piloted in 2009 and rolled out to the market in line with demand. It has the support of the LMA, the London broker community and the International Underwriting Association. Market-wide adoption of this facility is regarded as an important step in achieving further process efficiencies for Lloyd's and the London market.

Work to improve claims settlement is also making progress. The current focus is on segmenting and handling claims in a more tailored way according to their complexity. The Corporation and the LMA are working together to review the market's future business requirements for claims and gain a better understanding of the processes and IT support needed in the long-term.

Many of the market's support functions are currently provided by a major outsource provider. The Corporation recognises that technological advances provide an opportunity to rethink processes and introduce greater choice. Consultation with the market will continue so that an agreed approach can be found.

The Corporation will work with the LMA, the London and International Insurance and Reinsurance Brokers Association, the Market Reform Group, ACORD and other stakeholders to ensure that the market as a whole continues to move forward and embrace change.

More information on operational improvements can be found in the case study on page 25.

> "In my own experience with Lloyd's, their attitude towards claims settlement is what any buyer hopes it would be. They are practical, fair and are often the first to come to an agreement about claims and make a payment. This is invaluable both in terms of cash flow and to get the ball rolling on a placement involving several participants."

Virginia Lawson
Risk Manager, Century Aluminum
Century Aluminum owns primary aluminum capacity in the US and Iceland, as well as an ownership interest in alumina and bauxite assets in the US and Jamaica.

BUSINESS ENVIRONMENT
LLOYD'S INTERNATIONAL REACH

Lloyd's has an extensive global licence network, with licences to write direct insurance business in 80 jurisdictions and the ability to conduct reinsurance business in over 200 countries and territories. Our licences are supported by offices worldwide – ranging from third-party legal representatives who maintain the licences, to larger offices with country managers who maintain the licences and play a significant market development role.

During 2008, significant steps were taken to strengthen Lloyd's international trading position. These included appointing new staff, acquiring new licences and negotiating enhanced trading arrangements for Lloyd's syndicates. New resources were provided to support managing agents' decision making:

- → **Global Opportunities**: A tool for scanning insurance markets and assessing their potential for future licence development.
- → **Regional Watch**: An information tool for monitoring insurance environments and Lloyd's premiums in over 50 insurance markets.
- → **Crystal**: Interactive guidance on regulatory requirements around the world.
- → **Lloyd's International Trading Advice desk**: Based in the Underwriting Room, offering managing agents and Lloyd's brokers advice about Lloyd's international licences.

NORTH AMERICA

North America is Lloyd's biggest market. With a long-established presence and offices in New York, Illinois, Kentucky and Montreal, Lloyd's is also represented in Los Angeles and the US Virgin Islands.

During 2008, Lloyd's lobbied for changes to regulations that require collateralisation of gross liabilities for strong and well-regulated reinsurers. Lloyd's welcomes the changes which have so far been approved by the National Association of Insurance Commissioners.

Lloyd's plans to open a permanent office in Toronto in the next 12 months, subject to market conditions, and will also be reviewing Canadian coverholder requirements.

LATIN AMERICA

In April 2008, Lloyd's was approved as the first 'Admitted' reinsurer in Brazil. Lloyd's expects to open an office in Brazil in April 2009. Lloyd's also has representatives in Argentina, Belize and Chile.

EUROPE

Lloyd's has an extensive network in Europe's major insurance markets, with established offices in France, Germany, Italy, Spain and Switzerland. In 2008 new offices were opened in Ireland and Poland.

In 2009 Lloyd's has obtained approval for an establishment licence for Portugal, is working to obtain an establishment licence in the Czech Republic, and will explore options to obtain a new trading licence in Turkey.

INDIA, MIDDLE EAST AND AFRICA

Lloyd's is closely monitoring opportunities in these areas for future development.

ASIA AND PACIFIC

Lloyd's has a number of established offices in Australia, Hong Kong (SAR) and Singapore. We are exploring options to obtain new licences or improved trading positions in South Korea and Vietnam.

- → **China**: Onshore reinsurance business is written via Lloyd's Reinsurance Company (China) Ltd (LRCCL). Currently, there are five syndicates with underwriters based in China and we are encouraging more participation.
- → **Japan**: With significant reinsurance business sourced from Japan, Lloyd's is developing a more flexible operating model to facilitate the writing of insurance business via Lloyd's Japan.
- → **Singapore**: Singapore is fast becoming a hub for specialist non-life (re)insurance in the Asia Pacific region. There are currently 14 syndicates with further syndicates expected to join in 2009. Lloyd's has been working with regulators and market participants to make business and compliance processing more efficient.

More information on Lloyd's international reach can be found inside the fold-out front cover.

For more information on Lloyd's licences worldwide visit: www.lloyds.com/worldwide

Strengthening our position in Europe and Brazil

In consultation with managing agents, Europe has been identified as a key region for Lloyd's future focus; and in 2008 a series of initiatives were commenced to strengthen our presence across the region. New offices were set up in Ireland and Poland, licences obtained to conduct binding authority business through coverholders and service companies in Poland and Austria. And a further application was submitted for Portugal. To enhance the existing structure a market development manager was appointed in the German office and the first Nordic Area manager, based in Stockholm, will work closely with existing representatives in Norway, Sweden and Denmark to develop the Scandinavian market.

Outside Europe, Lloyd's has benefited from a significant change in the way reinsurance business is regulated in Brazil. In April 2008, Lloyd's became the first reinsurer to be granted 'Admitted status', now permitting the market to underwrite Brazilian reinsurance business. As a catastrophe free region, we believe that obtaining access to this market is a significant step forward for Lloyd's. The new Rio de Janeiro offices are scheduled to open in April 2009.

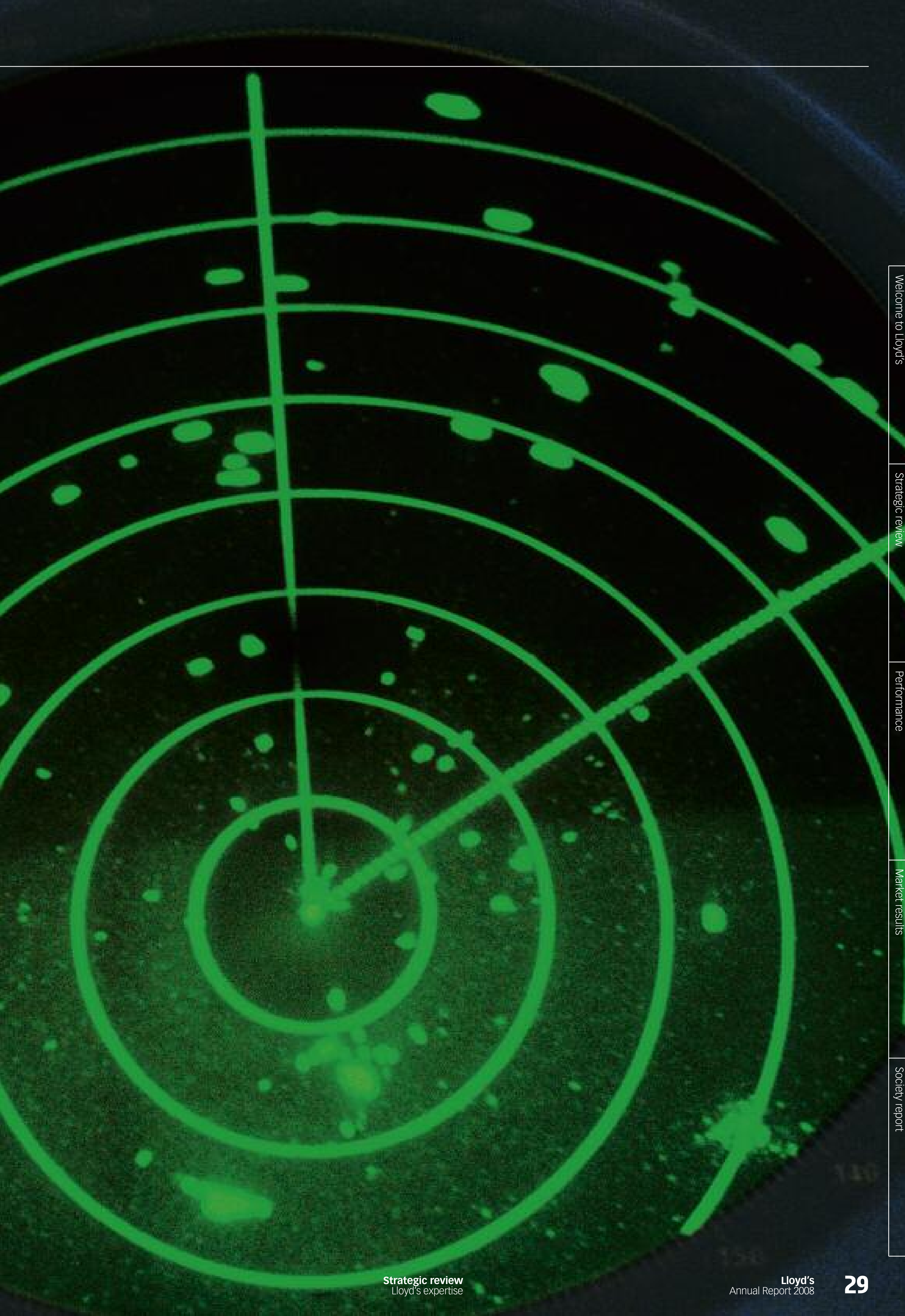
Lloyd's monitors, measures and anticipates risk continually, so that our underwriters can assess evolving challenges and address them. We share our thinking with the wider community to provide a catalyst for debate and adaptation.

The risk landscape is constantly changing. New threats can take shape in the laboratory, the street or the stratosphere. So Lloyd's set up 360 Risk Insight to analyse them as they emerge: recently it has considered climate change, terrorism and political risk, and corporate liability.

Lloyd's refines the market's response capability using Realistic Disaster Scenarios. And new techniques are developed, such as an online flood risk assessment tool to improve managing agents' control of flood risk exposures.

Initiatives like these underpin Lloyd's reputation for expertise and innovation, enable underwriters to make quick decisions when the need arises, and help the market to prepare for whatever challenges emerge.

LEADERSHIP CALLS FOR ALL-ROUND VISION



STRATEGY
PLATFORM OF CHOICE

LLOYD'S STRATEGY IS TO DELIVER THE PLATFORM OF CHOICE FOR SPECIALIST INSURANCE AND REINSURANCE BUSINESS.

VISION

The vision for Lloyd's is:

To be the platform of choice for insurance and reinsurance buyers and sellers to access and trade specialist property and casualty risks.

Lloyd's strategic direction and our aspiration to be the platform of choice remains unchanged. The Franchise Board's business focus continues to be to make Lloyd's the preferred market for specialist insurance and reinsurance business, irrespective of size or nature.

BENEFITS

The five principal benefits of operating at Lloyd's, as detailed below, remain valid. The first three benefits have broadly been delivered. On the other two – market access and the operating environment – progress has been made but more still needs to be done, as described on the following pages.

1 PERFORMANCE NETWORK →	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.

DEFINING CHARACTERISTICS

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 Strategic Plan period (2009-2011) 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 managing agents and capital providers who wish to participate at Lloyd's.
- Lloyd's is a disciplined marketplace where the standards of the best businesses will become those of the market as a whole.
- 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.

LLOYD'S OFFER TO PARTICIPANTS

For market participants, the attractions of operating at Lloyd's will be:

- **Managing agents:** A core central offer of security, market access and standards, plus flexible tools and services that can be used to execute individual strategies.
- **Brokers and policyholders:** A secure market bringing together diverse participants with differing strategies and risk appetites, where policyholders benefit from Lloyd's reputation and service quality.
- **Capital providers:** An opportunity to participate, within a capital efficient framework, in businesses with the ability to maximise their performance in the specialist insurance market.

For more information on Lloyd's value to market participants see page 34.

MANAGING THE CYCLE

The Franchise Board's major priority remains to work with managing agents to maintain prudent underwriting discipline during a period of changing market conditions.

Under the franchise model, managing agents have the primary responsibility for running their businesses in a proper and profitable manner. They are independent businesses with freedom to participate in whichever types of business they choose, provided they operate in accordance with an agreed business plan.

The Corporation will continue to work with agents to raise performance levels. Specifically, the Corporation will continue to review and critique syndicate business plans and monitor managing agents' performance against these plans. In addition, managing agent or syndicate specific reviews will be undertaken where underperformance has been identified. Thematic reviews impacting more than one managing agent will also continue.

While the Franchise Board is focused on working with managing agents to manage the soft cycle, it recognises that the market must be ready to respond to a market-turning event.

WORKING WITH THE MARKET

THE ROLE OF THE CORPORATION

Successfully delivering the platform of choice requires the Corporation and market participants to work together.

The Corporation's main function is to lead or support changes to ensure the Lloyd's market operates in the most commercially attractive and efficient manner. Close liaison and collaboration with market participants, particularly through the Lloyd's Market Association and London & International Insurance Brokers' Association, will continue to be key features in the delivery of the strategic priorities. Consultation with members' agents and capital providers, through their representative organisations, will also continue where appropriate.

VALUE ADDED SERVICES

The Corporation provides support services to the market either for the benefit of a specific stakeholder group – for example, providing tax advices to assist capital providers completing their UK tax returns – or to make the transaction of insurance at Lloyd's more efficient, such as the central settlement of insurance transactions between market participants.

The Corporation keeps these services under review as well as the potential for new services, where there is a sound commercial case and market demand.

A full version of the Lloyd's Strategic Plan is available at www.lloyds.com/strategy

STRATEGY
OUR PROGRESS

This table describes the features of Lloyd's five principal benefits, highlights progress against 2008 priorities and sets out our 2009 priorities to maintain and improve these benefits.

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. → 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. → Provision of data and analysis that allows managing agents to benchmark, plan, measure and manage their business. → A framework for expert management of complex and subscription claims to further enhance the market's claims handling capability.
2 CAPITAL ADVANTAGES	→ Risk-adjusted capital-setting process, based on the FSA's ICAS regime, that reflects the level of exposure of 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 standalone basis. → The cost of maintaining Lloyd's mutual assets targeted to average less than 1% of gross written premiums across the insurance cycle.	→ A capital framework that actively helps managing agents access 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, necessary ratings maintained throughout the insurance cycle.	→ 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 licences and reduce the burden on individual managing agents. **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.	→ Trading centres in international markets open to local capital providers as well as existing capital providers. **Market support** → Proactive market development in partnership with managing agents and a network of international offices that provide support services. → Access to world-class market intelligence on major international markets. **Brand** → A leading global brand and reputation, which help managing agents to win and retain preferred business.
5 OPERATING ENVIRONMENT	**Service and cost** → Fast, expert service from quotation through to claims settlement. → Brokers and other producers can deal easily with Lloyd's underwriters, using simple, streamlined processes with costs comparable to other markets. → 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 efficient conduct of business in the market. → Centrally sponsored, value-added services and tools which support high quality, efficient transaction of business.

2008 PRIORITIES	PROGRESS IN 2008	PRIORITIES FOR 2009
→ 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 project to acquire better performance data from the market to improve understanding of underwriting conditions.	→ Existing underwriting standards reviewed. Additional guidance on benchmark pricing published to the market and available on lloyds.com. → Further enhancements to business information tools completed, enabling better review of syndicate business plans. → Performance Management Data (PMD) project progressed to pilot stage.	→ Work with the market to improve underwriting discipline. → Deliver PMD to ensure information is available for the 2010 business planning exercise. → Complete implementation of the Claims Change Programme and agree and implement long-term priorities to improve claims process. → Identify options to help managing agents respond quickly to a market-turning event.
→ 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.	→ ICA review process and timetable now more flexible and tailored to the performance and characteristics of individual businesses. → New syndicate ICA benchmarking tool developed. → Decision taken to maintain the Central Fund at current levels so that Lloyd's remains well placed during a period of soft market conditions.	→ Maintain dialogue with the FSA and the EU to influence the outcome of Solvency II, and review the draft Level 2 'implementation measures'. → Work with the FSA, LMA and managing agents to ensure internal solvency capital models are being developed. → Complete the new Society ICA model and Market Capital Allocation Tool systems. → Review the level of capital flexibility afforded by the current strong Central Fund.
→ 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 with stakeholders to ensure they continue to meet market needs.	→ A.M. Best, Fitch Ratings and Standard & Poor's affirmed their Lloyd's ratings of 'A', 'A+' and 'A+' respectively during 2008. → Review confirmed that Lloyd's ratings are at an appropriate level.	→ Maintain ratings at the appropriate level. → Ensure rating agencies are fully conversant with the Lloyd's market's enterprise risk management framework.
→ Develop, maintain and exploit Lloyd's trading rights – eg develop Lloyd's trading position and presence in key territories such as India, Brazil and the Middle East. → Offer market support to exploit business opportunities – eg align Lloyd's overseas office network to support business development. → Continue to promote Lloyd's brand and reputation. → Develop access routes – eg deliver improvements in service company and coverholder distribution channels.	→ Lloyd's approved as an admitted reinsurer in Brazil and a new office opened in Rio de Janeiro. Lloyd's continues to monitor the situation in India and the Middle East to develop a presence when the time is right. → New Heads of North America and China appointed. New country managers appointed for Brazil, Canada, Ireland and Poland. Market relations manager recruited for Germany and Austria. → Work ongoing to improve the operational effectiveness of Lloyd's overseas trading centres. → Positioning as industry thought leader maintained – eg through the 360 Risk Insight project (visit www.lloyds.com/360 for details).	→ Monitor and respond to regulatory developments in US, Canada and other territories; engage with policy makers to maintain and improve Lloyd's trading position. → Explore options to obtain new licences in territories where there is a clear opportunity and market support. → With input from stakeholders, review the market development strategy for the US. → Enhance attractiveness of Lloyd's trading centres in Singapore, China and Japan. → As part of the distribution strategy, develop effective and tailored relationships with managing agents, brokers and coverholders. → Continue the 360 Risk Insight project to raise awareness of emerging industry issues.
→ Promote excellent service and reduce costs, eg – Work with the market to ensure 100% usage of Electronic Claims Files (ECF) and Accounting & Settlement (A&S) repositories. – Develop further solutions to simplify 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.	→ Increased market use of the A&S and ECF repositories: 90+% of in-scope claims and 96% of original premiums processed using the Insurers' Market Repository (as at December 2008). → Project initiated to identify potential improvements to information reporting for market participants. → Following an extensive selection process, IBM has been engaged to provide a messaging hub service (the Lloyd's Exchange) enabling market participants to send risk information using ACORD standard electronic messages. → Tactical changes made to improve support to systems and processes in Singapore, Canada, Kentucky and Illinois. → Work is ongoing with ACORD to formalise Lloyd's information needs into their messaging standards.	→ Ensure the ECF and A&S repositories are embedded in day-to-day market operations and deliver improvements as required. → Simplify market trading relationships through a pilot for the Lloyd's Exchange; if successful, roll out across the market and encourage take-up. → Review the means by which Lloyd's gathers information and eliminate duplication and redundancy. Simplify and design options for future information collection. → Working with the market, review the central servicing model and by clearly splitting out Lloyd's information reporting requirements, design and agree a new operating model that can be used worldwide. → Develop lloyds.com as the single market interface for information, services and reporting.

STRATEGY
VALUE TO MARKET PARTICIPANTS

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

	BENEFITS
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 return 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.

CAPITAL PROVIDERS	MANAGING AGENTS	BROKERS AND POLICYHOLDERS
→ The confidence that managing agents are meeting minimum standards and consequently reducing the volatility of their performance.	→ 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 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.	→ 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.
→ The ability to earn improved returns on capital as a result of the ratings and the better quality business that they attract.	→ 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 opportunity to obtain attractive returns from an investment in a bespoke portfolio of global insurance risks.	→ 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. → Coverholders will have simple, efficient and controlled access to the Lloyd's market. → Brokers and coverholders will benefit from a tailored relationship management approach (this will also include key local brokers).
→ More transparent, automated processes, supported by improved management information will reduce managing agents' operational risk, making Lloyd's more attractive.	→ 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. Brokers will be able to carry out some activities without the need for face-to-face interaction

MEASURABLE PROGRESS TOWARDS OUR STRATEGIC GOALS.

Key performance indicators (KPIs) are important measures used by the management team for evaluating the performance of both the Lloyd's market and the Corporation. Lloyd's uses a range of metrics internally for tracking and performance management. Those shown here best illustrate Lloyd's financial performance and progress in delivering our 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

For more information on the market's performance see pages 56 to 67.

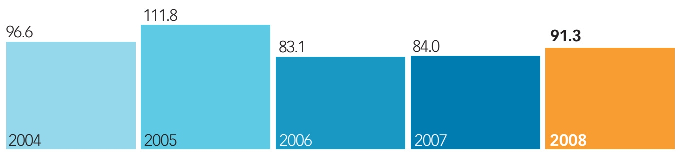
Combined ratio

%

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

Rationale Headline financial indicator for measuring underwriting performance.

Progress A solid performance in 2008. Increases in catastrophe losses and attritional claims have been offset by currency movements and releases on prior years.



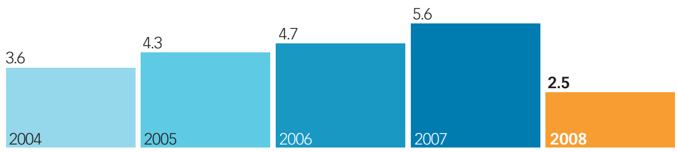
Investment return

%

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 A positive return of 2.5% reflects the conservative investment strategy in an exceptionally volatile year.



STRATEGIC PERFORMANCE

For more information on strategy see page 30.

Solvency deficit

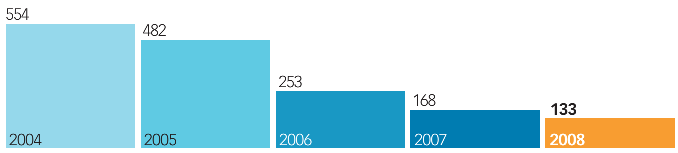
1 PERFORMANCE FRAMEWORK

Definition The aggregate shortfalls for all members where the members' assets are insufficient to cover their 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 2005.

£m



Cost of mutuality

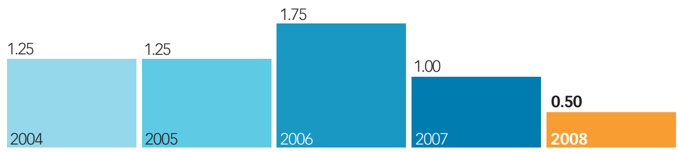
1 PERFORMANCE FRAMEWORK

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 and 2009 contribution rate of 0.5% represents a cost effective benefit of mutuality to members.

%



Pre-tax return on capital

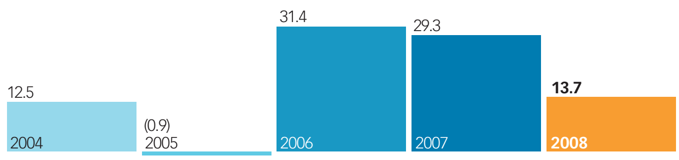
2 CAPITAL ADVANTAGES

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 with other insurance markets. The Franchise Board and Council aim to support the market in monitoring cross-cycle returns to all capital providers.

Progress A return of 13.7% is a solid performance in a difficult year for the financial sector.

%



Financial strength rating

3 SECURITY AND RATINGS

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

Rationale Indicates the strength of Lloyd's rating offering.

Progress Lloyd's ratings from all three ratings agencies are at the target level and were affirmed in 2008.

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

Brand strength

4 MARKET ACCESS

Definition Non-financial indicator, based on biennial independent survey of brokers and policyholders. The 'brand health' score is a combination of scores for awareness, familiarity, favourability, trust and endorsement. It is an index which tracks relative changes in perception over time.

Rationale A leading global brand and reputation help 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. Updated results will be available mid 2009.

Brand index score. Survey conducted biennially. Next results due mid 2009.

Customer satisfaction levels

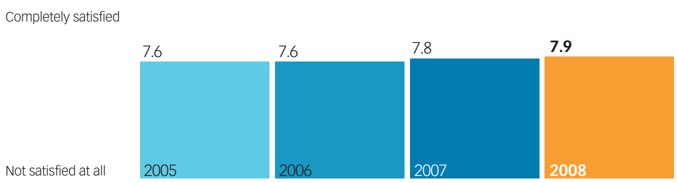
5 OPERATING ENVIRONMENT

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 to 7.9 in 2008, driven predominantly by improvements in satisfaction with speed of contract documentation, speed of quotation, process to notify of a claim and speed of claims payments.

Average score out of 10



Managing agent satisfaction levels

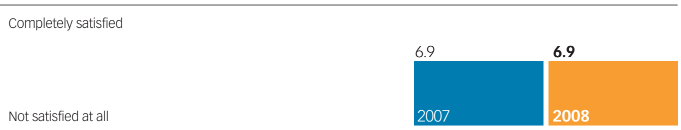
5 OPERATING ENVIRONMENT

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

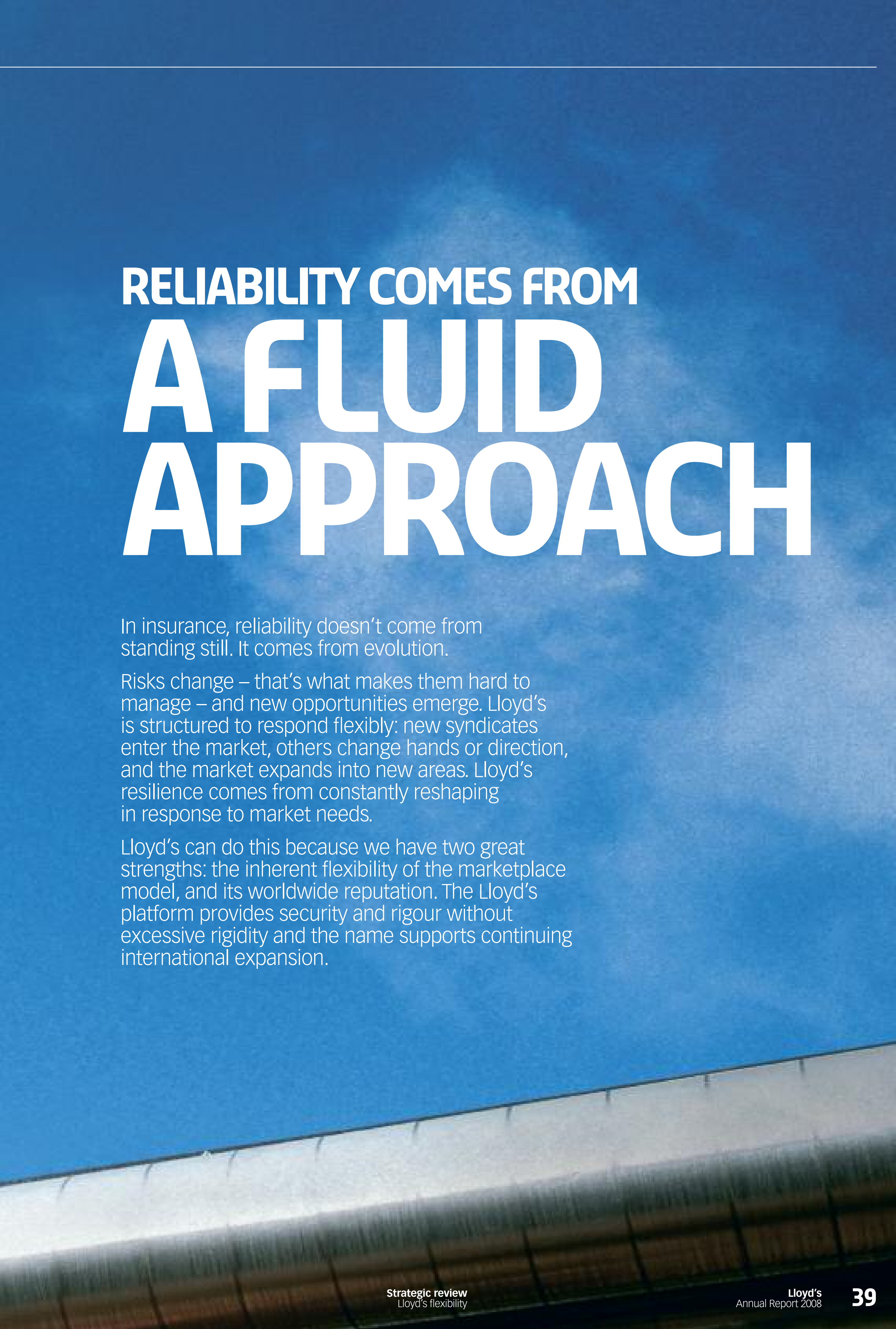
Rationale Recognition of managing agents as customers of the Lloyd's platform and the importance of tracking their satisfaction.

Progress Managing agent satisfaction (measured with senior contacts) has remained constant over the last two years.

Average score out of 10



Comparative score for senior management respondents. Score shown in 2007 annual report was 7.1, based on a broader audience base.



RELIABILITY COMES FROM A FLUID APPROACH

In insurance, reliability doesn't come from standing still. It comes from evolution.

Risks change – that's what makes them hard to manage – and new opportunities emerge. Lloyd's is structured to respond flexibly: new syndicates enter the market, others change hands or direction, and the market expands into new areas. Lloyd's resilience comes from constantly reshaping in response to market needs.

Lloyd's can do this because we have two great strengths: the inherent flexibility of the marketplace model, and its worldwide reputation. The Lloyd's platform provides security and rigour without excessive rigidity and the name supports continuing international expansion.

BECAUSE RISK IS OUR BUSINESS, WE MANAGE IT RIGOROUSLY.

In a challenging financial climate, effective risk management is a key tool underpinning strength and stability.

Risk is managed at Lloyd's through a comprehensive and unique risk management framework which works alongside the assurance processes of Internal Audit, Compliance and Financial Control to enable robust oversight of risk at all levels.

Managing risk is an explicit responsibility for all Lloyd's employees in the Corporation and the market. For Corporation employees, risk management responsibilities are set out in the Lloyd's Risk Policy. To ensure these responsibilities are clearly understood, all new employees receive risk management training as part of their induction. Risk management is also monitored as a key capability within the employee performance management framework and all employees are assessed against this capability in their annual performance appraisals.

The Risk Management Minimum Standards set out key risk management principles for managing agents. They are backed by the Risk Management Toolkit, which provides practical advice and guidance to help the market meet the required high standards of risk management.

The risk management framework aims to pull together the key risks facing the market and the Corporation so that they can 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 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 and Control Framework, which is overseen 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 101.

THE SYNDICATE RISK MATRIX (SRM)

The SRM tool brings together syndicate level risk and performance issues to enable coordinated decision making and action planning. Syndicates are assessed against key risk and performance indicators gathered from across the Corporation. This information is brought together in the SRM and analysed to enable structured discussion at monthly meetings of key senior Lloyd's managers. These 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, to avoid unnecessary duplication of supervisory activities. These issues are also fed into the Lloyd's Risk and Control Assessment discussed in the following pages. The key aim is to gain a wider understanding of syndicate and marketwide risk and performance issues, as a basis for coordinated management, decision making and action planning.

For information on insurance risk, see page 14.

“At KEMI we try to keep our approach to workers' compensation insurance simple by focusing on the basics. Our partners at Lloyd's help us maintain that focus by analyzing and managing risk with expertise, leadership and tailored service. We rely on Lloyd's proven reputation of strength and stability and believe their commitment to their customers makes our commitment to ours even stronger.”

Roger Fries
President of Kentucky Employers' Mutual Insurance
Kentucky Employers' Mutual Insurance (KEMI) is the largest provider of workers' compensation insurance in Kentucky.

THE LLOYD'S RISK AND CONTROL FRAMEWORK

The Lloyd's Risk and Control 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. This committee provides 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 committee is not intended to consider risks within individual syndicates or managing agents, it will discuss any such risks that are relevant at Lloyd's market level.

The Risk Committee oversees the identification, assessment and management of risk.

RISK IDENTIFICATION

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

The LRCA is a continuous self-assessment process embedded in the business. Coordinated and facilitated by the Risk Analysis team, it is the main channel for identifying new risks or changes to the profile of known risks.

The Risk Analysis team conducts continuous environment scanning for significant risk issues. This includes systematic reviewing of press publications (by external consultants), websites and internal communications. It also includes ongoing liaison with internal and external stakeholders.

The Emerging Risks team forms part of the Franchise Performance Directorate. Its remit is to consider new risks such as nanotechnology, and existing risks where new information suggests the level of risk is changing – for example, the impact of climate change on flood risk. The team aims to capture early warning information and ensure it is used effectively. The primary focus of the Emerging Risks team is insurance risk, the dominant category of risk that Lloyd's faces. However, where emerging risks impact other risk categories, the team also considers their wider implications.

The annual Executive Team and Franchise Board Risk Issue Assessments were conducted on 14 November 2008 and 15 December 2008 respectively. Their primary purpose 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. To derive additional value from the sessions, the Executive Team and Franchise Board were also asked to consider any new mitigating actions that might help reduce residual risk in key areas.

Segmenting claims to deliver superior service

Lloyd's vision is to achieve recognition as a world leader in claims management, delivering exceptional customer service, strong financial performance and global reach.

Our Claims Change Programme, begun in 2008, draws together several projects for enhancing and investing in claims handling processes. Over the next three years it will strengthen the Lloyd's brand by creating a more effective and competitive claims service for customers.

One major project deals primarily with the way Xchanging Claims Services (XCS) handles claims on behalf of the following market. XCS provides a unique service to the market where claims involve three or more syndicates, protecting the interests of the 'following' underwriters by peer-reviewing decisions made by the leader.

At any time, the Lloyd's market is dealing with around 180,000 claims. It is estimated that on average over 80% of these are relatively straightforward and low value, and classed as 'standard'. The rest, classed as 'complex', account for less than 20% of total volume but around 70% of the financial value.

By segmenting claims into these categories, we can ensure that claims are dealt with by XCS claims handlers with skills appropriate to the technical complexity and financial amounts involved.

This should bring benefits that have real value for clients. Payment of standard claims will be far quicker. These claims tend to involve payments to policyholders for whom cash flow is often crucial, so payment speed is a vital measure of service quality. For complex claims, which by nature can take months or even years to be resolved, our claims service is defined more by the quality of decision making. This will be greatly enhanced now that senior claims handlers at XCS can devote their time exclusively to resolving the more complex matters in a more proactive and strategically focused way.

RISK ASSESSMENT

All risks identified by the processes outlined on the previous page are monitored using the LRCA process. Each risk is allocated an appropriate owner, who is the key contact for the management of that particular risk, supported by a network of control and action owners across the Corporation. Risks are assessed by the risk owner, and scrutinised by the Risk Committee, in terms of their potential impact on Lloyd's, and the estimated probability of occurrence within a 12-month time period.

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 helps ensure 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 uses 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 review to identify internal control failures and any breach of compliance with legislation or regulation across the Corporation.
- → The Syndicate Risk Matrix: Although the SRM is designed to support the monitoring of risk at syndicate level, the risk data captured may be relevant at Lloyd's market level. Such 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

Risks are assessed on a 'residual' (after controls) basis in terms of their impact and probability. A risk appetite is determined for each risk, 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 LRCA process then tracks actions by key milestones or deliverables to ensure residual/target gaps are reduced within desired timeframes.

The results of the formal LRCA updates are reported to, and agreed by, the Risk Committee on behalf of the Executive Team. The committee uses these results to oversee the risks and satisfy the Franchise Board that risks are being managed effectively and internal controls are robust.

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 timeframe. 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 is used to identify relevant stress and scenario tests for risks that lie outside the stochastic model. These scenario tests are based on potential events where one or more of the risks in the framework could occur, and assess the potential loss from a significant event. The results are fed into the calculation of the Lloyd's ICA.

KEY RISKS ISSUES

RISK ISSUE	IMPACT	MITIGATION
Failure to manage Lloyd's response to the insurance cycle.	→ Lloyd's insurers suffer operational losses and/or erode their capital base through inadequate pricing.	→ Review and agreement of business plans, Realistic Disaster Scenarios and Individual Capital Assessments. → Continuing oversight of performance through reviews of premiums written, rate change, loss ratios, reserving and compliance with minimum standards. → Implementation of enhanced performance management information tools, including the Performance Management Data project.
Failure of market operations initiatives.	→ Lloyd's is unable to maintain its competitive position and deliver process improvements that create a more efficient marketplace.	→ Lloyd's cooperation with the market to agree, prioritise and deliver all market initiatives. → Creation of and adherence to a consistent project delivery methodology. → Franchise Board oversight and sponsorship of business process reform initiatives to drive and ultimately mandate the adoption of key market processes in the Lloyd's market.
Failure to assess exposure to catastrophes adequately, or to hold sufficient capital for them.	→ Underwriting losses incurred are outside expected thresholds, resulting in potential failure of members and subsequent Central Fund exposures.	→ Industry leading approach to catastrophe exposure management through Realistic Disaster Scenario framework and working closely with the market, wider insurance industry and academia to examine and act on emerging risks. → Review of managing agent compliance with exposure management standards and appropriate support provided to managing agents. → Lloyd's robust and well established Individual Capital Assessment process: syndicates' ICAs reflect catastrophe loss potential at a 1-in-200-year confidence level.
Failure to respond effectively to unstable financial climate.	→ Lloyd's suffers increased insurance liabilities, additional regulatory burden, decreased asset values and/or capital constraints.	→ Underwriting guidelines that effectively control exposure to specific insurance liabilities. → Significant additional monitoring and measures to protect Corporation and market assets in respect of investment and reinsurance counterparties. → Lloyd's continuing robust advocacy of regulation based on strong risk management principles.
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.	→ Datacentre facility rented from market leading providers as short-term solution. → Over the longer-term, construction of a primary datacentre operating alongside the rented facility as part of a dual datacentre strategy, alleviating current capacity concerns.
Failure to recognise the potential impact of Solvency II, or to adequately prepare to meet the requirements within specified timeframes.	→ Lloyd's fails to meet requirements of Solvency II, resulting in regulatory sanctions and disadvantageous capital requirements.	→ Solvency II recognised in the Strategic Plan as a key priority for the Corporation and the market; Solvency II steering group initiated, led by Luke Savage and Sean McGovern. → Solvency II working group established comprised of staff from the Finance, Risk Management and Operations, General Counsel and Franchise Performance directorates. → Lloyd's working closely with FSA to agree how best to implement Solvency II at Lloyd's.
Failure to control remote underwriting (service companies and coverholders) and protect the brand effectively.	→ Lloyd's suffers financial loss and/or reputational damage through poor underwriting.	→ Revised 'new service company' application and approval process, including strengthened business plans. → New coverholder applications subject to revised criteria for referral of business plans to Underwriting Performance team to enable underwriting rationale and controls to be approved. → Managing agent review programme to evaluate effectiveness of agent controls over coverholders and binding authorities.

IN TESTING TIMES, DEVELOPING AND APPLYING THE SKILLS OF OUR PEOPLE MATTERS MORE THAN EVER.

2008 PROGRESS
LEADERSHIP DEVELOPMENT

The Leadership Programme designed in partnership with London Business School has completed two programmes and embarked on a third. To date, participants from 15 managing agents, the LMA and Xchanging have participated with Corporation employees. In addition to the knowledge and development gained from the content, the participant mix has resulted in a richer learning experience, new levels of understanding of one another and the challenges we face, and stronger partnerships and networks. Projects undertaken during the programme have tackled issues such as understanding broker strategies and business models, capturing profitable business in emerging markets through microinsurance, and what is effective collaboration within Lloyd's.

The Corporation is continuing its commitment to improving leadership skills. Throughout 2008 the Executive and Management Teams have attended quarterly lectures, led by world renowned figures in the field of leadership. The themes of these lectures have been aligned to Lloyd's strategic objectives.

PEOPLE MANAGEMENT

We firmly believe that everything we do depends on developing and applying the skills of our people. People management is recognised as a core capability at Lloyd's and during 2008 the Corporation reviewed its provision of development in this area. As a result Human Resources will be developing and piloting a new management development programme in 2009.

IMPROVING COMMUNICATION

Staff briefings throughout 2008 provided the main platform for the CEO and Executive Team to engage Corporation staff on current topics and issues. They were strongly supported, regularly attracting over 300 attendees in London alone. The briefings were attended for the first time by the Lloyd's Chairman, who discussed his role and the development of Lloyd's as well as answering questions from the audience.

Regular CEO lunches throughout 2008 provided an opportunity for small groups of staff to discuss current issues and topics directly with the CEO.

The Corporation intranet, C-Net, continues to provide constant updates from across the organisation. C-Net is also supplemented by regular news bulletin emails sent to all staff, on current key topics.

Directorates and teams continued to hold regular meetings, ranging from large 'town hall' meetings for upwards of 100 people to small 'work in progress' sessions of a dozen or fewer.

UK Corporation employee profile
(number of employees)

EMPLOYEE ENGAGEMENT: EMPLOYEE OPINION SURVEY
For the third consecutive year Lloyd's Corporation has undertaken an online survey to measure employee satisfaction and engagement. While providing valuable information on staff perceptions and motivation, the survey also identifies key areas requiring continued improvement and focus. Ipsos MORI conducted the survey on behalf of Lloyd's, and provide Corporation results in comparison with industry and top performing company norms.

The most recent survey (February/March 2009) received an extremely high response rate of 91%; significantly higher than the average for financial organisations, and higher than the Lloyd's rate achieved in 2008 (88%) and 2007 (83%).

Overall satisfaction remains at a very high level (85%), and 93% agree that they are proud to work for Lloyd's (increased from 89% in 2008 and 82% in 2007). The Corporation will focus on these results during Q2 2009, identifying areas for further improvement.

WORKING ENVIRONMENT
The working environment project, which was announced in 2006, has been completed. All Corporation staff now work in a bright, modern, open-plan environment which is encouraging more collaborative ways of working. A project was launched to reduce printing, copying, faxing and scanning costs. This has replaced 250 separate devices with 45 multi-functional devices and 22 single-function printers. As well as providing significant projected cost savings, the project also introduces 'follow me' technology – providing the ability to print at any device and enhanced security as print jobs can only be released by a Corporation ID pass.

CAREER OWNERSHIP
During 2008, work began on a career ownership project, aimed at encouraging staff across the Corporation to take responsibility for their own development. Initiatives started in 2008 included a pilot of the Career Ownership Toolkit, a range of online career-related self-assessment tools. The Corporation will be working closely with the selected suppliers in 2009 to respond to the feedback before rolling-out the finished toolkit across the Corporation.

Attracting and developing new talent

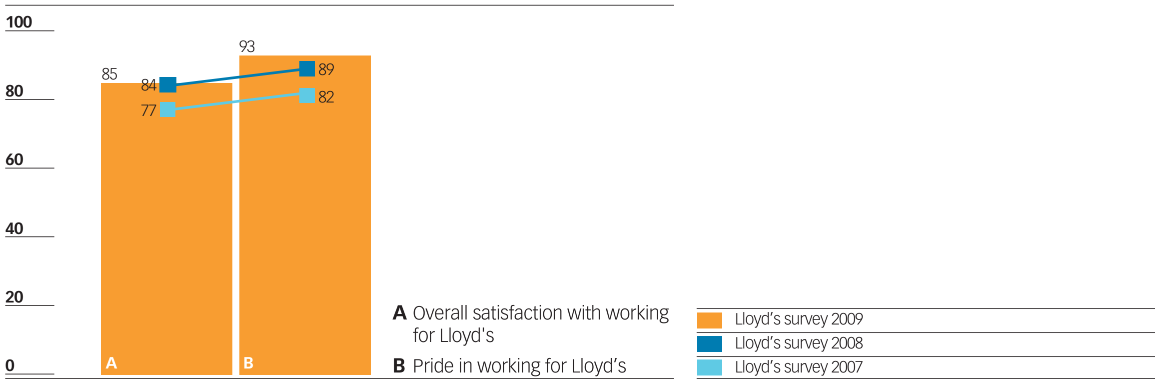
After a successful recruitment campaign, nine graduates joined the Corporation in 2008. After a week of induction they joined teams including Risk Management, Investor Relations, Market Intelligence and Exposure Management. The 18-month programme includes two further placements as well as training courses and work towards professional qualifications. Feedback from both the graduates and the business has been very positive.

Graduate training is also providing new ways for the Corporation to build relationships with the market. Managing agents Beazley, Hardy, Ark and Liberty have involved their graduates in some of Lloyd's centrally run graduate training programmes, helping them to network and giving them a broader perspective on the industry. And the Corporation has placed a further nine people with managing agents and brokers, helping the industry in the continuing drive for talent.

Building on the success of the 2007 graduate recruitment campaign, ten target universities were identified as the focus for much of the 2008 campaign. A variety of approaches – from attending careers fairs to sponsoring university debating society events – attracted a 50% increase in applications.

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

Employee opinion survey
(percentage in agreement)



DIVERSITY

The Diversity Steering Group continued its efforts to ensure that Lloyd's attracts and retains talent from a wide range of backgrounds. In research commissioned by the group, employees commented positively on their experiences at Lloyd's: the majority said they would recommend the organisation to a friend or family member. The research – undertaken during the past year among employees from ethnic minority backgrounds and non-UK nationals – sought to understand their experience of working at Lloyd's. There was a widespread view among respondents that their nationality or ethnicity was not a barrier to career progression. Before joining, many had expected Lloyd's to have a traditional and homogeneous culture, and they had been pleasantly surprised at the diversity of the Lloyd's workforce.

The drama-based training on diversity, which ran for senior managers at the end of 2007, was extended to the whole Corporation and overall feedback was very positive. Online diversity training was relaunched and all Corporation employees, including new starters, are now expected to complete it. During the year, the Chair of the Diversity Steering Group addressed representatives from recruitment agencies to ensure they were aware of Lloyd's commitment to diversity.

POLICY REVIEW

A 2008 review and audit of Corporation employment policies found that it offers a competitive benefits package, and that its practices are consistent with those of the best employers – ahead of them in some cases. This applies particularly to family friendly provisions and health and wellbeing benefits, which rank among the top ten employer-provided benefits according to the Chartered Institute of Personnel and Development (CIPD) reward survey (February 2008).

2009 INITIATIVES

IMPROVING HOW WE WORK

To support the alignment of the Corporation and overseas offices, a project began at the end of 2008 to replace the current HR and payroll systems in both international and UK offices with a robust online system. Using a single system to deliver information and data storage globally will simplify HR and payroll processes, allow integrated management of the employee life cycle and support more effective approaches to talent development.

GLOBAL POLICIES

Building on the work initiated in 2008, the Corporation will continue to review and audit employment policies and employee benefits to ensure a consistent approach across Lloyd's global offices.

LEADERSHIP DEVELOPMENT

Due to the success of the Leadership initiative, the 2009 programmes are already fully booked. Applications for 2010 will open in September 2009.

CAREER OWNERSHIP

To support career ownership within the Corporation, a new management development programme is being planned to provide a structured development programme for both experienced and new managers. This is being finalised with a view to going to tender in spring 2009.

The Community Affairs team will look at the external development opportunities offered by participation in the various Lloyd's community programmes.

To increase the transparency of options for career advancement and to challenge the assumption that progression requires promotion or management responsibility, career interviews with a cross section of Corporation staff will be posted on the Lloyd's intranet.

GRADUATE RECRUITMENT

For the 2009 programme, the Corporation is looking to recruit up to ten exceptional graduates. Assessment centres are currently being held to make final selections. As part of the programme, graduates will spend one of their placements with the market: the first of these placements will start in April 2009. It is also hoped that some managing agents will send their graduates on secondment to the Corporation.

CORPORATION EMPLOYEE DEMOGRAPHICS

UK EMPLOYEE TURNOVER AND ABSENCE	2008 number	2007 number
Employees as at 1 January 2008	**694**	668
Total joiners, year to date	**130**	156
Total voluntary leavers	**(47)**	(64)
Total involuntary leavers (redundancies, dismissals)	**(23)**	(35)
Total retirements	**(5)**	(5)
Contracts completed	**(30)**	(26)
Employees as at 31 December 2008	**719**	**694**

UK EMPLOYEE TURNOVER AND ABSENCE	%	%
Total turnover	**14.6**	18.7
Turnover (excluding contracts completed)	**10.4**	15.0
Industry average turnover	**17.5**	14.5
Voluntary turnover	**6.5**	9.2
Industry average voluntary turnover	**12.5**	9.9
Absence	**2.5**	2.1
Industry average absence	**3.0**	3.2

TOTAL EMPLOYEES	2008 number	2007 number
UK	**719**	694
US	**33**	30
Canada	**6**	3
Asia	**45**	31
Europe	**40**	33
Africa, Australia and South America	**8**	7
	851	**798**

The Corporation regularly monitors the level of staff turnover and absence against suitable industry benchmarks and corrective action is taken if required. During 2008, UK voluntary staff turnover, excluding redundancies, dismissals, retirements and contracts completed, continued to be below the industry average at 6.5%, as did the sickness absence record at 2.5%. 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 2008 is shown below:

UK employee segmentation	Executive		Head of function		Manager		Professional/ technical		Admin		Total	
Figures in numbers	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007
Male	**6**	6	**25**	29	**135**	131	**174**	147	**29**	35	**369**	348
Female	**1**	1	**8**	7	**67**	69	**163**	147	**111**	122	**350**	346
Total employees	**7**	7	**33**	36	**202**	200	**337**	294	**140**	157	**719**	694
Figures in years	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007	**2008**	2007
Average age	**51**	50	**46**	46	**42**	42	**39**	38	**38**	37	**40**	39
Average service	**5**	4	**9**	8	**9**	9	**8**	8	**6**	6	**6**	8

The segmentation as shown above includes 6 male and 63 female part time employees as at 31 December 2008 (31 December 2007: 4 male; 60 female).

The employee demographics shown above include both permanent staff and those working on a contract basis.

ALL THROUGH THE CYCLE

DISCIPLINE COMES FIRST

When times are good and claims are down, premiums tend to fall. When disaster strikes and claims rise, so do the premiums. That's the insurance cycle. But in turbulent conditions, some underwriters can be tempted to take chances – writing risks at a loss to maintain or advance their position against competitors. Their aim is to be better placed when the good times return; but over the long-term, the whole market loses. Such unbridled competition can cost them, and their competitors, dearly.

Lloyd's works to maintain a disciplined approach across the field. Writing for profit not market share – and being prepared to walk away from unprofitable business – should help to keep the market, and all its participants, profitable.

Over the longer-term, we believe this is a better way to manage the cycle – and one that will ultimately help reinforce Lloyd's reputation among both capital providers and policyholders.

MAKING A DIFFERENCE – A THOUSAND TIMES OVER.

In a record year for the Lloyd's Community Programme, over 940 volunteers took part in more than 1,048 volunteering opportunities. Its main focus continues to be support for schoolchildren and young people, to help them develop the skills they need for a successful education and, eventually, rewarding employment. In East London, the geographic focus for volunteers' efforts, this remains as important a goal as ever because Tower Hamlets has the highest unemployment rate in Great Britain and in Hackney unemployment is a significant problem, especially among the young.

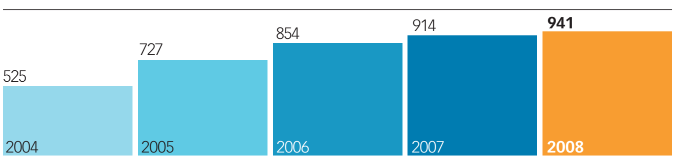
BASIC SKILLS
HELP WITH BASIC SKILLS THROUGH READING AND NUMBER PARTNER SCHEME

Supporting young people's basic skills remained a priority for Lloyd's Community Programme in 2008. 'Words and Numbers' proved to be the most popular of volunteer projects, with over 460 Reading and Number Partners spending a lunchtime a week in school to support children with their literacy and numeracy skills.

In Tower Hamlets, Lloyd's Community Programme has been involved in Reading Partners since the first pilot in 1994. Statutory Attainment Test results achieved by schools in the Key Stage 2 national curriculum tests in England in May 2007 were encouraging, with the borough achieving above the national average in English and maths.

During the year, the main focus for local schools was Key Stage 3 results for 14-year-olds in English and maths. In 2007, these showed a flat performance year-on-year, placing Tower Hamlets bottom of the London boroughs. The correlation between Key Stage 3 results and GCSE performance in English and maths makes the improvement of basic skills a priority, so a key objective for Lloyd's Community Programme in 2008 was to increase volunteer support for secondary school pupils. In November, the Corporation of Lloyd's launched a Number Partner scheme in Oaklands Secondary School and Lockton International launched a Reading Partner scheme in Mulberry Secondary School for Girls.

Lloyd's volunteer involvement



Volunteer Lee Langstaffe, Head of Corporate Audit at Lockton commented: "This is the first time I have participated in the Reading Partners project and I'm really looking forward to helping the students. For me it's not just about reading, but helping the students to develop interpersonal skills, letting them understand what some of the work opportunities are and making them think about their own aspirations for the future. It's a great way to spend my time and help out others in the process."

In Hackney, results at Key Stages 2 and 4 are well below the national average. For example, only 46.6% of students achieved five or more GCSEs including English or maths – five percentage points below the national average. Lloyd's Community Programme is keen to extend its support of Reading and Number Partners in Hackney, and in 2008 increased its financial support of Inspire! the borough's Education Business Partnership brokerage service for primary schools.

EMPLOYABILITY SKILLS
READY FOR WORK PREPARES STUDENTS

Since January 2008, Lloyd's volunteers have given over 230 hours of their time to take part in one-day work-related learning workshops. Sessions such as Head to Head or Getting PAID are aimed at preparing young people for the world of work and are great opportunities for people to get involved and share their skills and experience – especially those who find it difficult to make a commitment to ongoing volunteering.

Amlin gave an interesting twist to the Ready for Work programme when it ran a two-day Personal Effectiveness Programme for 17 students from Tower Hamlets College in December 2008. Lloyd's provided the training room and the training was delivered by Amlin's Training and Development Manager and Advisor, Julie Northfield and Nicole Almond respectively. The course was a great success and enjoyed by all. Adam Hart, a teacher from the college wrote, "There is still a real buzz about the days we spent with Lloyd's." And one of his students commented, "This course really helped clarify what this part of the insurance industry does. And the activities on personal skills were useful too."

VOCATIONAL TRAINING AND PLACEMENT
A BRIDGE TO THE INSURANCE WORLD

Managing agents from the Lloyd's market have been working alongside the Corporation to help young people from Tower Hamlets gain experience of working in insurance, by hosting work placements for 11 local graduates in autumn 2008.

The six- to eight-week work placements were one aspect of an insurance course developed for young people in East London by the National Skills Academy for Financial Services at Tower Hamlets College, the Chartered Insurance Institute (CII) and Lloyd's.

Before the placements, the students studied at the college for six weeks to complete three components of the Certificate of Insurance. Companies who provided placements included ACE, Capita, Chaucer, Hardy, the Corporation of Lloyd's, Talbot, Whittington, Xchanging and XL London Market.

Lloyd's Claims Account Manager Mark Burr worked on setting up the course and commented, "The skills the students have learnt in the programme will help their employment prospects in the future". By December 2008, three of the six trainees who had finished the programme with a managing agent had accepted employment. With other placements due to finish in 2009, it is hoped that even more of the graduates will secure full time employment and start a rewarding career in insurance in the Lloyd's market.

ACCESS TO TECHNOLOGY
2008 SPECIAL AWARD SUPPORTS E-LEARNING

In December, Lloyd's Charities Trust donated £50,000 to the e-Learning Foundation to provide access to computing at home for children in low-income families in Tower Hamlets and Hackney.

The e-Learning Foundation is the 2008 recipient of Lloyd's Special Award, a donation which is awarded to a charity addressing issues relevant to the Lloyd's market.

Lord Mitchell, Chairman of the e-Learning Foundation, says: "Increasingly, low income families are finding themselves on the wrong side of the digital divide through no fault of their own and are being disadvantaged in their future development through the lack of IT access for their studies. This generous donation will enable us to support further sustainable e-learning projects in schools in London, ensuring they have the technology skills required to take them forward in the 21st century."

The Special Award donation will support e-learning projects in schools in East London where Lloyd's has long-standing links through the Lloyd's Community Programme. The project will provide children in each selected school with laptop computers to use at school and home, giving over 500 pupils the e-learning tools they need for their education.

Graham White, Chairman of Lloyd's Charities Trust, says: "I'm delighted that we are able to contribute in helping the e-Learning Foundation expand its positive work in East London. The Lloyd's market has a long-standing commitment to investing in future talent – including unlocking the talent in our neighbouring communities. Harnessing the potential of technology is important to every part of society and we hope that our Special Award will particularly help young people who might otherwise have found themselves excluded from the opportunities that technology can open up."

The project will be rolled out to local schools in 2009, the 20th anniversary of Lloyd's support for East London through Lloyd's Community Programme.

Partnering Rachel from primary school to placement

Rachel Roberts should feel quite at home on her work experience placement at Lloyd's – we've been working with her since primary school.

As a student at St Anne's Primary School in Whitechapel, she was supported by one of Lloyd's Community Programme's long serving Reading Partners, Robin Anderson from Ace. Imagine Robin's delight in September 2008, when he heard from Rachel – now 17 and enrolled on a legal secretarial course at Epping Forest College.

Rachel needed to find a six-month work experience placement that would allow her to work in a business one day a week to develop her secretarial and office skills. Robin made some enquiries, and a few weeks later Rachel had an offer from the Corporation to work with two teams: Ratings and Investor Relations, and Market Reserving and Capital.

"I'm enjoying my work experience at Lloyd's," says Rachel. "I'm learning new skills and meeting lots of new people, which will help me progress further in my career. I hope to work for an organisation like Lloyd's once I've qualified."

Lloyd's Community Programme members

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
Glencairn 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
Markel
Marketform Group
Mazars
Miller Insurance Services Ltd
Munich Re Underwriting Ltd
Navigators Underwriting Agency Ltd
Newline Underwriting Agents Ltd
Novae
Omega Underwriting Agency Ltd
PricewaterhouseCoopers
QBE Insurance Group
Reynolds Porter Chamberlain
Talbot Underwriting Ltd
Travelers
Xchanging Claims Services
XL London Markets Ltd

HELPING PEOPLE AT RISK, FROM LONDON CHILDREN TO SUDANESE FARMERS.

One way people at Lloyd's can give something back to those less fortunate in the UK and abroad is through their support of Lloyd's charities. The demand from charities for help is increasing – whether for emotionally distressed teenagers in the UK, service and ex-service personnel injured in global conflicts, or farmers in Sudan. Lloyd's charities are continuing their tradition of supporting the vulnerable, with the firm backing of people at Lloyd's.

Lloyd's Charities Trust is the grant-making charity of the Lloyd's market. It works to support the vulnerable in the UK and abroad, through donations to a variety of charities and its commitment to its three partner charities.

The trust is supporting three partner charities – Coram, FARM-Africa and Samaritans – over a three-year period from 2007 to 2010. Grants of £150,000 to each organisation are enabling them to develop specific projects, from helping vulnerable babies and teenagers at risk in the UK, to working towards developing sustainable livelihoods for families in Sudan.

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

CORAM
TRANSFORMING VULNERABLE YOUNG LIVES

Coram works with vulnerable children, young people and their families, transforming their lives through practical help and support. Support from Lloyd's Charities Trust has enabled the charity to work with vulnerable babies at risk through the Concurrent Planning project – a unique adoption and fostering initiative which works with children whose parents may have drug or alcohol problems or mental health issues that place the child at risk. The charity recruits and trains specialist foster families who look after the child while a court decides whether the baby can go back to his or her parents. If that is not possible, the foster family adopts the child – avoiding further damaging moves.

SAMARITANS
COMBATING THE CONTAGION OF SUICIDE AND SELF HARM

Samaritans offers 24-hour confidential support to people in emotional distress. A particular problem, highlighted in the media in 2008 because of the suicide cases in Bridgend, Wales, is the number of suicides among young people. The Samaritans' Skills for Life project, supported by Lloyd's Charities Trust, is working to reduce the contagion effect of suicide and self harm in schools and its impact on the wider community.

The project will result in a suicide and self harm response service for schools, supported by Lloyd's Charities Trust, enabling Samaritans to deliver training for education and health professionals and volunteers on responding to suicide and self harm among young people.

Once rolled-out to schools across the UK and Ireland, it is hoped this service will provide a model for suicide and self harm response services across all age groups and settings.

FARM-AFRICA
REDUCING RELIANCE ON FOOD AID

FARM-Africa works with farmers and herders in eastern Africa to provide long-term solutions to poverty by introducing new ways to increase food production and manage natural resources. Lloyd's Charities Trust is supporting the Southern Sudan Household Recovery Programme, which aims to help vulnerable households rebuild and develop rural livelihoods and reduce their reliance on food aid.

The project has made real progress this year. Four boreholes have been drilled, ten shallow wells dug and nine pump mechanic tool kits distributed, giving thousands of Sudanese people access to clean drinking water. Over 3,000 households received an allocation of seed and tools and 97 vulnerable households received five goats each. Training for 78 animal healthcare workers led to the vaccination of 85,000 animals. These measures have had a significant impact on the lives of people at risk in Southern Sudan.

"This well has changed my life. My family are not thirsty again. My cows and goats are watered daily from this well. There are so many people from our village and outside our village that fetch water from this well – therefore, I opened a small market table and my wife prepares tea and food for sale. The business is very good and sometimes we earn 40-60 Sudanese pounds (around £10–£15) a day. I like to thank FARM-Africa because they gave us water, new friends and business."

John Garang, shallow well digger, Sudan

Coram's work in action, Sarah's story

Sarah's mother Lisa, 24, was seriously neglected as a child and has a diagnosis of bipolar disorder. Her father Peter, 20, has a history of alcohol and drug problems. When Lisa became pregnant, the local authority was very concerned about the couple's ability to look after the baby.

Sarah was born in early 2007 and when the local authority began care proceedings she was placed with two of Coram's Concurrent Planning carers, Simon and Sue. Coram staff undertook parenting assessments and worked with the birth parents on developing their parenting skills. Psychiatric assessments were also completed. In late 2007, the court decided Lisa and Peter were not able to care for Sarah safely and that the baby should be adopted.

When Sarah was placed with them, Simon and Sue brought her to Coram three times a week for contact with Lisa and Peter, enabling everyone to develop good relationships. Simon and Sue have now adopted Sarah, but Lisa and Peter will still have direct contact once a year.

Without Concurrent Planning, Sarah would have been placed with short-term foster carers and might have moved to several different carers before finally being placed with adopters. This could have gone on for two years, repeatedly disturbing her baby years and causing great stress.

Picture: Spencer Rowell, courtesy of Coram.
The names of people have been changed to protect their identity.

LLOYD'S CHARITY CHALLENGE
FUNDRAISING FOR OUR PARTNER CHARITIES

The Corporation and market demonstrated their support for the three partner charities through Lloyd's Charity Challenge, which raised £250,000 for Coram, FARM-Africa and Samaritans in 2008.

Eleven teams from the Corporation and Lloyd's market signed up for the challenge, and over a month devised and implemented innovative ideas to raise money for their allocated charity. As well as from their own fundraising ventures, the teams took part in a 10km run, classic car event and wine tasting evening overseen by judges Lord Levene, Chairman of Lloyd's, Holly Bellingham, Chairman of Marketform and Graham White, Managing Director of Argenta Private Capital.

The teams raised a significant amount for the three charities – boosting the number of people they can help in the UK and abroad. And they also shared a unique team-building experience: every one of the participants said they would recommend a colleague to take part in a future Charity Challenge.

LLOYD'S PATRIOTIC FUND
PROVIDING HOMES FROM HOME

With so many conflicts raging around the world, demand for support from the Lloyd's Patriotic Fund is as great as ever.

Over the past century the nature of military engagements has changed; but practical assistance for those who have made sacrifices for their country remains as important as it was in 1803, when the Lloyd's market established the fund to support serving and ex-service personnel and their families.

Today, the fund works closely with SSAFA Forces Help to identify individuals and their families who urgently need financial help. It demonstrated its commitment in 2008 with a donation of £300,000 to SSAFA Forces Help's Homes from Home appeal.

This project gives the families of injured service personnel the chance to stay close to their loved ones in hospital. The Homes from Home appeal has provided two homes for families, one at the Defence Rehabilitation Centre in Surrey, the other at the Royal Centre for Defence Medicine in Birmingham.

LLOYD'S BENEVOLENT FUND
HELPING THOSE FACING HARDSHIP

Founded in 1982, the objective of the Fund is to assist all those in necessitous circumstances, who work or have worked in the Lloyd's community, and their dependants or others at the discretion of the trustees. Attention is drawn to the request that members of the community requiring assistance should be put in touch with the Fund. Help given to beneficiaries is flexible, taking the form of, for example, annual grants or assistance to cover specific needs.

LLOYD'S TERCENTENARY FOUNDATION
FUNDING AND PROTECTING INTELLECTUAL CAPITAL

The 20th anniversary year of Lloyd's Tercentenary Foundation marked a turning point as the charity took on a new direction to maintain its relevance and significance.

The charity was established by Lloyd's in 1988 to mark 300 years of success, and has supported academic research for 20 years. It now aims to change its focus to reflect shifting priorities in the insurance industry and society at large. Steps were taken in 2008 to explore areas of research where the insurance industry can engage with the academic community and Lloyd's Tercentenary Foundation facilitated a seminar at Lloyd's involving academics and representatives of the insurance community and FSA.

One result was the Insurance Intellectual Capital Initiative (IICI), which will provide research funding. Lloyd's Tercentenary Foundation will continue to support its existing Research Fellows and will also contribute funding towards the new IICI, along with companies from the Lloyd's market and research councils. The IICI expects to get its first programme of new research under way in 2009.

TACKLING CLIMATE CHANGE REALLY MATTERS TO US: IT'S PRACTICAL RISK MANAGEMENT.

"Insurance companies are at the forefront of the fight against climate change. They have to assess what impact climate change will have across their business, and price their products to recognise the developing awareness of the risk it poses. They also have a strong vested interest in reducing that risk by supporting the transition to a low carbon economy. So the sector has a vital role to play in the response to climate change across the whole economy, helping society to mitigate its effects and adapt to a changing world"

ClimateWise: one year review, November 2008.

LLOYD'S AND CLIMATEWISE
RESPONDING TO THE CHALLENGE OF CLIMATE CHANGE

Lloyd's was a founding signatory of the ClimateWise principles for the insurance industry which were launched in September 2007. The initiative aims to encourage insurance companies worldwide to respond to the challenge of climate change as quickly and as effectively as possible for the compelling reasons set out in the quote above. Forty-one insurance companies are members, including 17 managing agents from the Lloyd's market.

During 2008, membership of ClimateWise has helped us to build on our existing environmental activity and provided a wider framework for looking at climate change. In November 2008, ClimateWise produced its first annual review of the progress that all companies involved are making against the six principles. Highlights of Lloyd's progress are set out below.

Further information can be found at www.lloyds.com/climatewise, where updates are provided throughout the year on work undertaken.

CENTRE FOR EARTH SYSTEMS INTELLIGENCE AND LIGHTHILL RISK NETWORK
TAKING A LEAD IN RISK ANALYSIS

Lloyd's has joined IBM Deep Computing, the University of Reading, the Proudman Oceanographic Laboratory and the Science and Technology Facilities Council to fund the creation of the Centre for Earth Systems Intelligence and catalyse research into climate change through modelling on a flagship Blue Gene supercomputer. Lloyd's contribution of £300,000, along with donations from the other parties, has provided pivotal funding and resourcing. The computer will be used for grand challenge problems such as storm surge forecasting, carbon cycle modelling and gaining a deeper understanding of climate uncertainty.

The Lighthill Risk Network receives core funding from the Corporation, Guy Carpenter, Benfield and Catlin. It encourages the flow of knowledge from academia to the insurance industry and helps articulate research challenges of relevance to the insurance industry. In May 2008, it hosted an event on climate change attended by representatives from the insurance industry, the Met Office and academia. Speakers shared their knowledge on European impacts of climate change, including flooding, windstorms and storm surge. Three catastrophe modelling firms took questions in a panel discussion on whether such models are keeping pace with scientific findings.

THE POZNAN PROCESS
INFORMING PUBLIC POLICY MAKING

Lloyd's is committed to working with policymakers to help make economies more resilient to climate risk. Along with many other global businesses, we supported the Poznan communiqué from HRH Prince of Wales's Corporate Leaders Group. This calls for international agreement on long-term greenhouse gas emissions both for the developed world, which must aim for deep cuts and to start the process immediately, and for the developing world. We support the view that a global emissions trading market is crucial to allow environmental considerations to be monetised on company balance sheets.

The ClimateWise group also fed into the Poznan process a statement which we support. Its proposals include national and local adaptation plans for all countries and a long-term international arrangement for collecting and sharing climate data. Good quality data is critical for risk management and in 2008 we took part in discussions where we stressed the importance of Global Earth Observational Systems which the insurance industry uses to calibrate many of its models.

360 RISK INSIGHT
SUPPORTING CLIMATE AWARENESS AMONG OUR CUSTOMERS

Through our 360 Risk Insight project, Lloyd's has continued to promote climate change as an emerging risk which businesses and their insurance providers need to plan and prepare for. In 2008, this work included a series of regular news and feature articles on different aspects of climate change and a special report, produced in partnership with the catastrophe modelling firm Risk Management Solutions, Coastal Communities and Climate Change. This report warns that unless action is taken to reduce global warming, losses from coastal flooding for high risk properties could double by 2030. But it also shows that careful use of adaptation measures could actually cut this risk below current levels. It concludes with recommendations on how policyholders and insurers can work together to achieve this.

For more information on the Lloyd's 360 Risk Insight, please visit www.lloyds.com/360

VOTING FOR CHANGE
BUILDING CLIMATE CHANGE INTO OUR INVESTMENT STRATEGIES

At Lloyd's we believe we should use our shareholder power to influence the companies in which we invest to alter their behaviour and respond more effectively to the impact of climate change as part of long-term value creation. F&C Investments has been appointed to provide a service engaging those companies in which Lloyd's Central Fund invests and to exercise the fund's voting rights in pursuit of environmental, social and governance issues.

We have shared our assessment of the impacts of climate change with our pension fund trustees through a presentation on Lloyd's response to climate change and the action that has been taken with respect to investments.

ENVIRONMENTAL ACTION PLAN
REDUCING THE ENVIRONMENTAL IMPACT OF OUR BUSINESS

During 2008, the Corporation's Environmental Working Group met regularly to monitor progress against its Environmental Action Plan. A primary objective for the group is to reduce energy consumption and the Corporation undertook a number of projects in 2008 to help achieve that.

These included investment of over £350,000 in upgrading the management systems and chilling and cooling plant of the Lloyd's Building in London which will result in saving in energy consumption. A new print management system was also rolled out across the organisation: it is expected to use up to 55% less energy than the previous system and up to 99% less energy when devices are on standby.

Lloyd's also switched to a renewable energy supply for our offices in London and Chatham and, with the help of external consultant Scott Wilson, undertook to calculate and disclose the greenhouse gas emissions of our UK operations. During 2007, these were calculated at 13,384 tonnes and 2008 greenhouse gas emissions, which will reflect the positive impact of switching to renewable energy, will be available on www.lloyds.com/carbonemissions from April 2009.

The assurance statement can be found at www.lloyds.com/carbonemissions

To engage employees, the Corporation launched its first Green Award to get employees' suggestions on improving its environmental impact. It has committed to implementing the winning idea during 2009.

While focusing on climate change, Lloyd's has continued to address other sustainability issues. Initiatives have included a major drive to replace bottled water with filtered tap water on the premises and to develop a new comprehensive recycling scheme for implementation in 2009.

CLICK THE 'OUR PROGRESS' BUTTON ONLINE
REPORTING AND BEING ACCOUNTABLE

We have set up a dedicated section of the Lloyd's website for ClimateWise issues at www.lloyds.com/climatewise. To find out more about our activities in this area, click the 'Our progress' button for a detailed table of work to date.

As part of the requirement to demonstrate board level support for ClimateWise, a paper on Lloyd's proposed climate actions in 2009 has been agreed by the Lloyd's Executive Team. Climate change is specifically identified as a critical issue on the Lloyd's Risk Register under the ownership of the Emerging Risks team and Luke Savage (Director, Finance, Risk Management and Operations) sponsors the team within Lloyd's which is responsible for ClimateWise.

Many members of the ClimateWise initiative are Lloyd's managing agents. Each considers how they can best make a difference, but they also look to the Corporation to carry out some functions on their behalf. To facilitate this, the Corporation hosts periodic meetings for representatives of this group.

REINSURANCE
See page 61.

PROPERTY
See page 62.

CASUALTY
See page 63.

MARINE
See page 64.

ENERGY
See page 65.

MOTOR
See page 66.

AVIATION
See page 67.

HOW THE MARKET PERFORMED IN 2008

2008 HIGHLIGHTS

→ Profit before tax of £1,899m (2007: £3,846m) and a combined ratio of 91.3% (2007: 84.0%), a solid performance during an exceptionally turbulent year for the financial sector.

→ Profit before tax, excluding foreign exchange movements on non-monetary items, of £1,529m (2007: £3,846m).

→ Total investment return of £957m (2007: £2,007m), benefiting from a conservative investment strategy.

→ Overall surplus on prior years of £1,265m (2007: £856m) as claims develop within projections for the fourth year in a row.

→ Pre-tax return on capital of 13.7% (2007: 29.3%).

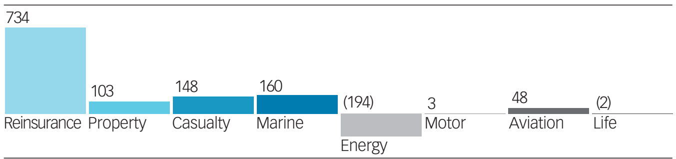
2008 combined ratio*

Accident year	100.5%
Prior year reserve movement	(9.2%)
Calendar year	91.3%

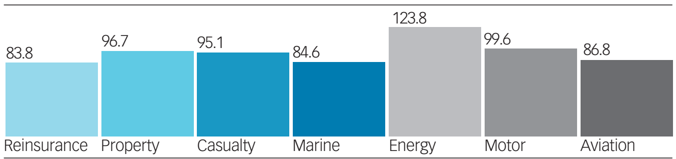
2008 combined ratio excluding foreign exchange movements on non-monetary items

Accident year	103.2%
Prior year reserve movement	(9.2%)
Calendar year	94.0%

Underwriting results by class
(£m)



Combined ratio by class
(%)



*See Glossary on page 140.

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 74 and 76). 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.

The Lloyd's market produced a good result during a year that brought a series of challenges, both old and new, for the insurance industry. Not only did it see an increased level of catastrophes and a series of major individual risk losses, but it was also faced with unprecedented turmoil in financial markets.

Following two years of remarkably few catastrophes, the US windstorm season again brought havoc to the southern United States and the Gulf of Mexico. Hurricanes Gustav and Ike struck in September, causing huge disruption to communities and destruction to homes, business property and the offshore energy industry. The extent of the damage and the cost of reconstruction inevitably impacted the Lloyd's market's results – principally for the reinsurance, property and energy lines of business.

In addition, there was a series of single event losses that were significant in size and frequency. Man-made and technological catastrophes caused around US$7bn in insured losses last year, some 46% higher than the annual average of US$4.8bn. Nineteen events across 11 countries resulted in insured losses ranging from US$80m to nearly US$2bn each.

2008 will be remembered above all for the near-collapse of confidence in the banking system, extreme dislocation in financial markets and the onset of recession. For Lloyd's and other insurers, the return on investments suffered as a result. Despite this, our overall investment performance remained positive, with strong cash balances and the high credit quality of fixed income investments offsetting falls in value of many corporate bond securities and equities. Lloyd's conservative investment policy has preserved capital and ensured that our balance sheet has remained strong.

CURRENCY MOVEMENTS

The last four months of 2008 also saw sterling's rapid depreciation against the US dollar and other Lloyd's operating currencies. The US is Lloyd's single largest market and this, together with the fact that a large proportion of the world's trade is transacted in US currency, means that some 60% of Lloyd's premiums are written in US dollars. The decline in the value of sterling against the US dollar, in particular, has had a marked effect on our reported results in sterling terms.

Another consideration is that Lloyd's has a diverse capital base and our US and Bermudian capital providers report their own group results in US dollars. For these companies, the US dollar is their home currency.

Lloyd's results are reported in sterling and in accordance with UK GAAP. Each managing agent applies the appropriate accounting policies for its managed syndicates. As a result of the different accounting treatments applied, some agents have reported the impact of currency exchange movements within the profit and loss account (P&L) while others have recognised the movements within the Statement of Total Recognised Gains and Losses (STRGL). Where the movement is booked through the P&L, it comes through in three ways:

Firstly, for underwriting profit and investment returns generated in currencies other than sterling; under conventional accounting methods, these items are reported at the average rate of exchange for the period. Balance sheet items, however, are generally restated at closing rates of exchange. The retranslation of the reported results for the period from average rate (in the P&L) to closing rate (in the balance sheet) is recognised as a profit or loss on exchange and is reported within net operating expenses in the P&L. In 2008, the average rate of exchange was US$1.85:£1 and the closing rate of exchange at 31 December was US$1.44:£1. The retranslation of US dollar underwriting profits and investment returns into sterling therefore produces a gain on exchange in 2008.

Secondly, the assets and liabilities held in different currencies at 1 January are retranslated from the opening rates of exchange to the closing rates. Lloyd's naturally holds assets in currency to match outstanding liabilities, principally future claims. Indeed, at 1 January 2008, some US$30bn (£15bn) of future liabilities were denominated in US dollars. Following the Lloyd's market's record profits in the last two years, the Lloyd's market holds more assets than liabilities in both sterling and foreign currency. The opening rate of exchange at 1 January 2008 was US $1.99:£1 and retranslating these balances at the rate prevailing at 31 December 2008 produces an additional profit on exchange.

Thirdly, profits on exchange have arisen through an accounting treatment adopted for non-monetary items. The main items defined as 'non-monetary' are unearned premium reserves and deferred acquisition costs. Some 21 syndicates have adopted this treatment in their syndicate accounts, in line with their group reporting under IFRS, where this accounting treatment is mandatory. This accounting policy requires the accounts to carry non-monetary items at the foreign exchange rate prevailing at the time of initial recognition, without revaluation to the closing exchange rate. There is therefore a mismatch between the exchange rates used to convert non-monetary items (predominantly liabilities in the balance sheet) and monetary items (net assets). This produces unfortunate volatility in reported results across different periods – if sterling continues to trade at or around US$1.44, the past year's exchange gain will largely reverse this year.

The gain on exchange arising from retranslation of profits made in foreign currency and net assets and liabilities totals £445m.

The gain arising through carrying non-monetary items at initial rates of exchange and monetary items at closing rates totals £408m. A significant proportion of this gain, £370m, will reverse in 2009.

The overall impact is an exchange gain of £853m in the P&L and a gain of £659m recognised in the STRGL.

Future movements in foreign exchange rates will have an impact on the market's results and net assets reported in sterling.

LOOKING AHEAD

The outlook for 2009 is dominated by concerns about the impact of the financial crisis. Capital constraints and the low yield environment for investments would normally be expected to create a favourable climate for improvements in underwriting conditions. More difficult to predict is the effect of the economic downturn on the demand for insurance cover and premium volumes as asset values fall and world trade contracts.

Attritional claims levels rose throughout 2008 and are expected to continue rising into 2009. Coupled with this rise is the heavy claims inflation, which was fuelled by the escalating costs of raw materials in the earlier part of 2008.

Great uncertainty exists over the impact that a prolonged downturn will have on the insurance industry, but it is expected that claims frequency will rise further across all lines of business.

The dislocation in financial markets will trigger multiple class actions as investors seek to recover their losses. We anticipate that plaintiffs will bring suits against any targets that they consider have the resources to recompense them and the Professional Indemnity (PI) coverage available will be a key consideration. This will include Directors & Officers' insurance (D&O) and Errors & Omissions insurance (E&O) for financial institutions and financial advisers. In previous years, Lloyd's has suffered material losses on these accounts, notably during the soft market conditions of 1997–2001. The level of coverage now offered by the Lloyd's market, however, is much lower as many syndicates have largely withdrawn from providing PI cover for major US financial institutions. This greatly reduced exposure will be the single most significant defence against such losses recurring, although the tighter terms and conditions imposed in recent years and the burden of proof on plaintiffs should also limit industry losses.

The crisis may well give rise to numerous claims and class actions on credit insurance and the reinsurance of bond insurers. However, Lloyd's exposure to such claims is limited by the restrictions on the level of financial guarantee business that Lloyd's syndicates can write.

2008 PERFORMANCE

Gross written premium for the year increased by 10% to £17,985m (2007: £16,366m), reflecting new business opportunities and the strengthening of the US dollar in the latter part of the year.

A number of syndicates have started trading in the past three years, bringing new business to the market. In addition, the peak in the oil price and increased commodity prices during the earlier part of the year brought additional premiums for the energy and cargo lines of business, among others. This offset weakening terms and conditions that reduced premium per risk written.

The depreciation in sterling has increased the value of business written in foreign currencies when reported in sterling in the results. The accounting convention is to recognise premiums at the rate prevailing when the contract is written, and with an average rate throughout the year of US$1.85:£1 in 2008 (2007: US$2.00:£1), this results in an estimated increase of 5% in reported premiums. In underlying currency, the true business growth is closer to 5% than the 10% headline figure.

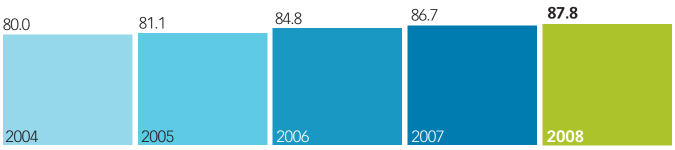
ACCIDENT YEAR RESULTS

Despite the high level of catastrophe losses occurring in 2008, Lloyd's achieved a near break-even accident year combined ratio of 100.5% (2007: 90.5%).

This includes a gain on exchange from non-translation of non-monetary items, which reduced the combined ratio in 2008 by 2.7%. This should be borne in mind when considering the performance by class in 2008.

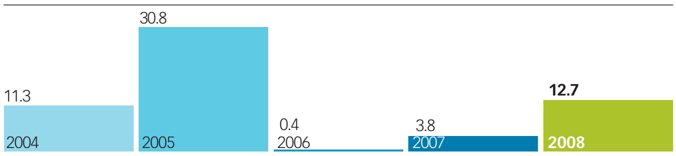
The combined ratio, excluding major losses, of 87.8% (2007: 86.7%) has been achieved through disciplined underwriting in the face of softening market conditions experienced in 2007 and 2008.

Accident year excluding major losses
(%)



Combined ratio

Major losses
(%)



Combined ratio

Sixteen named storms in the Atlantic basin made 2008 the fourth worst year on record for named storms. The length of the hurricane season was record breaking – with the last storm, Hurricane Paloma, developing as late as November. This was only the fourth major hurricane to develop in November since Atlantic storm records began.

While Lloyd's did not incur significant losses on all these events, the severity of Ike and Gustav led to substantial claims. The current estimated ultimate net loss to Lloyd's is £1,211m (US$2,180m) for Ike, and £219m (US$394m) for Gustav.

Ike was the most destructive hurricane of 2008. It made landfall in the US on 13 September as a strong Category 2 storm on the Saffir-Simpson scale, although its windfield and pressure characteristics were those of a much stronger storm.

It was extremely difficult to estimate the cost of Ike in the immediate aftermath, principally because of the size of the windfield and the storm surge impacts on coastal areas.

Catastrophe modelling agencies provided an initial range of claims estimates of US$6bn to US$18bn (onshore and offshore combined). Various (re)insurance companies reported potential industry losses ranging from US$10bn to US$16bn for the storm's onshore component. Offshore losses remained uncertain. Lloyd's advised a more conservative view in line with an aggregate industry loss for Gustav and Ike of between US$20bn and US$25bn. Subsequent year end reporting has produced estimated industry loss estimates of over US$20bn.

Industry loss estimates have increased since the Q3 estimates were announced by a number of primary insurance and reinsurance companies, The principal reasons for the increase are:

Firstly, the storm's spatial extent was underestimated. The area that experienced high wind speeds extended a long way both inland and along the Gulf Coast. Once Ike hit land, the winds persisted and continued to cause damage much further inland than would normally be associated with a hurricane. In addition, Ike encountered an extratropical frontal system in the northern US states, creating hurricane force winds in states such as Ohio.

Secondly, early assessments of the impact of coastal storm surge on land were inaccurate. Although flooding in and around Galveston was less extensive than initially feared one or two days before landfall, the coastal surge was experienced along large stretches of the Texas and Louisiana coastline. Offshore, the large windfield caused widespread platform damage in the Gulf of Mexico with some 1,450 of the Gulf's 3,800 oil and gas platforms exposed to hurricane force winds. Of these, 54 were subsequently confirmed as destroyed.

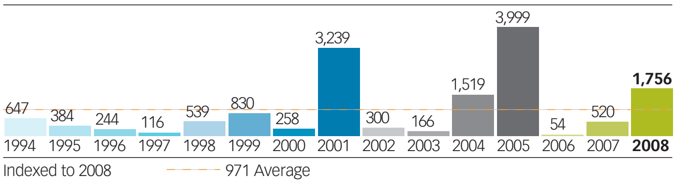
Lastly, offshore losses have historically proved difficult to estimate, and this again has proved to be the case with Ike. Initial estimates of losses around US$2-3bn, have increased to over US$4bn.

Early estimates suggested that Ike and Gustav losses would be borne mainly by direct insurers. The increase in loss estimates across the board has shifted the impact of the storms from primary insurers to reinsurers. Late advices such as the Louisiana cat pool have only served to exacerbate this.

Despite the exceptional nature of Hurricane Ike, the Lloyd's market was well prepared for a storm of this type. Since the mid-1990s, we have been using our Realistic Disaster Scenario (RDS) framework to manage peak catastrophe risk within individual syndicates and the market as a whole. The RDS framework regularly tests the market against necessarily severe catastrophe scenarios, involving claims of over US$100bn, including a Gulf of Mexico onshore and offshore loss event. The RDS for 2009 is being reviewed, following Ike, to reassess the assumptions, particularly regarding the impact on Offshore Energy.

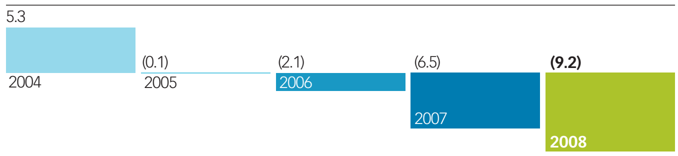
Largely as a consequence of Ike and Gustav, the level of catastrophe claims in 2008 was above the long-term average for the Lloyd's market.

Lloyd's major losses: net ultimate claims
(£m)



Lloyd's continues to benefit from prior year reserve movement, improving the combined ratio by 9.2% (2007: 6.5%). This was the fourth successive year of prior year surpluses. The strong levels of reserves support these releases, but future years are likely to see reductions in the levels of release.

Prior year reserve movement
(%)



Combined ratio

As in 2007, the emerging surpluses arise mainly on claims reserves established for business written during 2002-2006, where claims development remains benign and well within previous estimates.

The claims estimates for the 2005 US hurricanes have been stable and development on the longer-tail business written in the soft market conditions of 1997-2001 continues to be within expectations.

The surplus includes foreign exchange gains arising from the retranslation of assets and liabilities in foreign currency from opening rates of exchange to closing rates.

REINSURANCE PROTECTION

With respect to traditional reinsurance, there have been a number of credit downgrades during the year. The credit quality of the market's reinsurance cover remains extremely high, however, with over 95% rated A and above. The anticipated recoveries due within claims reserves have risen, principally due to the cost of Hurricane Ike and in sterling terms through the strengthening of the US dollar.

For non-traditional reinsurance, 2008 began with an anticipation that the trend of increasing catastrophe bond issues would continue. While the first half of the year produced a strong pipeline of securitisations, all issuances came to an abrupt halt in August/September. Liquidity in financial markets dried up and finally the collapse of Lehman Brothers signalled the end of any activity for 2008.

Along with the financial crisis, the increase in natural catastrophe activity has also increased investor uncertainty and reluctance to participate in catastrophe bond transactions. While principal remained untouched, the US windstorms had an effect on issuer perspectives, as fears mounted about having to pay higher interest rates for new catastrophe bond issuances. Credit risk concerns exacerbated the fall in investor confidence as existing bonds were downgraded by the rating agencies.

The uncertainty as to the direction of traditional reinsurance rates has also played a part as insurers considered their risk transfer options. Line of business, geography, and loss history influenced pricing, making generalisation difficult. Few could say with confidence that they knew where reinsurance rates were going, and the uncertainty led insurers to wait for the 1 January 2009 renewals to become evident before pursuing any further bond issuances.

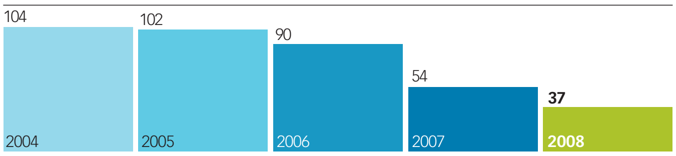
RESULT FOR THE CLOSED YEAR AND RUN-OFF YEARS OF ACCOUNT

The 2006 calendar year had one of the lowest catastrophe claims levels on record. This is reflected in the result of the 2006 underwriting year of account which closed with a profit of £4,035m. This includes the benefit arising from surpluses on the 2005 and prior reinsurance to close (RITC) received as at December 2007 of £964m.

In aggregate, run-off years reported an overall profit of £104m including investment income (2007: £75m) and syndicates backed by insolvent members supported by the Central Fund reported a small overall surplus.

In 2008, the market maintained its appetite for the RITC of orphan syndicates, and by the year end the number of underwriting years of account in run-off was significantly down. A number of specialist syndicates have been set up to underwrite third-party RITC and this has led to strong competition in the run-off market. No fewer than six managing agents have written RITC in the past two years, enabling 18 syndicates to close.

Years of account in run-off



The results of the major classes of business are discussed in detail on pages 61 to 67.

INVESTMENT REVIEW

Financial markets experienced unprecedented volatility throughout much of 2008. The US sub-prime mortgage crisis, which emerged during 2007, rapidly developed into a global financial crisis with sweeping consequences for nearly all asset classes.

As investor confidence in the credit quality of structured securities deteriorated, the value of these instruments fell significantly. Many banks held large amounts of these securities and increasingly hoarded their dwindling capital, causing credit conditions to tighten dramatically. As a result, liquidity all but disappeared in many financial markets and investors' risk appetite evaporated, causing further reductions in the value of riskier securities.

With financial markets closed, corporate entities, including banks, were unable to refinance maturing borrowings and some banks failed as confidence collapsed. The insolvency of Lehman Brothers in September dramatically increased fears about the integrity of the global financial system. Subsequently, global governments have committed substantial amounts of capital to ensure that markets continue to function and that credit remains available to consumers. These measures, however, could not prevent the global economic recession.

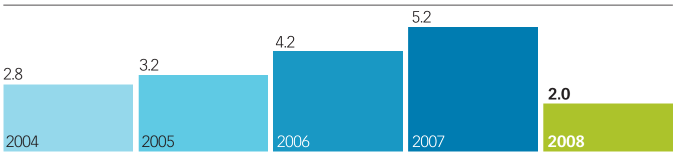
The list of types of investment which did not experience losses in 2008 is uncomfortably short. Even cash deposited with banks was not necessarily considered safe, as a number of institutions with respectable credit ratings required significant government support.

Equities fell faster than had been seen for three-quarters of a century, many structured debt securities lost a substantial proportion of their value and even highly rated and established corporate entities saw significant reductions in the value of their debt as the yields demanded by investors rose. Margins (yield in excess of the risk free rate) on highly rated 'AA' UK corporate securities maturing in three to five years rose from 1.6% to 5.2% during 2008. Hedge funds generally failed to live up to their promise – to be able to make money irrespective of underlying market conditions – and many experienced large losses. Only government debt proved robust in this environment. As interest rates were cut repeatedly, the yield on UK government bonds maturing in two years fell from 5.2% to 1.1% in the final six months of 2008, generating significant capital gains on these securities. Government bonds in most developed economies were similarly affected.

Syndicate premium assets form the largest element of investment assets at Lloyd's. Managing agents are responsible for the investment of these funds, which are used to meet insurance claims as they become payable. This need to ensure sufficient liquidity, often at relatively short notice, has traditionally led syndicates to adopt conservative investment policies using cash and high quality fixed interest securities of relatively short duration. More recently, a number of syndicates have diversified their investments to include elements of more volatile asset classes, such as equities, hedge funds and lower rated debt. Exposures to these riskier asset classes, however, generally remain limited and are less than 5% in aggregate; high quality, short dated, fixed interest securities continue to dominate syndicate portfolios. The predominance of more liquid investments has ensured that syndicates remain able to liquidate assets as required to meet cash flow needs, notwithstanding the significant reduction in capital supporting secondary trading in many areas of the financial markets.

Investment returns varied significantly between syndicates in 2008. Some syndicates experienced negative returns, driven by exposures to more volatile asset classes, but most of these limited their losses by maintaining significant exposures to more conservative asset classes. Conversely, many syndicates benefited from significant government bond exposures and generated relatively high returns. Overall, syndicate investments returned £521m, or 2.0% (2007: £1,226m, 5.2%). Investments are valued at market prices and unrealised gains and losses are included within quoted investment returns. Although the contribution from syndicate investments was well below the return achieved in 2007, it remained significant in 2008 and represented a solid performance in very difficult market conditions.

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' discretion. A notional investment return on members' capital of £271m or 2.7% (2007: £653m, 6.0%) has been included in the Pro Forma Financial Statements (PFFS). This is based on the investment disposition of the relevant assets and market index returns. The investment return on Lloyd's central assets is also included in the PFFS. This was £165m or 7.8% in 2008. (2007: £128m, 6.6%) The investment performance of central assets is discussed on page 99. The total contribution from investment returns, including syndicate assets, members' capital and central assets, was £957m or 2.5%.(2007: £2,007m, 5.6%).

RESULTS SUMMARY

Lloyd's achieved a profit for the financial year before tax of £1,899m (2007: profit of £3,846m) and a combined ratio of 91.3% (2007: 84.0%). 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 pro forma financial statements (PFFS) is set out in note 2 on page 74. The syndicate annual accounts reported an aggregate profit of £1,523m (2007: profit of £3,029m). These results are reported in a separate document (the Aggregate Accounts) and can be viewed at www.lloyds.com/financialreports.

REINSURANCE
STRONG DEMAND FOR LLOYD'S SECURITY

2008 highlights

- High catastrophe loss experience worldwide.
- Rating environment remained strong.

2008 combined ratio

Accident year	95.9%
Prior year reserve movement	(12.1%)
Calendar year	83.8%

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 (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 companies for their peak earthquake and windstorm exposures. In addition, many syndicates underwrite accident & health and liability reinsurance on a facultative basis, although the amount of casualty treaty business written is limited. The sector also includes class specific reinsurance, including energy, marine and aviation.

2008 PERFORMANCE

Lloyd's reported gross written premium for 2008 of £6,298m (2007: £5,453m), an increase of 15%.

The Lloyd's market's excellent credit ratings, together with its effective broker subscription market have led to increased demand from insurers to place their reinsurance programmes with Lloyd's security.

ACCIDENT YEAR PERFORMANCE

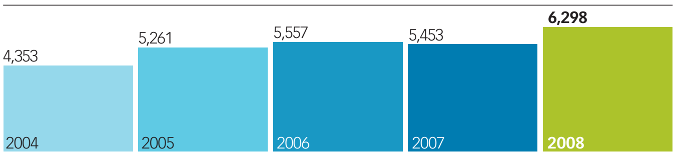
The accident year combined ratio for 2008 was 95.9% (2007: 86.3%). The increase in claims through Gustav and Ike makes 2008 one of the worst years ever for catastrophes in the US. And while the US windstorms tended to grab the headlines in 2008, the rest of the world was also affected by natural catastrophes. China experienced both snowstorm and earthquake events; Australia had both floods and hail; and Europe saw Windstorm Emma and hailstorms.

Other major losses that affected the Lloyd's market in 2008 were the Californian fires and the Severstal furnace explosion.

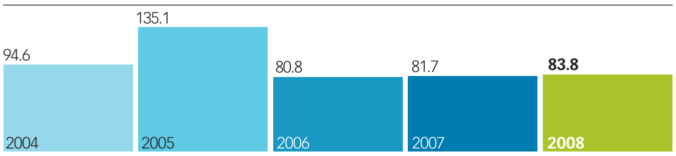
PRIOR YEAR RESERVE MOVEMENT

The prior year reserve movement was a surplus of 12.1% (2007: 4.6%). This follows the release of catastrophe risk loadings within claims reserves, which can be released due to the limited claims experience in the last two years.

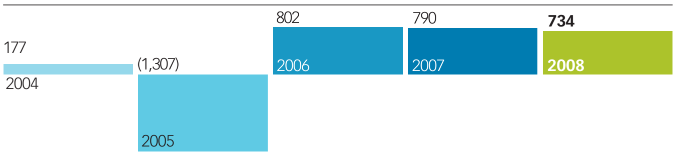
Gross written premium
(£m)



Combined ratio
(%)



Underwriting result
(£m)



LOOKING AHEAD

The January 2009 reinsurance renewal season showed that rates had stabilised and some rises had been achieved. The balance between underlying improvement in terms and conditions and re-rating accounts for changes in risk profile following loss experience remains unclear. It would appear, however, that the reinsurance market is a driving force in applying pressure on primary insurers to increase rates. Lloyd's is well placed to take advantage of opportunities that arise, but there is no room for complacency. Rapidly changing exposures must be properly understood and factored into pricing. The recession will mean a very challenging claims environment for many classes – robust risk selection and cycle management are now even more crucial.

All of the published forecasts for Atlantic hurricane activity in 2009 are above the 1950-2008 long-term average. For example, the Colorado State University team are forecasting 14 named storms and three major hurricanes.

While the focus has been on the recent level of hurricanes in the Gulf of Mexico, an area that has not received much attention, but may in the future, is a major earthquake related catastrophe. As the insurance industry has not been hit by a major earthquake for some time, the likelihood that one will occur is arguably increasing.

Demand for reinsurance is likely to increase in 2009. A number of industry balance sheets have suffered due to the crisis in financial markets as well as higher attritional and catastrophe loss experience. Surplus capital has been eroded and many primary insurers will look to de-risk their balance sheets and modify their own risk appetite; reinsurance protection is a valuable tool available to protect against further capital depletion. Optimism is more focused on US business that renews later in the year, where the recent loss experience means that an increase in rates should be achievable.

PROPERTY
RATE SOFTENING SLOWS, BUT MARGINS INSUFFICIENT TO MEET CATASTROPHE CLAIMS

2008 highlights

- → Hurricane claims and major risk losses push current trading into loss.
- → Recent years produce significant reserve releases.

2008 combined ratio

Accident year	103.2%
Prior year reserve movement	(6.5%)
Calendar year	96.7%

The Lloyd's property sector covers both commercial and private property, with the US representing the largest market. Business is written via the broker distribution chain or through appointed local agents and coverholders.

2008 PERFORMANCE
Gross written premium for the Lloyd's property sector in 2008 was £3,971m (2007: £3,809m), an increase of 4%.

During the year US catastrophe rates fell to their pre Katrina/Rita/Wilma levels, and some indices showed rates returning to 2002 levels or below. The first half of the year saw rate reductions of over 10% and, although the level of reductions slowed in the second half after Hurricanes Gustav and Ike, rates have not yet recovered. Higher reinsurance costs put a further squeeze on margins in a soft market.

The market for terrorism insurance has become increasingly competitive. The implementation of the Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) for 2008, which extended cover to include both domestic and international terrorism, has reduced the demand for standalone policies covering US risks. Demand for this cover is expected to diminish further if the broader property market reduces the number of terrorism exclusions.

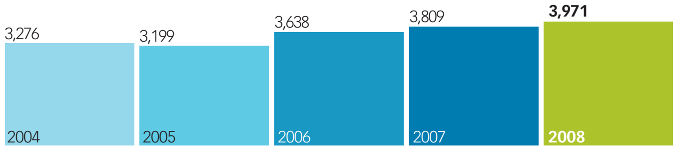
ACCIDENT YEAR PERFORMANCE
The increases in loss levels caused the accident year loss ratio to rise to 103.2% (2007: 92.3%).

The Lloyd's market was heavily impacted by Hurricanes Gustav and Ike, which affected states as far inland as Ohio.

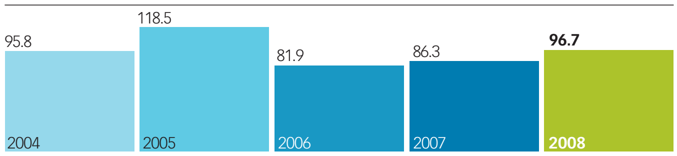
As well as the catastrophe losses there was an increase in the frequency of large losses including the incidents at the Severstal furnace and Universal Studios in the US.

PRIOR YEAR RESERVE MOVEMENT
Further surpluses were generated in 2008, as releases from reserves established in 2002 to 2006 continued, while 2005 US hurricane losses remained stable. This improved the combined ratio by 6.5% (2007: 6.0%).

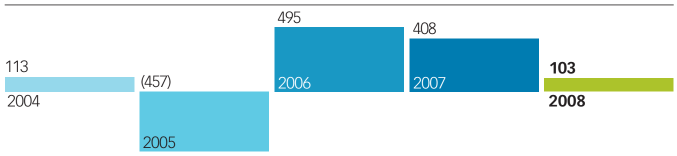
Gross written premium
(£m)



Combined ratio
(%)



Underwriting result
(£m)



LOOKING AHEAD
In 2009, the downward trend in rates is expected to reverse as direct property writers feel the pressure of higher reinsurance and capital costs.

On the other hand, a higher frequency of loss will minimise any anticipated margin in this business. The increased value of the US dollar will continue to squeeze the cost of capital for those entities backed by non-US dollar assets. Ultimately this will force insurers to raise prices.

Should capacity suddenly be reduced by, for instance, the withdrawal of one or two larger players, rate increases could follow quickly.

CASUALTY
RECESSION MAY HERALD SURGE IN CLAIMS FREQUENCY

2008 highlights

- Impact of financial crisis spreads across all liability lines.
- Prior year releases of £227m.

2008 combined ratio

Accident year	103.9%
Prior year reserve movement	(8.8%)
Calendar year	95.1%

Lloyd's casualty sector covers professional indemnity, medical malpractice, accident and health, general liability and employers' liability. Casualty business is written worldwide with the largest markets being in the US, UK and Europe.

2008 PERFORMANCE

2008 saw gross written premium of £3,762m (2007: £3,364m), an increase of 12%.

In the US, general liability rates peaked in 2003/04 and have been falling by an average of 10% each year since then. In 2008, transportation, energy and manufacturing rates came under the most pressure.

International professional indemnity (PI) rates showed a patchy improvement following the September banking and economic crisis. For some business, rates remained flat; but in other cases reductions of around 5% were being given, although this was less than previous reductions of 10% or more.

ACCIDENT YEAR PERFORMANCE

The casualty sector achieved an accident year combined ratio of 103.9% (2007: 101.8%).

While we expect claims resulting from financial turmoil, no firm loss amounts have so far been reported. Attritional losses did rise compared to 2007 and are expected to increase much further in 2009 and 2010.

PRIOR YEAR RESERVE MOVEMENT

Prior year reserve movement improved the combined ratio by 8.8% (2007: 9.1%). For the fourth successive year underlying claims development led to a surplus. The pressure on margins and terms and conditions, together with the consequences of the financial crisis, may well reduce the levels of release in future years.

LOOKING AHEAD

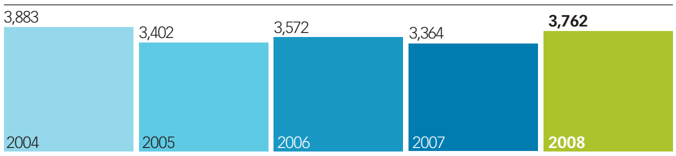
The full impact of the economic recession will begin to materialise in 2009 and is expected to continue through to 2010. The widely anticipated surge in claims has been trailed extensively in the press and at conferences but the market response to this potential claims exposure is still mixed.

Insurers remain concerned by the prospect of rising claims driven, for example, by increased litigation, particularly in the US. Some are already seeing an increase in claims notifications that they regard as directly related to the financial crisis.

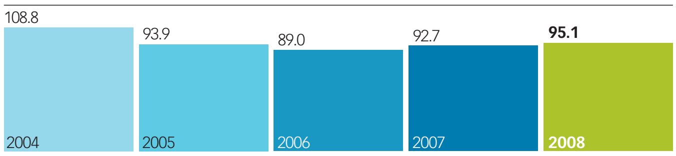
Any increase in rates will depend on the level of capacity in the casualty market. Going into 2009 there appears to be more than enough, making rate rises difficult to achieve. However, capacity may reduce if some insurers choose to use their capacity in other markets.

A longer-term factor that may affect the level of future claims is whether or not Europe adopts class actions closer to the US model. Currently European litigants must opt in to an action, in contrast to the US, where all possible litigants are assumed to be included in the action unless they opt out. The opt-in basis makes it harder to establish a class action. Another key difference is that in the US the award is decided by jury – considered to be one of the main causes of the high level of tort costs in the US.

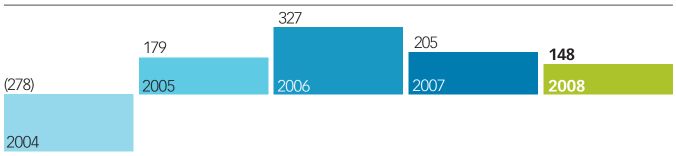
Gross written premium
(£m)



Combined ratio
(%)



Underwriting result
(£m)



The cumulative impact of sub-prime related losses, the failure and subsequent bail-out of US banks and finally the Madoff fraud have led to significant rate increases for US Financial Institutions (FI) business – E&O and D&O liability – at 1 January renewal.

These increases are gradually extending to non-US domiciled FI business as the full extent of the European exposures to Madoff emerges. The significant reduction in FI reinsurance has also encouraged primary underwriters to improve their rates in order to secure and cover the increased costs.

The non FI Directors and Officers (D&O) and Errors and Omissions (E&O) covers have shown a less pronounced movement at renewal. International E&O covers (including the UK) have generally been renewed at either unchanged rates or small increases. International D&O rates are still under pressure as there have been very few claims. There is anecdotal evidence that the first and second quarters of 2009 will start to show evidence of increasing claims activity as the full impact of the recession related losses begins to be apparent.

UK employers' liability had still not shown major rate increases at 1 January renewal. But here, too, the increased incidence of recession related claims in the first two quarters – for example, stress caused by threat of redundancy – will start to impact results that have so far been satisfactory due to low claims frequency. To a lesser extent, general liability business will follow the same pattern.

The overall picture for casualty business is cautiously optimistic for 2009, as the combined effects of Lloyd's financial standing and a continuing deterioration in the economic environment encourage underwriters to adopt a more proactive stance at 1 April and 1 July renewals.

MARINE
RECENT STRONG PERFORMANCE UNDER THREAT AS WORLD ECONOMIES CONTRACT

2008 highlights

- Premiums continued to rise on the back of spiralling commodity prices earlier in the year.
- Limited incidence of total losses.

2008 combined ratio

Accident year	92.4%
Prior year reserve movement	(7.8%)
Calendar year	84.6%

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

2008 PERFORMANCE
The marine sector achieved gross written premium of £1,334m (2007: £1,226m), an increase of 9%.

The earlier part of the year saw the escalating cost of raw materials and this fed through into higher cargo and hull premium volumes.

The marine market remained soft throughout 2008 as an abundance of capacity more than offset any reaction to the increase in attritional losses. The general economic downturn caused freight rates to plummet in the second half of 2008 and this has led to reducing fleet values. The industry has therefore been faced with the problem of insured values being greater than current market value.

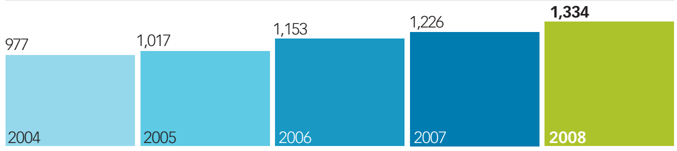
ACCIDENT YEAR PERFORMANCE
The accident year combined ratio was 92.4% (2007: 95.0%) reflecting the absence of significant total losses. Major partial losses, however, continued to increase, both in frequency and in cost. The rise in frequency can be attributed, at least in part, to the shortage of trained crews. Lack of experience can cause losses through poor navigation or poor vessel maintenance.

Towards the end of 2008 there was a rise in pirate activity off the coast of East Africa. It was not just the rise in the number of vessel hijackings that caused concern, but also the size of the ships being targeted. The hijacking of the oil tanker Sirius Star took these events to a new level – both in the size of the ship the pirates were prepared to tackle, and the fact that it was 450 nautical miles off the coast of Kenya when it was boarded.

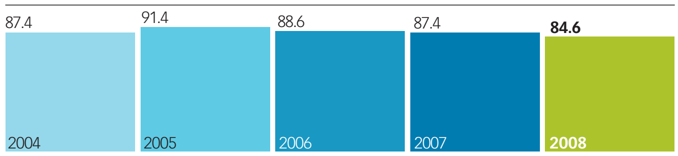
The marine liability account has suffered from the escalating cost of claims settlements – wreck removal costs on the Napoli and the New Flame have increased – and higher reinsurance costs.

PRIOR YEAR RESERVE MOVEMENT
An overall release from prior years' reserves reduced the combined ratio by 7.8% for the year (2007: 7.6%). This has continued the trend for prior years to develop within expectation, with a surplus arising for the fifth consecutive year.

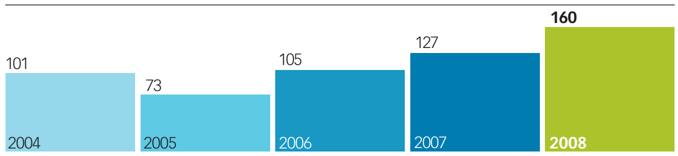
Gross written premium
(£m)



Combined ratio
(%)



Underwriting result
(£m)



LOOKING AHEAD
Hull underwriters are undertaking critical price renegotiations after the collapse of ship values amid the crisis that stalled capital markets. Most of the world merchant fleet, estimated to be US$1.3trn shortly before the upheavals at the end of last year, has fallen in value, giving rise to 'moral hazard' – the temptation for less scrupulous ship operators to commit fraud. Reassessment will reduce global marine hull insurance premium; it will also reinforce the need for tighter underwriting.

Against this background, the market is hardening very slightly and rate increases are expected to gather pace through 2009. However, hull premium income may decline due to the reduction in agreed values. There is still no sign of upward movement in deductibles, which have not changed since the mid '90s.

The economic downturn will also impact the cargo market. The value of cargoes to be transported is reducing – oil in particular, but also all other commodities from foodstuffs to metals. While cargo rates remain flat, this will reduce premium income for underwriters.

ENERGY
HURRICANE CLAIMS PRODUCE SECOND MAJOR LOSS IN FOUR YEARS

2008 highlights

- Offshore energy market hit by Gulf of Mexico hurricanes.
- Volatile results reflect the sector's catastrophe risk.

2008 combined ratio

Accident year	132.0%
Prior year reserve movement	(8.2%)
Calendar year	123.8%

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 (GOM).

2008 PERFORMANCE

The Lloyd's energy sector achieved gross written premium of £1,150m (2007: £1,019m), an increase of 13%.

At the beginning of 2008 the market was soft, with onshore energy rates seeing price reductions typically around 25-35%. However, increasing losses as the year progressed had the effect of reversing the trend so that by the end of the year rate increases of 10% and more were being achieved.

The GOM has seen five named, major windstorms in the last five years. In 2004 Hurricane Ivan resulted in record losses for the offshore energy insurance industry. It was followed in 2005 by Hurricanes Katrina and Wilma. The next two years provided some respite from losses but also saw rates fall. And then, in 2008, Hurricanes Gustav and Ike struck, with Ike proving to be the second largest energy loss ever, after Katrina.

ACCIDENT YEAR PERFORMANCE

The accident year combined ratio for 2008 was 132.0% (2007: 77.3%). This high combined ratio was inevitable after the impact of Ike and Gustav on the oilfields in the GOM.

Ike has required a further revision to the estimating of losses from GOM windstorms. As a Category 2 storm, Ike was not expected to have a significant impact, but this assessment ignored Ike's windfield that caused damage over a much greater area than anticipated.

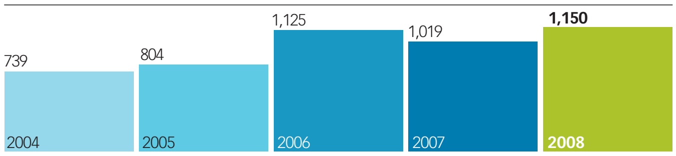
While the impact of Ike and Gustav in the GOM generated the most noteworthy losses, the industry also suffered other large losses in 2008, particularly in the onshore market.

The claims ratio, excluding operating expenses, climbed to 90% of net premiums. This included the benefit of considerable reinsurance recoveries with Ike losses exceeding primary insurers' retentions. The gross claims ratio of 119% of gross premiums reflects the high level of catastrophe risk inherent in this class. This volatility demands high capital requirements as the exposures to both large single risk losses and natural catastrophes are key drivers of peak losses for many syndicates. Rating in this class must bear in mind the returns required over time to compensate for the potential for large losses to occur.

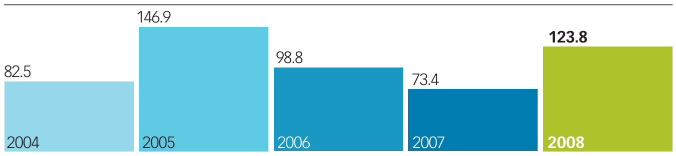
PRIOR YEAR RESERVE MOVEMENT

The prior year reserve movement improved in 2008 as the loss estimates for the 2005 hurricanes remained stable, resulting in a surplus on prior years of 8.2% (2007: 3.9%).

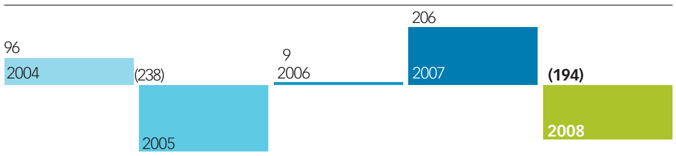
Gross written premium
(£m)



Combined ratio
(%)



Underwriting result
(£m)



LOOKING AHEAD

While there have been considerable increases in the insured values, the retention levels have remained relatively static. Retentions and premiums need to be increased to the point where the offshore energy sector's profitability can withstand another major windstorm.

The high frequency of major losses requires the offshore energy insurance industry to radically rethink the way that it offers insurance in the GOM. Achieving substantial increases in rates is part of the answer but another significant contribution can be made by changing the amount of exposure that the energy industry retains itself.

There are concerns over the level of capacity that will be available in this sector throughout 2009. As a result, some clients are bringing forward their renewal dates rather than wait until June when there may be no more capacity available.

While the GOM is the main focus of the need for change, there have been a number of significant energy losses in 2008 and rates and conditions are likely to be amended across the whole onshore and offshore energy account.

MOTOR
HIGHLY COMPETITIVE MARKET CONTINUES ITS BATTLE WITH CLAIMS INFLATION

2008 highlights

- Marginal results reflect soft market conditions.
- Lloyd's motor sector focuses on niche markets.

2008 combined ratio

Accident year	100.9%
Prior year reserve movement	(1.3%)
Calendar year	99.6%

This class has become less prominent in the market in recent years, but remains an important part of Lloyd's overall diversified business. In the face of intense competition in 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. As a result, less than half the market's premium income now 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% of business now originating outside of the UK.

2008 PERFORMANCE

Gross written premium in 2008 for the Lloyd's motor sector was £939m (2007: £983m), a decrease of 4%.

For UK motor, 2008 saw a return to rate increases at or above claims inflation for the personal lines sectors of the motor market and profitability returned to more sustainable levels.

The commercial areas of fleet, commercial vehicles and taxis have yet to realise the same levels of rate increases and while profitability was feasible in some areas, this arena remained challenging.

Claims inflation continues at around 4.5%. Credit hire costs have grown significantly in recent years to become a large element of claims costs. This is an issue that needs addressing across the market. Courts Act claims remain a concern but, to date, there are very few in the market.

Lloyd's overseas motor business is diverse and rates and performance vary significantly between territories. A large proportion of this business emanates from North America and relates to physical damage exposures for private auto and static risks.

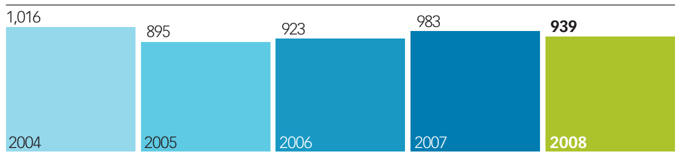
ACCIDENT YEAR PERFORMANCE

The trend for claims costs to outstrip inflation continues. Personal injury costs are the main driver of this and continue to increase through higher medical and legal costs. Combined with continuing soft market conditions, this resulted in a further accident year loss of 100.9% (2007: 104.8%).

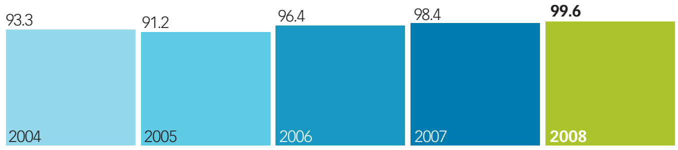
PRIOR YEAR RESERVE MOVEMENT

Prior year reserve movement improved the combined ratio by 1.3% (2007: 6.4%) as claims continue to develop as expected.

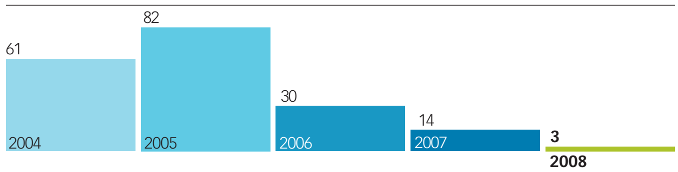
Gross written premium
(£m)



Combined ratio
(%)



Underwriting result
(£m)



LOOKING AHEAD

2009 should show further price improvement. UK personal lines motor products are already realising improvements in rates and it is expected that commercial motor products will follow suit. The current recession has impacted expected investment returns and with some insurers reporting losses there will be added pressure on rates to increase throughout 2009.

UK Ministry of Justice reforms are expected in October 2009. The main impact on insurers is the need to ensure they are in a position to make a decision on liability within 15 days. If they are unable to do so, there will be a cost implication in the handling of road traffic accident personal injury claims under £10,000. Fast track limits will be raised to £25,000 from £15,000, enabling these claims to be dealt with faster at lower cost.

Over 60% of Lloyd's UK motor business is fleet/commercial vehicle, and although commercial fleet rates are slower to respond than private car rates, there are reports that they are now also starting to improve. The impact of the financial crisis on the motor industry may see an increased tendency to claim as well as fraudulent claims – two trends which are closely linked to economic conditions and will require close monitoring.

Fraud remains a huge issue for the industry, particularly in an economic downturn. The industry continues to improve and refine fraud strategies to combat this growing problem.

AVIATION
POOR RATING LEVELS UNABLE TO COVER NORMAL LOSS EXPERIENCE

2008 highlights

- A return to longer-term claims experience highlights inadequate rating levels.
- Overall profit dependent on reserve releases.

2008 combined ratio

Accident year	110.5%
Prior year reserve movement	(23.7%)
Calendar year	86.8%

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

2008 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 £481m (2007: £464m), an increase of 4%. In 2008, Lloyd's syndicates wrote £262m of aviation business on a facultative and treaty reinsurance basis (2007 figures not available).

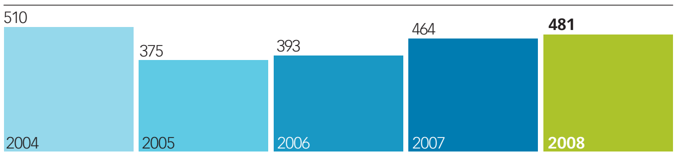
Rates in the aviation market have been in steady decline since the rise that immediately followed the heavy 9/11 and Queens losses in 2001. This trend continued in 2008 until the final quarter of 2008, which saw some improvement in airline rates and a more stable rating environment elsewhere.

ACCIDENT YEAR PERFORMANCE
The accident year combined ratio for 2008 was 110.5% (2007: 102.8%). The reasons for this further increase in the ratio are similar to those highlighted last year: continuing softening market conditions coupled with an increase in loss incidence.

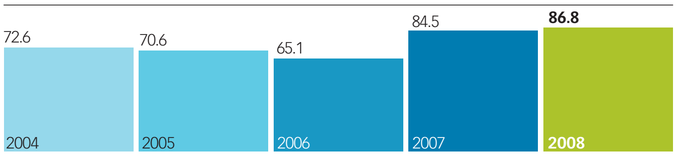
When the Air New Zealand Airbus 320 leased to XL crashed in the Mediterranean in November 2008 it was the 24th Western-built aircraft to suffer a total loss in the year, bringing the total hull loss figure for the year to over US$350m.

PRIOR YEAR RESERVE MOVEMENT
Surpluses on prior years' claims reserves improved the combined ratio by 23.7% (2007: 18.3%), continuing the trend for benign claims development across the entire portfolio. This reflects the low incidence of loss in recent years, which is considerably lower than the long-term average.

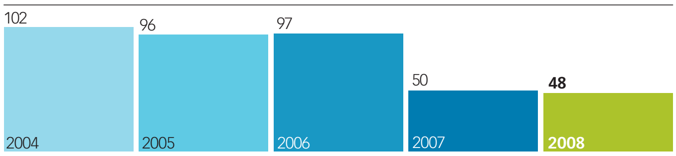
Gross written premium
(£m)



Combined ratio
(%)



Underwriting result
(£m)



LOOKING AHEAD
The economic downturn will have consequences for airline underwriters, particularly in 2009, as the reduction in passengers and flights will inevitably result in less premium unless there is a substantial rise in rates. The demise of a number of carriers, XL Leisure Group being the largest to date, provides another challenge to maintaining premium levels.

There is still overcapacity in this market, but lines are shrinking and further tightening is expected in 2009 as capital providers insist on higher returns to offset the increased cost of capital.

General aviation continues to be keenly rated. Claims experience is generally good, so that the sector remains profitable, but not enough to offset the wider problems in aviation.

THE MARKET'S FINANCIAL RESULTS

REPORT OF ERNST & YOUNG LLP TO THE COUNCIL OF LLOYD'S ON THE 2008 LLOYD'S PRO FORMA FINANCIAL STATEMENTS

We have examined the Lloyd's pro forma financial statements ('PFFS') for the year ended 31 December 2008, 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 17 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 2008 have been properly prepared in accordance with the basis of preparation set out in note 2.

Ernst & Young LLP, London

23 March 2009

PRO FORMA PROFIT AND LOSS ACCOUNT

for the year ended 31 December 2008

Technical account	Note	2008 £m	2008 £m	2007 £m	2007 £m
Gross written premiums – continuing operations			**17,945**		16,349
– discontinued operations	5		**40**		17
	9		**17,985**		16,366
Outward reinsurance premiums			**(3,768)**		(3,110)
Premiums written, net of reinsurance			**14,217**		13,256
Change in the gross provision for unearned premiums		**(558)**		(237)	
Change in provision for unearned premiums, reinsurers' share		**137**		78	
			(421)		(159)
Earned premiums, net of reinsurance			**13,796**		13,097
Allocated investment return transferred from the non-technical account			**543**		1,223
			14,339		14,320
Claims paid					
Gross amount		**9,736**		8,741	
Reinsurers' share		**(2,158)**		(2,515)	
			7,578		6,226
Change in provision for claims					
Gross amount		**1,777**		(1,278)	
Reinsurers' share		**(891)**		1,599	
			886		321
Claims incurred, net of reinsurance			**8,464**		6,547
Net operating expenses	11		**4,134**		4,451
Balance on the technical account for general business			**1,741**		3,322
Attributable to: – continuing operations			**1,624**		3,290
– discontinued operations	5		**117**		32
Total			**1,741**		3,322
Non-technical account					
Balance on the technical account for general business			**1,741**		3,322
Syndicate investment return	12	**521**		1,226	
Notional investment return on funds at Lloyd's	6	**271**		653	
Investment return on Society assets		**165**		128	
		957		2,007	
Allocated investment return transferred to the technical account		**(543)**		(1,223)	
			414		784
Other income			**75**		89
Contribution to Equitas-Berkshire Hathaway transaction			**–**		(90)
Other expenses			**(331)**		(259)
Profit for the financial year before tax	8		**1,899**		3,846

Statement of total recognised gains and losses	Note	2008 £m	2007 £m
Profit for the financial year		**1,899**	3,846
Other recognised gains and losses		**619**	106
Total recognised gains and losses	8	**2,518**	3,952

PRO FORMA BALANCE SHEET
as at 31 December 2008

	Note	2008 £m	2008 £m	2007 £m	2007 £m
Investments					
Financial investments	13		**34,942**		29,484
Deposits with ceding undertakings			**10**		9
Reinsurers' share of technical provisions					
Claims outstanding		**10,504**		7,449	
Unearned premiums		**1,167**		841	
			11,671		8,290
Debtors					
Debtors arising out of direct operations		**4,663**		3,428	
Debtors arising out of reinsurance operations		**3,763**		2,918	
Other debtors		**419**		318	
			8,845		6,664
Other assets					
Tangible assets		**30**		26	
Cash at bank and in hand	14	**9,428**		7,497	
Other		**8**		28	
			9,466		7,551
Prepayments and accrued income					
Accrued interest and rent		**125**		144	
Deferred acquisition costs		**2,064**		1,656	
Other prepayments and accrued income		**209**		155	
			2,398		1,955
Total assets			**67,332**		53,953
Capital and reserves					
Members' funds at Lloyd's	6	**10,630**		9,858	
Members' balances	15	**2,562**		2,652	
Members' assets (held severally)		**13,192**		12,510	
Central reserves (mutual assets)		**990**		939	
	8		**14,182**		13,449
Subordinated debt			**586**		516
Subordinated perpetual capital securities			**496**		496
Capital, reserves and subordinated debt and securities			**15,264**		14,461
Technical provisions					
Provision for unearned premiums		**9,043**		7,282	
Claims outstanding		**38,420**		28,971	
			47,463		36,253
Deposits received from reinsurers			**161**		42
Creditors					
Creditors arising out of direct insurance operations		**770**		697	
Creditors arising out of reinsurance operations		**2,517**		1,534	
Other creditors including taxation		**883**		774	
			4,170		3,005
Accruals and deferred income			**274**		192
Total liabilities			**67,332**		53,953

Approved and authorised for issue by the Council of Lloyd's on 23 March 2009 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 2008

	2008 £m	2007 £m
Profit on ordinary activities before tax	**1,899**	3,846
Depreciation	**3**	3
Realised and unrealised (gains)/losses and foreign exchange	**(4,643)**	(157)
Net purchase of investments	**(44)**	(1,576)
Notional return on funds at Lloyd’s	**(271)**	(653)
Increase/(decrease) in technical provisions	**7,800**	585
(Increase)/decrease in debtors	**(2,656)**	243
Increase/(decrease) in creditors	**1,293**	(15)
Cash generated from operations	**3,381**	2,276
Tax paid	**(54)**	(20)
Net cash from operating activities	**3,327**	2,256
Cash flows from financing activities		
Net profits paid to members	**(2,201)**	(1,537)
Net movement in funds at Lloyd’s	**772**	(1,424)
Capital transferred into syndicate premium trust funds	**107**	322
Interest paid	**(74)**	(46)
Net increase/(decrease) in cash holdings	**1,931**	(429)
Cash holdings at 1 January	**7,497**	7,926
Cash holdings at 31 December	**9,428**	7,497

NOTES TO THE PRO FORMA FINANCIAL STATEMENTS
as at 31 December 2008

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 83 to 137.

The Aggregate Accounts do not present a consolidated view of the results of Lloyd's business taken as a single entity. In particular, each managing agent selects the accounting policies most appropriate to its managed syndicates. Where UK GAAP permits different accounting policies and managing agents have adopted various accounting treatments, these are reflected in the PFFS without making consolidation adjustments. In addition, the PFFS do not eliminate inter-syndicate reinsurances.

The aggregate of syndicate annual accounts report the audited results for calendar year 2008 and the financial position at 31 December 2008 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 82). The Aggregate Accounts are reported as a separate document and can be viewed at www.lloyds.com/financialreports. During 2008, certain syndicates changed their accounting policies in relation to foreign exchange resulting in a restatement of the comparative figures for 2008 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 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 82. 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. Where Lloyd's is the investment manager for FAL, the actual return achieved has been included. For other assets the notional investment return, net of management fees, 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 2008

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 2008 and earlier years include those members' results and at the balance sheet date will report the outstanding liability within members' balances.

(3) 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 £50m (2007: £101m). 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. The Society financial statements on pages 105 to 137 provide additional information.

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. In particular, in certain circumstances, UK GAAP permits various accounting treatments for the movement in foreign exchange. The following accounting policies 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.

Outwards reinsurance premiums

Outwards reinsurance premiums 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.

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.

3. ACCOUNTING POLICIES NOTES CONTINUED

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. Non-monetary assets and liabilities at the balance sheet dates, primarily deferred acquisition costs and unearned premiums, are maintained at the rate of exchange rate ruling when the contract was entered into (or the approximate average rate). Resulting exchange differences on translation are recorded in the profit and loss account.

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.

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.

Members that only participate on one syndicate may 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 108 to 112.

4. VARIABILITY

Calendar year movements in reserves are based upon best estimates as at 31 December 2008 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.

NOTES TO THE PRO FORMA FINANCIAL STATEMENTS CONTINUED

as at 31 December 2008

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 2008, the results for that business have also been reported as discontinued in the 2007 comparative figures.

6. MEMBERS' FUNDS AT LLOYD'S

The valuation of members' FAL in the balance sheet totals £10,630m (2007: £9,858m).

The notional investment return on FAL included in the non-technical profit and loss account totals £271m (2007: £653m).

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 £198m (2007: £296m) in the technical account and a loss of £93m (2007: £132m) 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	2008 £m	2007 £m
Result per syndicate annual accounts	**1,523**	3,029
Result of the Society	**102**	164
Central Fund claims and provisions (credit)/charge in Society financial statements	**(6)**	(18)
Central Fund recoveries from insolvent members	**(21)**	(48)
Taxation charge in Society financial statements	**40**	66
Notional investment return on members' funds at Lloyd's	**271**	653
Society income not accrued in syndicate annual accounts	**(10)**	–
Result on ordinary activities before tax	**1,899**	3,846

Statement of total recognised gains and losses	2008 £m	2007 £m
Result for the financial year	**1,899**	3,846
Foreign currency movements in the syndicate annual accounts	**659**	73
Other recognised gains and losses per syndicate annual accounts	**11**	(4)
Other recognised gains and losses of the Society	**(51)**	37
Total recognised gains and losses	**2,518**	3,952

Capital and reserves	2008 £m	2007 £m
Net assets per syndicate annual accounts	**2,502**	2,523
Net assets of the Society	**990**	939
Central Fund claims and provisions	**102**	129
Members' funds at Lloyd's	**10,630**	9,858
Unpaid cash calls reanalysed from debtors to members balances	**(32)**	–
Society income receivable not accrued in syndicate annual accounts	**(10)**	–
Total capital and reserves	**14,182**	13,449

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.

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.

2008	**Gross written premiums £m**	**Net earned premium £m**	**Result £m**
Reinsurance	**6,298**	**4,522**	**734**
Property	**3,971**	**3,125**	**103**
Casualty	**3,762**	**3,005**	**148**
Marine	**1,334**	**1,041**	**160**
Energy	**1,150**	**814**	**(194)**
Motor	**939**	**897**	**3**
Aviation	**481**	**363**	**48**
Life	**49**	**28**	**(2)**
Total from syndicate operations	**17,984**	**13,795**	**1,000**
Transactions between syndicates and the Society (notes 2 and 8) and insurance operations of the Society	**1**	**1**	**198**
Total per PFFS	**17,985**	**13,796**	**1,198**

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
Energy	1,019	774	206
Motor	983	866	14
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

10. LIFE BUSINESS

The PFFS include the results of all life and non-life syndicates transacting business during 2008. 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

	2008 £m	2007 £m
Acquisition costs	**3,897**	3,519
Change in deferred acquisition costs	**(177)**	(70)
Administrative expenses	**1,267**	1,117
	4,987	4,566
(Profit)/loss on exchange	**(853)**	(115)
	4,134	4,451

NOTES TO THE PRO FORMA FINANCIAL STATEMENTS CONTINUED

as at 31 December 2008

12. SYNDICATE INVESTMENT RETURN

	2008 £m	2007 £m
Income from investments	**1,064**	1,029
Net realised (losses)/gains on investments	**(60)**	57
Net unrealised (losses)/gains on investments	**(452)**	165
Investment management expenses, including interest	**(31)**	(25)
	521	1,226

The breakdown of the society investment return is provided in the Society's financial statements on page 117. This analysis is not appropriate for the notional investment return on funds at Lloyd's.

13. FINANCIAL INVESTMENTS

	2008 £m	2007 £m
Shares and other variable yield securities and units in unit trusts	**3,278**	3,075
Debt securities and other fixed income securities	**25,176**	20,811
Participation in investment pools	**1,254**	1,180
Loans and deposits with credit institutions	**5,216**	4,414
Other	**18**	4
	34,942	29,484

14. 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 £6,140m (2007: £5,399m).

15. MEMBERS' BALANCES

	2008 £m	2007 £m
Balance at 1 January	**2,652**	597
Result for the year per syndicate annual accounts	**1,523**	3,029
Distribution on close of 2005 (2004) year of account	**(687)**	(1,204)
Advance distributions from open years of account	**(1,626)**	(414)
Movement in cash calls	**50**	79
Capital transferred into syndicate premium trust funds	**107**	322
Repayment of syndicate loans from the Central Fund	**–**	214
Foreign currency movements	**570**	(14)
Other movements	**(27)**	43
Balance at 31 December	**2,562**	2,652

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.

Members that only participate on one syndicate may hold the capital supporting their underwriting in their syndicate's premium trust funds. Where a member takes advantage of this facility in the year, the movement is reflected in the above table as 'capital transferred into syndicate premium trust funds'.

16. TECHNICAL PROVISIONS

	2008 £m	2007 £m
Gross		
Claims reported and loss adjustment expenses	**22,307**	16,343
Claims incurred but not reported	**16,113**	12,628
Unearned premiums	**9,043**	7,282
Total technical provisions, gross	**47,463**	36,253
Recoverable from reinsurers		
Claims reported and loss adjustment expenses	**7,172**	5,037
Claims incurred but not reported	**3,332**	2,412
Unearned premiums	**1,167**	841
Total reinsurers' share of technical provisions	**11,671**	8,290
Net		
Claims reported and loss adjustment expenses	**15,135**	11,306
Claims incurred but not reported	**12,781**	10,216
Unearned premiums	**7,876**	6,441
Total net technical provisions	**35,792**	27,963

17. FIVE YEAR SUMMARY

	2008 £m	2007 £m	2006 £m	2005 £m	2004 £m
Results					
Gross written premiums	**17,985**	16,366	16,414	14,982	14,614
Net written premiums	**14,217**	13,256	13,201	11,770	11,734
Net earned premiums	**13,796**	13,097	12,688	11,785	11,797
Result attributable to underwriting	**1,198**	2,099	2,142	(1,388)	396
Result for the year before tax	**1,899**	3,846	3,662	(103)	1,367
Assets employed					
Cash and investments	**44,370**	36,981	35,091	35,012	31,412
Net technical provisions	**35,792**	27,963	27,371	29,402	25,079
Other net assets	**5,604**	4,431	5,116	4,881	5,330
Capital and reserves	**14,182**	13,449	12,836	10,491	11,663
Statistics					
Combined ratio (%)	**91.3**	84.0	83.1	111.8	96.6
Return on capital (%)	**13.7**	29.3	31.4	(0.9)	12.5

SECURITY UNDERLYING POLICIES ISSUED AT LLOYD'S

as at 31 December 2008

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 80 syndicates, (including syndicates set up to accept RITC of orphan syndicates and Special Purpose Syndicates) as at 31 December 2008, 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 2008) 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 requirements 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 over seas 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 judgement 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 £38,306m at 31 December 2008.

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 ie 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 2008, the total value of capital supporting underwriting held in trust by members amounted to £10,630m.

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 2008 were £852m.

In 2004 and 2007, Lloyd's issued subordinated loan notes and perpetual capital securities respectively which, as at 31 December 2008, are included as a liability of £1,082m 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 £138m at 31 December 2008, 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 £2,072m at 31 December 2008.

AGGREGATE RESOURCES

The total of syndicate assets, members' capital to support underwriting (ie funds at Lloyd's and capital held in syndicate premiums trust funds) and central resources of the Society as at 31 December 2008 was £51,008m. The total of net syndicate technical provisions at the end of 2008 was £35,744m. The total net resources of the Society and its members were therefore £15,264m (excluding the subordinated debt liability) as shown in the PFFS on page 71.

The aggregated resources are based on the total of 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.

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 2008.

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, ie that part of the callable layer not attributable 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.

SECURITY UNDERLYING POLICIES ISSUED AT LLOYD'S CONTINUED

as at 31 December 2008

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 requires 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.

	2008 £m	2007 £m
I Syndicate level assets (several basis)	**38,306**	30,601
II Members' funds at Lloyd's (several basis)	**10,630**	9,858
III Central assets (mutual basis)		
Net Central Fund assets	**852**	767
Subordinated loan notes	**586**	516
Subordinated Perpetual Capital Securities	**496**	496
Other net assets of the Society	**138**	172
	2,072	1,951
Total resources of the Society of Lloyd's and its members	**51,008**	42,410
Net syndicate technical provisions	**(35,744)**	(27,949)
Total net resources of the Society of Lloyd's and its members	**15,264**	14,461

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. 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, 2008 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 2008 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

	2008 £m	2007 £m	2006 £m	2005 £m	2004 £m
Operating result					
Operating and other group income	**248**	262	198	184	201
Central Fund contributions	**84**	168	152	70	191
Total income	**332**	430	350	254	392
Central Fund claims and provisions released/(incurred)	**6**	18	(116)	(224)	(126)
Contribution to Equitas – Berkshire Hathaway transaction	**–**	(90)	–	–	–
Net insurance claims and provisions	**(34)**	(1)	2	–	5
Other group operating expenses	**(188)**	(188)	(171)	(172)	(173)
Operating surplus/(deficit)	**116**	169	65	(142)	98
Profit on sale of Lloyd's buildings	**–**	–	–	–	24
Surplus/(deficit) before finance, associates and tax	**116**	169	65	(142)	122
Net finance income and unrealised exchange differences on borrowings	**22**	57	24	95	38
Share of profits of associates	**4**	4	2	2	2
Surplus/(deficit) before tax	**142**	230	91	(45)	162
Tax (charge)/credit	**(40)**	(66)	(7)	17	(39)
Surplus/(deficit) for the year	**102**	164	84	(28)	123
Balance sheet					
Net assets	**990**	939	957	765	690
Movement in net assets %	**5.4%**	(1.9%)	25.1%	10.9%	22.1%
Solvency*					
Central assets for solvency purposes	**2,608**	2,465	2,054	1,850	1,663
Solvency shortfalls	**(133)**	(167)	(253)	(482)	(554)
Excess of central assets over solvency shortfalls	**2,475**	2,298	1,801	1,368	1,109
Solvency ratio %	**1,961%**	1,476%	812%	384%	300%
Movement in central assets for solvency purposes %	**5.8%**	20.0%	11.0%	11.2%	194.3%

*The solvency position for 2008 is estimated and will be finalised in June 2009 for submission to the FSA.

CORPORATE GOVERNANCE

The Council of Lloyd's is committed to the principle of 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 23 March 2009 are listed on page 16. 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 amongst its members.

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, Andreas Prindl (a nominated member) was elected Deputy Chairman by the Council in February 2009.

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 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 six times in 2008.

GOVERNANCE POLICIES

Amongst other matters, the Governance Policies are intended to improve the clarity around the role of the Council and to establish a more structured relationship with the Franchise Board.

The Governance Policies establish 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 establish the process by which the Council manages its own activities and affairs. There are a number of issues 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 Strategic Plan). 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 both the interests of capital providers and 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

Following a public consultation exercise, and overwhelming support from Lloyd's members at an Extraordinary General Meeting held on 21 May 2008, Parliament approved a Legislative Reform Order ('LRO') amending Lloyd's Act 1982 which came into force on 19 November 2008.

The LRO updates or removes a number of provisions in the Lloyd's Act 1982. These were the removal of the statutory restrictions on the re-election of working members; the removal of the requirement that the Chairman and Deputy Chairmen 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; modernising the rules on membership of disciplinary committees; repealing the requirement to have the rarely used Committee of Lloyd's; and reforming the delegation process. Furthermore, the LRO removes the requirement that managing agents generally only accept insurance business from or through a Lloyd's broker (although the class of Lloyd's brokers continues to exist for those that wish to describe themselves as 'Lloyd's brokers'). It also removes the associated 'divestment provisions' that prohibit prescribed associations between managing agents and Lloyd's brokers.

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 23 March 2009 are listed on page 17. In 2008, 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. The balance of the Board was made up of three non-executives connected with the Lloyd's market and four independent non-executives. The Franchise Board held 10 meetings in 2008. 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 takes decisions regarding the exercise of Lloyd's enforcement powers. It also 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. MSARC met on four occasions in 2008.

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 three occasions in 2008.

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 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 five occasions in 2008.

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 Legal and Compliance department on internal and overseas compliance are reviewed by the Audit Committee and appropriate action taken in response. The Audit Committee met on six occasions in 2008.

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, new 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 the remuneration of these individuals and makes recommendations to the Council on the remuneration of the members of these bodies, including the Chairman, CEO, Director, Finance, Risk Management and Operations and Franchise Performance Director. The NACC is also responsible for succession planning arrangements for these positions. The NACC met on three occasions in 2008.

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 2008 (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 2008 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 and that the Council and its principal committees were operating in accordance with their terms of reference.

Amongst the other major findings of the review were:

→ An acknowledgement that while the responsibilities of the Council and Franchise Board were generally understood by each body, greater clarification around the role each should play when considering strategic matters would be helpful.

→ A view that the wider market was sometimes unclear on the respective responsibilities of the Council and Franchise Board, as outlined in the Governance Policies.

These and other suggestions for improvement will be taken forward by the Council and the relevant 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 2008, three 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.

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[3]	Investment Committee
Council and Franchise Board members:							
Chairman of the Council of Lloyd's:							
Lord Levene of Portsoken	[4a]6/6	[a]10/10					
Executive Directors							
Richard Ward	6/6	10/10					
Luke Savage		10/10					5/5
Rolf Tolle		10/10					
Non-Executive Council members							
Working members							
Rupert Atkin	4/6			3/3			
Ewen Gilmour	5/6		5/6	3/3			
Christopher Harman	6/6						
Nick Marsh	6/6						
Graham White	6/6			2/2			
External members							
Paul Jardine	4/6			1/2			
Alan Lovell	6/6					3/3	
Barbara Merry	6/6						
Peter Morgan	5/6			2/3			
Dermot O'Donohoe	4/6						
David Shipley	6/6		6/6				
Nominated members							
Celia Denton	6/6		6/6		4/4		
Reg Hinkley	6/6						
Bill Knight	6/6		4/6	[a]3/3	[a]4/4		
Philip Lader	4/6			1/3			
Andreas Prindl	6/6		5/6	2/2		[a]3/3	[a]5/5
Non-Executive Franchise Board members							
Roy Brown		8/10					
Edward Creasy		10/10					
Nick Furlonge (joined 4/2/2008)		7/9					
Stephen Hodge (retired 2/4/2008)		2/2	[6a]2/2				
Claire Ighodaro		10/10	[6a]6/6				
Andrew Kendrick		9/10	4/6				
Dipesh Shah (joined 3/4/2008)		[5]9/10					
Jim Stretton		9/10	6/6				
Former Council members							
Nigel Hanbury				0/1			
Anthony Townsend				0/1			
Other Committee members							
Ian Agnew					3/4		
Lady Delves Broughton						3/3	4/5
Margaret Chamberlain						1/3	
Christine Dandridge					3/3		
David Gilchrist					1/1		
David Gittings						3/3	
Mark Graham							4/5
Michael Green							5/5
Ian Salter						3/3	
Paul Swain						3/3	
David Winkett							5/5

a Chairman

1 Nominations, Appointments and Compensation Committee.

2 Market Supervision and Review Committee.

3 Capacity Transfer Panel.

4 Pending his re-election to Council as a working member, Lord Levene was not a member of Council at the time of the 1 December 2008 Council meeting. At the invitation of the Council, he attended the December Council meeting in his capacity as the Chairman of the Franchise Board.

5 Dipesh Shah officially joined the Franchise Board on 3 April 2008. He also attended the first two Franchise Board meetings of the year as an observer.

6 Stephen Hodge chaired the first two Audit Committee meetings of the year prior to his retirement on 2 April 2008. Claire Ighodaro chaired the remaining four meetings of the Audit Committee.

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 Combined Code 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, the Legal and Compliance department or, where appropriate, to the Chairman of the Audit Committee or the FSA, are clearly set out. 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 Combined Code.

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 declarations 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. These policies and procedures are regularly reviewed and updated.

Lloyd's maintains an internal audit function that reports to the CEO and the Audit Committee. The Head of Internal Audit 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 risk and control assessment procedure was conducted on an ongoing basis throughout 2008. 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 40 to 43.

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 risks facing the Society 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 2008 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 the Legal and Compliance department report 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 the Legal and Compliance department provide 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 three nominated, two external and three working members of the Council. The NACC members for 2008 are indicated within the remuneration table on page 94.

The Committee met three times during the year. The attendance at meetings by members of the Committee is set out in the Corporate Governance report, page 88. 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 the Council on the appointment of the Chairman, CEO, new 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.

Apart from the annual exercise of making recommendations with respect to the composition of Council and Franchise Board committees (together with any other necessary changes in composition during the year), the NACC made the following recommendations to Council during 2008:

→ To appoint Sir Robert Finch as a new nominated member of Council for a three year term to replace Bill Knight following his retirement from Council on 31 December 2008.

→ To appoint two market connected non-executive directors on the Franchise Board. Nick Furlonge was appointed as from 4 February 2008 to serve a three year term and David Shipley was appointed as from 1 January 2009 to serve a three-year term.

These recommendations were accepted by Council. The NACC made use of its own resources and expertise in identifying candidates for these appointments.

The NACC also started the process of finding a successor to Rolf Tolle who will be retiring at the end of 2009. The NACC has employed an external search consultant to assist with this process.

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 LLP. During the year, Deloitte LLP also provided other services to the Corporation including support to the Lloyd's Exchange project and the Claims Service Review.

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 Working at Lloyd's Policies and Procedures document as follows:

'Lloyd's operates a total reward approach, which is designed to meet employee and Corporation needs by providing rewards that are linked to individual performance and the delivery of Lloyd's Corporation objectives.

Our total reward 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 also founded on the proposition that the ultimate source of value in the business is people. Combining this creates a reward offering which:

→ Emanates from business strategies and priorities.

→ Is based on business success, ie our ability to pay.

→ Provides a flexible mix of rewards which will attract, retain and motivate a performance driven workforce with the varied range of experience and skills the business requires.

→ Is externally competitive and regularly monitored by means of benchmarking exercises.

→ Rewards for performance rather than cost of living.

→ Ensures employees understand the criteria by which rewards are determined and reviewed.

→ Gives managers the tools to make informed decisions regarding rewarding their teams.

→ Is in line with our equality and diversity policy.'

REMUNERATION

The policy outlined above has been applied throughout 2008. Whilst this policy is envisaged as applying for 2009 and subsequent years, the NACC will continue to monitor its policies, particularly its arrangements for performance related pay, against evolving market practice and relevant guidelines prepared in response to the current economic climate.

The current remuneration package of Council and Franchise Board members who are employees of the Corporation comprises both performance and non-performance related components. For the CEO, Director, Finance, Risk Management and Operations and the Franchise Performance Director, the performance related components comprise annual bonuses as well as a Lloyd's Performance Plan (the former is determined by reference to performance against objectives while the latter is linked to the overall performance of the Lloyd's market). The non-performance related components comprise base salaries, benefits and pension entitlements. The Chairman does not participate in the Lloyd's Performance Plan.

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 private medical and life insurance in addition to their base salary.

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

LLOYD'S PERFORMANCE PLAN

As reported in last year's report, following a review by NACC, and with the agreement of Council, a new Lloyd's Performance Plan (LPP) was introduced from 1 January 2008. Subject to the transitional provisions described below, it replaced the previous long-term incentive plan (LTIP) available to the CEO, Directors and Level 1 employees.

The LPP is available to all employees and 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 plan is operated at the discretion of the NACC and can be amended or terminated at any time.

LONG-TERM INCENTIVE PLAN (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. Details of its operation are included below because of its impact on the transitional provisions of the LPP.

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 pools 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 were eligible for the scheme including the CEO, directors and existing staff in role Level 1 as at 1 January each year. The NACC retained absolute and sole discretion as to who participated 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.

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, at 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 2008, 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 2006–2008 of £7,832m x relevant % x salary of LTIP participant per £1m.

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 94.

LLOYD'S PERFORMANCE PLAN (LPP) APPLICABLE FOR THE YEAR ENDED 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. LPP 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 LPP 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 ie £5bn of PBT
Senior managers (Level 1)	10% salary per £1bn of PBT		30% of salary ie £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) ie £3bn of PBT

REPORT OF THE NOMINATIONS, APPOINTMENTS AND COMPENSATION COMMITTEE CONTINUED

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, directors and Level 1 employees.	Any LPP Award will be notified to the employee after the PBT for the relevant year has been announced (ie 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). However, the general intention is as follows:

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 paragraphs (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

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 is 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 is 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 were 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.

Level 2–4 employees

(a) For all Level 2–4 employees eligible to participate in the LPP for the financial year 2008 (ie all employees who were employed by the Corporation as at 2 January 2008), the provisions set out below were applied.

(b) For the financial year 2008 only, the LPP Award for Level 2–4 employees described above was based on the adjusted interim PBT for the six months to 30 June 2008 and was 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 £117,600 from 6 April 2008. 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.

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 to compensate for their pension benefits being based on the Scheme earnings cap rather than their base salaries.

A cash allowance of £46,560 was payable in respect of the Chairman for 2008 which equates to 40% of the Scheme earnings cap applicable during the period.

The Lloyd's Pension Scheme is contributory and the Director, Finance, Risk Management and Operations and the Franchise Performance Director pay 10% of the earnings cap as a contribution via salary sacrifice. The CEO pays 5% of the earnings cap as a contribution for a sixtieth accrual rate and an extra 26.1% decreasing to 25.4% with effect from 1 July 2008 of the earnings cap to increase the accrual rate to thirtieths, both paid via salary sacrifice.

CONTRACTS OF EMPLOYMENT

Lord Levene's three-year contract for services expired on 6 November 2008. The Council offered and Lord Levene accepted a one-year contract, subject to renewal each year, commencing 7 November 2008. The contract covers Lord Levene's services as Chairman of the Franchise Board and Chairman of Lloyd's.

Following the making of the Legislative Reform Order to amend Lloyd's Act 1982 in November 2008, Lord Levene was able to stand for re-election to Council. He was re-elected for a further three-year term, commencing on 10 December 2008. Lord Levene's previous term of office expired on 6 November 2008. He was re-elected as Chairman by Council on 16 December 2008.

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 December 2008	Notice Period[i]
Lord Levene of Portsoken	See above	10 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 2008, fees for members of Council and Franchise Board were £31,500 and £50,000 per annum, respectively. The Deputy Chairmen were paid £41,500 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 2008. 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 LPP.

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 96.

	Salary/Fees(xxvi)		Taxable benefits(i)		Annual bonus		Other(ii)		Total	
	2008 £000	2007 £000	**2008 £000**	2007 £000	**2008 £000**	2007 £000	**2008 £000**	2007 £000	**2008 £000**	2007 £000
Chairman of Council of Lloyd's										
Lord Levene of Portsoken(iii) (iv)	**627**	610	**1**	1	**100**	–	**78**	72	**806**	683
Executive Directors										
Richard Ward(iii) (iv)	**477**	460	**12**	12	**603**	464	**101**	97	**1,193**	1,033
Luke Savage(iii) (v)	**412**	394	**12**	12	**290**	200	**86**	82	**800**	688
Rolf Tolle(iii) (v) (xxv)	**543**	522	**22**	21	**800**	520	**135**	128	**1,500**	1,191
Non-Executive Council Members										
Working members										
Rupert Atkin(vi)	**39**	32	**–**	–	**–**	–	**–**	–	**39**	32
Ewen Gilmour, Deputy Chairman(vi)	**57**	52	**–**	–	**–**	–	**–**	–	**57**	52
Christopher Harman	**32**	26	**–**	–	**–**	–	**–**	–	**32**	26
Nick Marsh(viii)	**29**	–	**–**	–	**–**	–	**–**	–	**29**	–
Graham White, Deputy Chairman(vi) (vii)	**48**	37	**–**	–	**–**	–	**–**	–	**48**	37
External members										
Paul Jardine(vi) (vii) (viii)	**35**	–	**–**	–	**–**	–	**–**	–	**35**	–
Alan Lovell	**39**	33	**–**	–	**–**	–	**–**	–	**39**	33
Barbara Merry(ix)	**32**	26	**–**	–	**–**	–	**–**	–	**32**	26
Peter Morgan(vi) (x)	**39**	35	**1**	1	**–**	–	**–**	–	**40**	36
Dermot O'Donohoe(xi)	**32**	26	**–**	–	**–**	–	**–**	–	**32**	26
David Shipley(xii)	**40**	35	**–**	–	**–**	–	**–**	–	**40**	35
Nominated members										
Celia Denton	**49**	44	**–**	–	**–**	–	**–**	–	**49**	44
Reg Hinkley(xiii)	**32**	7	**–**	–	**–**	–	**–**	–	**32**	7
Bill Knight, Deputy Chairman of the Council of Lloyd's(vi)	**79**	62	**–**	–	**–**	–	**–**	–	**79**	62
Philip Lader(vi)	**39**	34	**2**	8	**–**	–	**–**	–	**41**	42
Andreas Prindl(vi) (vii)	**66**	52	**–**	–	**–**	–	**–**	–	**66**	52
Non-Executive Franchise Board Members										
Roy Brown	**50**	45	**–**	–	**–**	–	**–**	–	**50**	45
Edward Creasy	**50**	45	**–**	–	**–**	–	**–**	–	**50**	45
Nick Furlonge(xiv)	**46**	–	**–**	–	**–**	–	**–**	–	**46**	–
Claire Ighodaro(xv)	**61**	–	**–**	–	**–**	–	**–**	–	**61**	–
Andrew Kendrick	**57**	41	**–**	–	**–**	–	**–**	–	**57**	41
Dipesh Shah(xvi)	**50**	–	**–**	–	**–**	–	**–**	–	**50**	–
Jim Stretton	**58**	52	**5**	6	**–**	–	**–**	–	**63**	58
Former Members of Council										
Tom Corfield(xvii) (xxiii)	**–**	2	**–**	–	**–**	–	**–**	–	**–**	2
Christine Dandridge(xxiii)	**–**	3	**–**	–	**–**	–	**–**	–	**–**	3
Quentin Davies(xviii) (xxiii)	**–**	2	**–**	–	**–**	–	**–**	–	**–**	2
Nigel Hanbury(vii) (viii)	**3**	34	**–**	–	**–**	–	**–**	–	**3**	34
Judith Hanratty(xix)	**–**	28	**–**	–	**–**	–	**–**	–	**–**	28
Bronek Masojada(xxiii)	**–**	4	**–**	–	**–**	–	**–**	–	**–**	4
Charles Philipps(xx) (xxiii)	**–**	3	**–**	–	**–**	–	**–**	–	**–**	3
Anthony Townsend(vii) (viii) (xxi)	**3**	34	**–**	–	**–**	–	**–**	–	**3**	34
Former Members of the Franchise Board										
Steven Burns(xxiv)	**–**	45	**–**	–	**–**	–	**–**	–	**–**	45
Stephen Hodge(xxii)	**16**	56	**–**	–	**–**	–	**–**	–	**16**	56

(i) Taxable benefits include items such as company car or car allowance, medical and life insurance.

(ii) For executive directors, other includes payments of 20% of annual base salary as their pension benefits are based on a maximum earnings cap, which from 6 April 2008 was £117,600. The amount stated in respect of the Chairman represents a cash allowance in lieu of pension contributions and the premium in respect of additional life cover.

(iii) Employee of the Corporation of Lloyd's.

(iv) Member of both Council and the Franchise Board for 2008.

(v) Member of the Franchise Board only.

(vi) Member of the Nominations, Appointments and Compensation Committee (NACC) for 2008.

(vii) Nigel Hanbury and Anthony Townsend were members of the NACC until 31 January 2008. Paul Jardine, Andreas Prindl and Graham White joined NACC in February 2008.

(viii) Nick Marsh and Paul Jardine (the latter the representative of Catlin Syndicate Limited) were elected as members of Council from 1 February 2008. Nigel Hanbury and Anthony Townsend (the latter the representative of Brit UW Limited) retired from Council on 31 January 2008.

(ix) Representative of Hardy Underwriting Limited.

(x) Representative of AJSLP 9 Limited.

(xi) Representative of Dornoch Limited.

(xii) Representative of MAP Underwriting Limited.

(xiii) Reg Hinkley joined as a Nominated member of Council on 29 October 2007.

(xiv) Nick Furlonge was appointed to the Franchise Board on 4 February 2008.

(xv) Claire Ighodaro was appointed to the Franchise Board on 1 January 2008.

(xvi) Dipesh Shah was appointed to the Franchise Board on 3 April 2008. He also attended the first two meetings of 2008 as an observer.

(xvii) Representative of Liberty Corporate Capital Limited.

(xviii) Representative of SUMAC Underwriting (UK) Limited.

(xix) Judith Hanratty retired as a Nominated member of Council on 4 August 2007.

(xx) Representative of Amlin Corporate Member Limited.

(xxi) Representative of Brit UW Limited.

(xxii) Stephen Hodge retired from the Franchise Board on 2 April 2008.

(xxiii) Tom Corfield, Christine Dandridge, Quentin Davies, Bronek Masojada and Charles Philipps retired from Council on 31 January 2007.

(xxiv) Steven Burns retired from the Franchise Board on 31 December 2007.

(xxv) Rolf Tolle occupies a property leased to Lloyd's. Rolf Tolle pays the lease rental of £36,000 (2007: £36,000) on the property by salary sacrifice. These amounts are not included in the table above.

(xxvi) Salary/Fees are inclusive of compensation for time worked in excess of contractual obligations.

REPORT OF THE NOMINATIONS, APPOINTMENTS AND COMPENSATION COMMITTEE CONTINUED

LLOYD'S PENSION SCHEME PROVISIONS

	Salary sacrifice in year to 31 December 2008[(i)] £000	Age at 31 December 2008	Increase in pension in year to 31 December 2008 – actual £000	Increase in pension in year to 31 December 2008 – net of price inflation £000	Total accrued annual pension in year to 31 December 2008 £000 pa	Normal retirement age
Richard Ward	36	51	4	4	10	65
Luke Savage	12	47	3	3	12	60
Rolf Tolle	12	61	5	4	23	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 December 2007 £000	Transfer value of accrued pension as at 31 December 2008 £000	Increase in transfer value over the year less director's contributions via salary sacrifice £000
Richard Ward	65	73	(28)
Luke Savage	113	107	(18)
Rolf Tolle	354	436	70

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 December 2007 £000	Change in year £000	As at 31 December 2008 £000	Total £000	Amount paid in prior years £000	Amount paid during the year ended 31 December 2008 £000	Total award outstanding as at 31 December 2008 £000
Richard Ward	2006	8	17	–	17	25	8	8	9
	2007	–	113	–	113	113	–	38	75
	2008	–	–	268	268	268	–	–	268
Luke Savage	2005	15	30	–	30	45	30	15	–
	2006	32	63	–	63	95	31	32	32
	2007	–	176	–	176	176	–	59	117
	2008	–	–	261	261	261	–	–	261
Rolf Tolle	2005	21	41	–	41	62	41	21	–
	2006	46	92	–	92	138	46	46	46
	2007	–	247	–	247	247	–	82	165
	2008	–	–	367	367	367	–	–	367

Andreas Prindl, 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 2008.

COMPOSITION OF THE AUDIT COMMITTEE

In 2008 the Audit Committee comprised three nominated members of Council, one working and one external member of the Council and four non-executive members of the Franchise Board (this reduced to three non-executive members of the Franchise Board following Stephen Hodge's retirement after the March Audit Committee meeting). The Committee met six times during the year. The members of the Committee in 2008 and their attendance at meetings are shown in the Corporate Governance report on page 88.

Stephen Hodge chaired the February and March meetings and retired from the Committee after the March meeting. Claire Ighodaro assumed Chairmanship of the Committee from the June meeting.

All of the Committee have extensive commercial experience. For the purposes of the Combined Code, Celia Denton, Ewen Gilmour and Claire Ighodaro, 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 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 2008

The principal issues addressed during 2008 were:

- →The annual financial statements for 2007 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 2008 including the pro forma financial statements and the financial statements of the Society of Lloyd's.
- →The interim management statements of the Society of Lloyd's.
- →A consideration of those accounting policies which involved significant estimates and judgements.
- →The 2007 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 the Legal and Compliance department, 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.
- →Assessment of the effectiveness of the internal and external auditors.

The Committee has reviewed the work carried out by the external auditors in the year under review. On the basis of the level of service provided and confirmation of the auditors' independence, the Committee recommended the continuing appointment of the external auditor.

The Committee held a workshop training session during 2008 with presentations made by Standard and Poor's and Citigroup Investment Research on financial reporting from the user's perspective.
The Committee also reviewed its own performance.

SUPPORT

The CEO, Director, Finance, Risk Management and Operations, General Counsel, Head of Internal Audit and a member of the Legal and Compliance department, Financial Controller, Head of Market Finance 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.

Claire Ighodaro, 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 ended 31 December 2008.

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 one major new complaint was received, which I am still investigating.

COSTS

The expenses incurred by my office amounted to £20,775.

REPORT OF THE CHAIRMAN OF THE MEMBERS' COMPENSATION PANEL

BILL KNIGHT CHAIRMAN OF THE MEMBERS' COMPENSATION PANEL

As reported in the 2007 Annual Report an application for compensation was made relating to syndicates 535 and 536 as managed by Cotesworth & Co Limited. The Members' Compensation Panel required the applicants to pursue the claim in the High Court before proceeding with the application. The application remains adjourned pending the outcome of the High Court case.

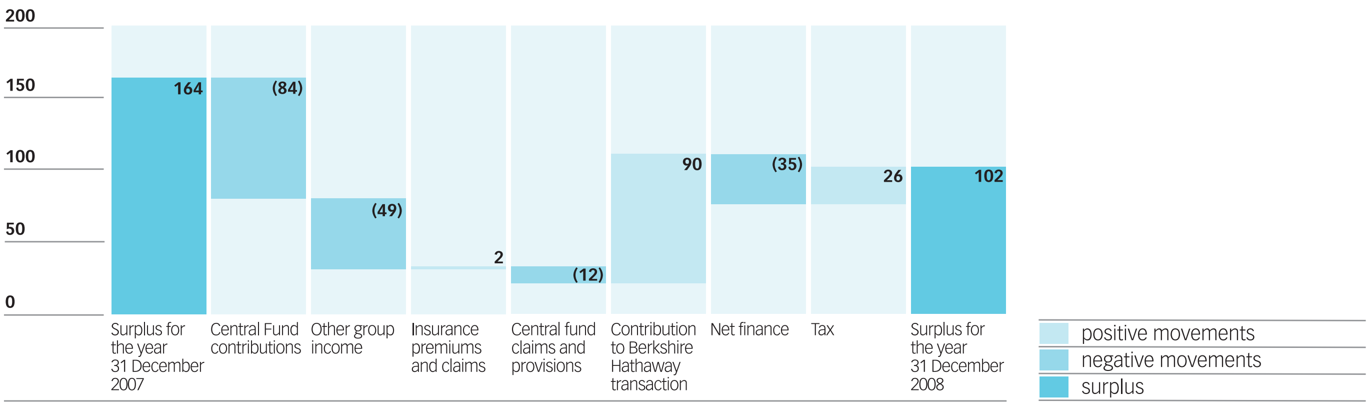
In 2008, and following consultation, the Panel made its recommendations to Council in respect of a number of amendments to the Members' Compensation Scheme. Accordingly, on 24 September 2008 Council made the new Members' Compensation Scheme Byelaw (No 3 of 2008) to give effect to those recommendations.

This review should be read in conjunction with the financial statements of the Society on pages 105 to 136.

OVERALL FINANCIAL RESULT

The Society of Lloyd's achieved a surplus for the year after taxation of £102m (2007: surplus of £164m). The movement in the surplus for the year is shown below:

Movement in group income statement
£m



INCOME

In aggregate the Society's income decreased in 2008 by £98m to £332m (2007: £430m). This was driven by the reduction in Central Fund contributions from 1.0% to 0.5%, this was possible due to the strong capitalisation of the Central Fund. Additionally, there has been a change in the basis of charging new Central Fund contributions and members' subscriptions from capacity to written premiums.

Other group income also decreased in 2008 by £49.0m to £32m (2007: £81m), due to the non-recurring income received in 2007 arising from litigation settlement receipts and recoveries in respect of undertakings previously given by the Central Fund.

On 27 February 2008, Centrewrite entered into a contract to reinsure the members of syndicate 535 for outstanding claims liabilities in respect of the 1999, 2000 and 2001 years of account on 31 December 2007. As a result general insurance net premium income has increased significantly year-on-year. However, this has been offset by the increase in the level of insurance claims arising form the portfolio transfer resulting in a net increase of £1m. Subsequent to the year end, Centrewrite has entered into a reinsurance to close contract reinsuring the liabilities of another Lloyd's syndicate.

CENTRAL FUND CLAIMS AND PROVISIONS

Central Fund claims and provisions is a net credit for the year of £6m (2007: £18m). This includes a reassessment of provisions as at 31 December 2008 which resulted in £27m 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 2008, payments made in respect of insolvent corporate members were £16m (2007: £9m) with additional payments made in respect of individual members of £3m.

OTHER GROUP OPERATING EXPENSES

In aggregate operating expenses remained stable in 2008 at £188m (2007: £188m). 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 £74m in 2008 (2007: £54m) predominantly relates to interest on the subordinated notes and perpetual subordinated capital securities. The increase in finance costs of £20m reflects the full year impact of the perpetual subordinated capital securities issued during 2007. Unrealised exchange losses on borrowings have increased in 2008 by £51m to £69m (2007: £18m), due to the retranslation of euro denominated subordinated notes at the prevailing year end rate. The exposure to movements in the euro is naturally hedged through euro denominated investments held.

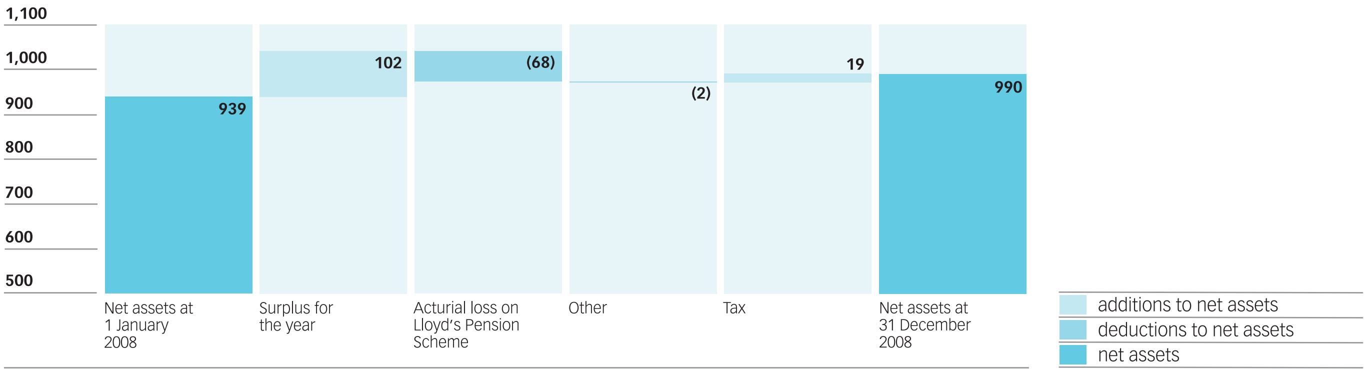
The increase in finance income in 2008 of £37m to £165m (2007: £128m) reflects strong returns from the Society's fixed interest investments in 2008. Commentary on investment strategy and investment performance is detailed below. The disposition of the Society's financial investments is set out in note 15 on pages 123 to 125.

TAXATION

A tax charge of £40m (2007: £66m) on the surplus before tax of £142m (2007: £230m) has been recognised for the year ended 31 December 2008. Further details are set out in note 8 on pages 117 and 118.

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

Movement of net assets
£m



The net assets of the Central Fund are included within the above amounts and at 31 December 2008 were £852m (2007: £768m).

PENSION SCHEMES

LLOYD'S PENSION SCHEME

On an IFRS valuation basis, the group pension scheme valuation at 31 December 2008 deteriorated from a surplus of £17m to a deficit of £32m before allowance for deferred tax asset of £9m (31 December 2007: £17m surplus before allowance for a deferred tax liability of £5m). The movement in the pension asset during the year is summarised below:

	2008 £m
Pension asset as at 1 January 2008	17
Pension expense recognised in the group income statement	(7)
Employer contributions – normal	5
– special	21
Actuarial loss recognised in the group statement of recognised income and expense	(68)
Pension deficit as at 31 December 2008	**(32)**

In addition to discretionary payments in respect of past service costs, a special payment of £15m was made to the pension scheme in December 2008 to improve the funding position. The Society is committed to a fully funded scheme and will contribute further on the basis of affordability.

At 31 December 2008, 17% of the pension liabilities were in respect of current employees. 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 126 to 129 which includes the sensitivity of the valuation to changes in these assumptions.

OVERSEAS PENSION SCHEMES

Overseas pension schemes' actuarial valuation at 31 December 2008 was £0.8m (2007: £0.7m). Further details are provided in note 18.

SOLVENCY

Total assets for solvency purposes are set out below. The 2008 position is an estimate of the amount which will be finalised in June 2009 for submission to the FSA:

	2008 £m	2007 £m
Net assets at 31 December	**990**	939
Subordinated notes and perpetual subordinated capital securities	**1,082**	1,012
Central assets	**2,072**	1,951
Callable Central Fund contributions	**495**	478
Other solvency adjustments	**41**	36
Central assets for solvency purposes	**2,608**	2,465
Solvency shortfalls	**(133)**	(167)
Excess of central assets over solvency shortfalls	**2,475**	2,298

Based on central assets for solvency purposes of £2.6bn (2007: £2.5bn), the estimated solvency ratio is 1,961% (2007: 1,476%). 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.

CASH FLOWS AND LIQUIDITY

Cash and cash equivalents increased during the year ended 31 December 2008 by £19m to £201m (2007: £182m). 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 2008 decreased by £11m to £73m (2007: £84m).

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 three-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 £1bn. 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. Value At Risk (VAR) methodology is used to assist with the objective of maximising expected investment returns over longer periods whilst controlling risk within defined limits. Such longer term investments are diversified amongst different asset classes to help manage risk. Current exposures include global equities, global bonds, global property (via property related equity securities) and hedge funds. Fixed interest assets of high credit quality are managed 'in house' by Lloyd's. Third party investment managers are retained to manage investments in other asset classes.

INVESTMENT PERFORMANCE

During the year ended 31 December 2008, the Society reported a 7.2% gross investment return (2007: 6.6%). Most of the Society's investments are held within the Central Fund. Unprecedented volatility in financial markets resulted in significant negative returns in some asset classes, including equities and corporate bonds. Central Fund hedge fund exposures produced a small negative return, but significantly out performed the hedge fund universe, which performed very poorly in 2008. High quality fixed interest investments form the largest element of Central Fund dispositions and these performed strongly as global yields declined in the second half of the year, driving the strong overall return on the Society's assets in the period.

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 135.

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 2008 (2007: £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 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 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. Further disclosures with regard to financial instruments are provided in note 21 on pages 132 and 133.

RELATED PARTY TRANSACTIONS
Except for disclosures made in note 24 see page 135, no related party had material transactions with the Society in 2008.

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 of fellow Council member and of the Society's auditors, 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 £2.1bn in 2009.

On 23 March 2009, 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 2009 income statement is £11m (see note 4 on page 115).

The operating expenses for the Corporation are budgeted to increase by £3m to £187m in 2009 (2008: actual £184m) 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) as 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 IFRS as adopted by the European Union. 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 2008 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 2008 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
23 March 2009

GROUP INCOME STATEMENT

for the year ended 31 December 2008

	Note	2008 £000	2007 £000
Operating income		**177,542**	177,853
Central Fund contributions		**84,294**	168,346
General insurance net premium income		**37,937**	2,046
Other group income		**32,397**	81,478
Total income	3B	**332,170**	429,723
Central Fund claims and provisions released	4	**6,349**	18,208
Contribution to Equitas – Berkshire Hathaway transaction	26	**–**	(90,000)
Gross insurance claims	13	**(77,314)**	16,330
Insurance claims recoverable from reinsurers	13	**42,806**	(17,041)
Other group operating expenses	5	**(187,703)**	(187,823)
Operating surplus		**116,308**	169,397
Finance costs	7	**(74,405)**	(53,752)
Finance income	7	**165,008**	128,468
Unrealised exchange losses on borrowings		**(69,233)**	(18,059)
Share of profits of associates	12A	**3,930**	4,395
Surplus before tax		**141,608**	230,449
Tax charge	8A	**(39,620)**	(65,994)
Surplus for the year		**101,988**	164,455

GROUP STATEMENT OF RECOGNISED INCOME AND EXPENSE

for the year ended 31 December 2008

	Note	2008 £000	2007 £000
Unrealised gain on revaluation of Lloyd's Collection	12B	**–**	1,138
Actuarial (loss)/gain on pension liabilities – group	18	**(67,855)**	52,452
– overseas		**(245)**	–
– associates	12A	**(1,954)**	1,835
Tax credit/(charge) on items taken directly to equity		**19,585**	(18,357)
Net income and expense recognised directly in equity		**(50,469)**	37,068
Surplus for the year		**101,988**	164,455
Total recognised income and expense for the year		**51,519**	201,523

GROUP BALANCE SHEET

as at 31 December 2008

	Note	2008 £000	2007 £000
Assets			
Intangible assets	9	**97**	438
Lloyd's Collection	12B	**10,824**	10,848
Property, plant and equipment	10	**19,220**	15,463
Deferred tax asset	8C	**4,356**	–
Investment in associates	12A	**6,465**	7,504
Insurance contract assets – Lioncover Insurance Company Limited	13	**514,137**	387,440
– other insurance activities		**48,901**	381
Pension asset	18	**–**	16,500
Loans recoverable	14	**57,541**	61,826
Financial investments	15	**2,230,156**	1,981,476
Inventories		**206**	197
Trade and other receivables due within one year		**69,639**	51,956
Prepayments and accrued income		**21,327**	39,650
Forward currency contracts	21	**32,646**	9,440
Cash and cash equivalents	16	**201,275**	181,689
Total assets		**3,216,790**	2,764,808
Equity and liabilities			
Equity			
Accumulated reserve	22	**979,269**	927,726
Revaluation reserve	22	**10,824**	10,848
Total equity		**990,093**	938,574
Liabilities			
Subordinated notes and perpetual subordinated capital securities	17	**1,082,023**	1,011,754
Insurance contract liabilities – Lioncover Insurance Company Limited	13	**514,137**	387,440
– other insurance activities	13	**97,002**	14,319
Pension liabilities	18	**32,786**	667
Deferred tax liabilities	8C	**–**	13,654
Provisions	19	**109,864**	132,226
Loans funding statutory insurance deposits		**148,310**	101,562
Trade and other payables	20	**100,466**	68,019
Accruals and deferred income		**45,961**	44,045
Tax payable		**16,182**	31,788
Forward currency contracts	21	**79,966**	20,760
Total liabilities		**2,226,697**	1,826,234
Total equity and liabilities		**3,216,790**	2,764,808

Approved and authorised for issue by the Council of Lloyd's on 23 March 2009 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 2008

	Note	2008 £000	2007 £000
Surplus before tax		**141,608**	230,406
Net finance income	7	**(90,603)**	(74,716)
Unrealised exchange loss on borrowings		**69,233**	18,059
Share of profits of associates	12A	**(3,930)**	(4,395)
Operating surplus		**116,308**	169,354
Central Fund claims and provisions released		**(6,349)**	(18,208)
Operating surplus before Central Fund claims and provisions		**109,959**	151,146
Adjustments for:			
Depreciation of property, plant and equipment	10	**3,246**	2,536
Amortisation of intangible assets	9	**131**	161
Impairment losses	9/10	**152**	352
Profit on sale of fixed assets		**(22)**	(41)
Operating surplus before working capital changes and claims paid		**113,466**	154,154
Changes in Pension obligations		**(19,370)**	(8,600)
Increase in receivables		**(17,513)**	(57,681)
Increase in inventories		**(9)**	(13)
Increase in payables		**93,783**	62,661
Increase/(decrease) in provisions other than for Central Fund claims		**4,102**	(814)
Cash generated from operations before claims paid		**174,459**	149,707
Claims paid in respect of corporate members	19	**(15,551)**	(9,348)
Tax and interest payments in respect of corporate members	4	**(25)**	(83)
Claims paid in respect of individual members	4	**(2,764)**	(307)
Claims paid in respect of Limited Financial Assistance Agreements	19	**(1,775)**	(1,174)
Cash generated from operations		**154,344**	138,795
Tax paid		**(54,238)**	(20,183)
Net cash from operating activities		**100,106**	118,612
Cash flows from investing activities			
Purchase of plant, equipment and intangible assets	9/10	**(7,432)**	(6,531)
Proceeds from the sale of equipment		**340**	233
Purchase of financial investments		**(1,578,376)**	(2,111,891)
Receipts from the sale of financial investments		**1,435,679**	1,797,931
Increase/(decrease) in short-term deposits	15B	**170,875**	(121,069)
Dividends received from associates	12A	**3,602**	2,554
Interest received		**74,550**	76,601
Dividends received	7	**6,444**	4,494
Realised (loss)/gain on settlement of forward currency contracts		**(128,429)**	5,777
Net cash used in investing activities		**(22,747)**	(351,901)
Cash flows from financing activities			
Syndicate loan interest paid		**–**	(13,401)
Other interest paid		**(73,503)**	(32,675)
Increase/(decrease) in borrowings for statutory insurance deposits		**15,019**	(32,625)
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
Repayment of syndicate loans		**–**	(331,611)
Net proceeds from financing activities		**(58,484)**	206,301
Net increase/(decrease) in cash and cash equivalents		**18,875**	(26,988)
Effect of exchange rates on cash and cash equivalents		**711**	(1,621)
Cash and cash equivalents at 1 January		**181,689**	210,298
Cash and cash equivalents at 31 December	16	**201,275**	181,689

NOTES TO THE FINANCIAL STATEMENTS

as at 31 December 2008

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 are 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 IFRIC 14 IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction. There has been no impact on the financial statements as a result of adopting this guidance.

The Society is regulated by the FSA.

2. PRINCIPAL ACCOUNTING POLICIES

GENERAL

In preparing the financial statements, significant estimates and judgements 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 14).

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 three 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.

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.

2. PRINCIPAL ACCOUNTING POLICIES CONTINUED

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

Financial assets

Initial recognition

Financial assets within the scope of IAS 39 are classified as financial assets at fair value through profit or loss and loans and receivables. The Society determines the classification of its financial assets at initial recognition.

Financial assets are recognised initially at fair value plus, in the case of loans and receivables, directly attributable transaction costs.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the marketplace (regular way purchases) are recognised on the settlement date.

The Society's financial assets include loans recoverable, statutory insurance deposits and other investments designated at fair value through profit or loss, trade and other receivables, accrued income, cash and cash equivalents and derivative assets.

Subsequent measurement

The subsequent measurement of financial assets depends on their classification as follows:

(i) Financial assets at fair value through profit or loss include derivative financial assets which are classified as held for trading and financial assets designated upon initial recognition at fair value through profit or loss. They are carried in the balance sheet at fair value. Gains and losses arising from changes in their fair value are included in the group income statement in the period in which they arise. When financial assets are interest-bearing, interest calculated using the effective interest method is recognised in the group income statement.

(ii) Loans and receivables are non-derivative financial assets with fixed or determinable payment that are not quoted in an active market. They arise when the Society provides money, goods or services directly to a debtor with no intention of trading the receivable. These financial assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in the group income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Financial liabilities

Initial recognition

Financial liabilities within the scope of IAS 39 are classified as financial liabilities at fair value through profit and loss and other financial liabilities. The Society determines the classification of its financial liabilities at initial recognition.

Financial liabilities are recognised initially at fair value and in the case of other financial liabilities, directly attributable transaction costs. The Society's financial liabilities include trade and other payables, accruals, subordinated loan notes and perpetual capital securities and derivative liabilities.

The subsequent measurement of financial liabilities depends on their classification as follows:

(i) Financial liabilities at fair value through profit or loss include derivative financial liabilities which are classified as held for trading. Gains or losses on liabilities held for trading are recognised in the group income statement.

(ii) 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

Fair value of financial instruments

The fair value of the financial instruments that are actively traded in organised financial markets is determined by reference to quoted market bid 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 so far as possible 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.

Amortised cost of financial instruments

Amortised cost is computed using the effective interest method less any allowance for impairment and principal repayment or reduction. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of the effective interest rate.

Impairment of financial assets

The Society assesses at each balance sheet date whether there is an indication that an asset may be impaired. If any such indication exists, the asset is written down to its recoverable amount.

Derecognition of financial instruments

Other investments are derecognised when the right to receive cash flows from the asset have expired, or in the case of financial liability when the obligation under the liability is cancelled or discharged.

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 expired.

Reinsurance assets 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.

Short-term bonuses are accrued in the period to which they relate, long-term bonuses are recognised over their vesting period.

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.

2. PRINCIPAL ACCOUNTING POLICIES CONTINUED

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 substantively 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 NOTES AND PERPETUAL SUBORDINATED CAPITAL SECURITIES

Subordinated debt is initially recognised at fair value, 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 for 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 collectability 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. Premium income is recognised over the period of cover. Premiums written are stated before deduction of commissions but net of taxes, duties levied on premiums and other similar 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.

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 undertakings previously given are credited to the group income statement when contractually committed to be received.

R. FOREIGN CURRENCY AND DERIVATIVE INSTRUMENTS

Foreign Currency Translation

(i) Functional and presentation currency

The group financial statements are presented in pound 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.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2008

2. PRINCIPAL ACCOUNTING POLICIES CONTINUED

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:

	2008	2007
US$	**1.44**	1.99
Can$	**1.77**	1.96
Euro	**1.03**	1.36

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. 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

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.

Inter-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. On 27 February 2008, Centrewrite entered into a contract to reinsure the members of Syndicate 535 for outstanding claims liabilities in respect of the 1999, 2000 and 2001 years of account at 31 December 2007. 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	2008 Corporation of Lloyd's £000	2008 Lloyd's Central Fund £000	2008 Insurance activities £000	2008 Society total £000
Segment income					
Segment income (unconsolidated)		**182,106**	**108,896**	**44,831**	**335,833**
Less inter-segment income		**(3,663)**	**–**	**–**	**(3,663)**
Total income from external sources	3B	**178,443**	**108,896**	**44,831**	**332,170**
Segment operating expenses (consolidated)					
Central Fund claims and provisions released	4	**–**	**6,349**	**–**	**6,349**
Gross claims incurred		**–**	**–**	**(77,314)**	**(77,314)**
Claims recoverable from reinsurers		**–**	**–**	**42,806**	**42,806**
Other group operating expenses:					
Employment (including pension costs)	6	**(84,540)**	**–**	**(1,951)**	**(86,491)**
Premises		**(35,888)**	**–**	**(749)**	**(36,637)**
Legal and professional	5	**(16,043)**	**(182)**	**(719)**	**(16,944)**
Systems and communications		**(20,565)**	**–**	**(702)**	**(21,267)**
Other		**(22,662)**	**(3,092)**	**(610)**	**(26,364)**
Total other group operating expenses		**(179,698)**	**(3,274)**	**(4,731)**	**(187,703)**
Total segment operating expenses		**(179,698)**	**3,075**	**(39,239)**	**(215,862)**
Central Fund and Insurance activity finance costs	7	**–**	**(73,868)**	**(164)**	**(74,032)**
Central Fund and Insurance activity finance income	7	**–**	**146,400**	**10,813**	**157,213**
Unrealised exchange losses on borrowings		**–**	**(69,233)**	**–**	**(69,233)**
Segment surplus		**(1,255)**	**115,270**	**16,241**	**130,256**
Corporation finance costs	7	**(373)**	**–**	**–**	**(373)**
Corporation finance income	7	**7,795**	**–**	**–**	**7,795**
Share of profits of associates	12A	**3,930**	**–**	**–**	**3,930**
Tax charge					**(39,620)**
Surplus for the year					**101,988**
Segment assets and liabilities					
Segment assets		**362,539**	**2,159,673**	**683,757**	**3,205,969**
Investment in associates	12A	**6,465**	**–**	**–**	**6,465**
Tax assets					**4,356**
Total assets					**3,216,790**
Segment liabilities		**(294,561)**	**(1,295,386)**	**(620,568)**	**(2,210,515)**
Tax liabilities					**(16,182)**
Total liabilities					**(2,226,697)**
Other segment information					
Capital expenditure	9/10	**7,402**	**–**	**30**	**7,432**
Depreciation	10	**2,988**	**–**	**258**	**3,246**
Amortisation of intangible assets	9	**46**	**–**	**85**	**131**
Impairment of long-term assets	9/10	**108**	**–**	**44**	**152**
Average number of UK employees (permanent and contract)		**689**	**–**	**4**	**693**
Average number of overseas employees (permanent and contract)		**101**	**–**	**12**	**113**
Average number of total employees (permanent and contract)		**790**	**–**	**16**	**806**

Average staff numbers shown above are on a full time equivalent basis.

3. SEGMENTAL ANALYSIS CONTINUED

A. INFORMATION BY BUSINESS SEGMENT CONTINUED	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 inter-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		(20,856)	(10,658)	(2,313)	(33,827)
Total other group operating expenses		(170,906)	(12,372)	(4,545)	(187,823)
Total segment operating expenses		(170,906)	(84,164)	(5,256)	(260,326)
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		7,788	207,236	3,659	218,683
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					164,455
Segment assets and liabilities					
Segment assets		292,210	2,008,193	456,901	2,757,304
Investment in associates	12A	7,504	–	–	7,504
Tax assets					–
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.

3. SEGMENTAL ANALYSIS CONTINUED

B. INCOME	Corporation of Lloyd's 2008 £000	Corporation of Lloyd's 2007 £000	Lloyd's Central Fund 2008 £000	Lloyd's Central Fund 2007 £000	Insurance activities 2008 £000	Insurance activities 2007 £000	Society total 2008 £000	Society total 2007 £000
Market charges								
Managing agents and syndicates	**65,708**	61,282	**–**	–	**3,007**	255	**68,715**	61,537
Members and members' agents	**12,585**	14,133	**–**	–	**–**	–	**12,585**	14,133
Franchise performance and risk management charge	**13,260**	12,442	**–**	–	**–**	–	**13,260**	12,442
Total market charges	**91,553**	87,857	**–**	–	**3,007**	255	**94,560**	88,112
Members' subscriptions	**71,535**	81,376	**–**	–	**–**	–	**71,535**	81,376
Other charges	**11,447**	7,680	**–**	–	**–**	685	**11,447**	8,365
Total operating income	**174,535**	176,913	**–**	–	**3,007**	940	**177,542**	177,853
Central Fund contributions	**–**	–	**84,294**	168,346	**–**	–	**84,294**	168,346
General insurance net premium income	**–**	–	**–**	–	**37,937**	2,046	**37,937**	2,046
Litigation settlement receipts	**–**	–	**–**	26,000	**–**	–	**–**	26,000
Equitas return premium	**–**	–	**–**	–	**–**	2,381	**–**	2,381
Other income	**3,908**	1,781	**24,602**	51,316	**3,887**	–	**32,397**	53,097
Other group income	**3,908**	1,781	**24,602**	77,316	**3,887**	2,381	**32,397**	81,478
Total income	**178,443**	178,694	**108,896**	245,662	**44,831**	5,367	**332,170**	429,723

During the year, members paid to the Corporation of Lloyd's (members' subscriptions) and to the Central Fund (Central Fund contributions from members) at 0.5% of their allocated overall written premium limit (2007: members' subscriptions 0.5% and Central Fund contributions 1.0%). The ultimate amounts to be retained by the Corporation of Lloyd's and the Central Fund for 2008 will be based on actual 2008 written premiums, of members , the quantification of which will not be known until 2010. The £84.3m (Central Fund contribution from members) and £71.5m (members' subscriptions) included in the group income statement are based on the present best estimates of the ultimate amounts that will be retained by the Central Fund and the Corporation of Lloyd's respectively. In 2007, the amounts retained were 100% of the amounts received from members.

In 2007 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 foreign exchange gains, 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

	2008 £000	2007 £000
Net undertakings released	**14,586**	14,828
Decrease in the value of supporting commitments (note 19)	**–**	6,057
Provisions made in respect of Limited Financial Assistance Agreements (note 19)	**(5,448)**	(2,287)
Claims payable in respect of individual members	**(2,764)**	(307)
Tax and interest payable in respect of insolvent members	**(25)**	(83)
	6,349	18,208

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 2008 were £120m. Of these amounts, £93m were included in undertakings granted on 23 March 2009 and the balance of £27m has been released to the group income statement in these financial statements. During 2009 further annual undertakings of £11m will be granted and no provision has been included in these financial statements in respect of these amounts.

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.

NOTES TO THE FINANCIAL STATEMENTS CONTINUED

as at 31 December 2008

5. OTHER GROUP OPERATING EXPENSES

	2008 Corporation of Lloyd's £000	2008 Lloyd's Central Fund £000	2008 Insurance activities £000	2008 Total £000
Other group operating expenses include:				
Employment costs (note 6)	**84,540**	**–**	**1,951**	**86,491**
Operating lease rentals – Lloyd's 1986 building	**16,767**	**–**	**–**	**16,767**
Operating lease rentals – other	**3,043**	**–**	**–**	**3,043**
Professional fees, including legal fees and related costs	**14,352**	**126**	**622**	**15,100**
Audit services	**293**	**56**	**78**	**427**
Assurance services payable to Ernst & Young LLP	**994**	**–**	**–**	**994**
Actuarial services payable to Ernst & Young LLP	**224**	**–**	**19**	**243**
Tax services payable to Ernst & Young LLP	**133**	**–**	**–**	**133**
Other services payable to Ernst & Young LLP	**47**	**–**	**–**	**47**
Total legal and professional fees	**16,043**	**182**	**719**	**16,944**
Charitable donations	**327**	**–**	**–**	**327**

	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, were capitalised and are not included above.

6. EMPLOYMENT

	2008 £000	2007 £000
Salaries and wages (including performance-related bonus)	**52,617**	45,365
Lloyd's Performance Plan (excluding social security costs – note 19)	**5,896**	871
Lloyd's Pension Scheme costs (note 18)	**6,601**	17,833
Other pension costs	**807**	224
Social security costs	**6,386**	5,338
Severance costs	**1,574**	1,629
Contract and agency staff	**3,658**	5,065
Other employment costs	**8,952**	6,427
	86,491	82,752

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 94.

7. FINANCE

	2008 Corporation of Lloyd's £000	2008 Lloyd's Central Fund £000	2008 Insurance activities £000	2008 Total £000	2007 Total £000
Finance costs					
Interest payable on financial liabilities measured at amortised cost	–	**(72,833)**	–	**(72,833)**	(52,523)
Other interest payable and similar charges	**(373)**	–	**(164)**	**(537)**	(413)
Amortisation of issue costs and discount	–	**(1,035)**	–	**(1,035)**	(816)
Total interest payable on financial liabilities	**(373)**	**(73,868)**	**(164)**	**(74,405)**	(53,752)
Finance income					
Bank interest received	**9,761**	**9,986**	**1,164**	**20,911**	23,523
Dividends received	–	**5,270**	**1,174**	**6,444**	4,494
Other returns on investments designated at fair value through profit or loss	**(2,483)**	**308,467**	**8,513**	**314,497**	162,442
Unrealised fair value movement of investments designated at fair value through profit or loss	**664**	**(12,690)**	**3,135**	**(8,891)**	(57,095)
Unrealised fair value movement of forward contracts held for trading	**(147)**	**(47,515)**	**(1,310)**	**(48,972)**	(12,173)
Realised fair value movement of forward contracts held for trading	–	**(113,594)**	**(1,863)**	**(115,457)**	5,779
Increase in valuation of loans recoverable designated at fair value through profit or loss	–	**(3,524)**	–	**(3,524)**	1,498
Total finance income	**7,795**	**146,400**	**10,813**	**165,008**	128,468

8. TAXATION

A. TAX ANALYSIS OF CHARGE IN THE YEAR

	2008 £000	2007 £000
Current tax:		
Corporation tax based on profits for the year at 28.5% (2007: 30%)	**(38,333)**	(61,800)
Adjustments in respect of previous years	**161**	(714)
Foreign tax suffered	**(458)**	(234)
Total current tax	**(38,630)**	(62,748)
Deferred tax:		
Origination and reversal of temporary differences – current year	**(1,332)**	(4,923)
– prior year	**342**	1,677
Tax charge	**(39,620)**	(65,994)

B. RECONCILIATION OF EFFECTIVE TAX RATE

	2008 £000	2008 £000	2007 £000	2007 £000
Surplus on ordinary activities before tax		**141,608**		230,449
Corporation tax at 28.5% (2007: 30%)	**28.5%**	**(40,358)**	30.0%	(69,135)
Expenses not deductible for tax purposes	**0.6%**	**(901)**	2.1%	(4,798)
Non-taxable income	–	–	(0.3%)	588
Utilisation of tax credits	**(0.4%)**	**498**	(0.1%)	279
Unutilisation of capital losses not previously recognised	–	–	(2.1%)	4,952
Overseas tax	**0.3%**	**(458)**	0.1%	(234)
Other	**(0.8%)**	**1,096**	(0.8%)	1,831
Deferred tax prior year adjustments	**(0.2%)**	**342**	(0.7%)	1,677
Deferred tax current year adjustments	–	–	0.2%	(440)
Adjustments in respect of previous years	**(0.1%)**	**161**	0.3%	(714)
Tax charge (note 8A)	**28.0%**	**(39,620)**	28.6%	(65,994)

8. TAXATION CONTINUED

C. DEFERRED TAX

	2008 Balance at 1 January £000	2008 Income Statement £000	2008 Equity £000	2008 Balance at 31 December £000
Property, plant and equipment	**4,199**	**(195)**	**–**	**4,004**
Loans recoverable	**(9,658)**	**1,226**	**–**	**(8,432)**
Financial investments	**(1,172)**	**2,294**	**–**	**1,122**
Pension (assets)/liabilities	**(4,620)**	**(5,424)**	**19,000**	**8,956**
Other employee benefits	**628**	**1,102**	**–**	**1,730**
Other items	**(3,031)**	**7**	**–**	**(3,024)**
	(13,654)	**(990)**	**19,000**	**4,356**

There were no unrecognised deductible temporary differences at 31 December 2008 (2007: nil).

	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)

9. INTANGIBLE ASSETS – SOFTWARE DEVELOPMENT

	Total £000
Cost:	
At 1 January 2007	4,881
Additions	280
At 31 December 2007	5,161
Additions	**29**
Disposals	**(138)**
At 31 December 2008	**5,052**
Amortisation:	
At 1 January 2007	4,562
Charge for the year	161
At 31 December 2007	4,723
Charge for the year	**131**
Impairment losses	**110**
Disposals	**(9)**
At 31 December 2008	**4,955**
Net book value at 31 December 2008	**97**
Net book value at 31 December 2007	438

IMPAIRMENT LOSSES

As part of an assessment of the carrying value of assets, £110,000 was written off in 2008 (2007: nil). The impairment and amortisation charges are included within other group operating expenses.

10. PROPERTY, PLANT AND EQUIPMENT

	Freehold land and buildings £000	Plant and equipment £000	Total £000
Cost:			
At 1 January 2007	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
Additions	**–**	**7,403**	**7,403**
Disposals	**(69)**	**(2,182)**	**(2,251)**
At 31 December 2008	**–**	**49,307**	**49,307**
Depreciation and impairment:			
At 1 January 2007	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
Depreciation charge for the year	**–**	**3,246**	**3,246**
Impairment losses	**–**	**42**	**42**
Disposals	**(69)**	**(1,824)**	**(1,893)**
At 31 December 2008	**–**	**30,087**	**30,087**
Net book value at 31 December 2008	**–**	**19,220**	**19,220**
Net book value at 31 December 2007	–	15,463	15,463

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, £42,000 was written off in 2008 (2007: £352,000). The charge is included within other group operating expenses.

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:

i) 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.

ii) 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

	2008 Goodwill £000	2008 Share of other net assets £000	2008 Total £000	2007 Total £000
At 1 January	**861**	**6,643**	**7,504**	4,379
Share of operating profits	**–**	**5,119**	**5,119**	5,720
Share of interest income	**–**	**429**	**429**	334
Share of tax on profit on ordinary activities	**–**	**(1,618)**	**(1,618)**	(1,659)
Total share of profits of associates	**–**	**3,930**	**3,930**	4,395
Share of actuarial (loss)/gain on pension liability	**–**	**(1,954)**	**(1,954)**	1,835
Share of tax on items taken directly to equity	**–**	**587**	**587**	(551)
Dividends received	**–**	**(3,602)**	**(3,602)**	(2,554)
At 31 December	**861**	**5,604**	**6,465**	7,504

Summary financial information for associates – 100%:

	Assets £000	Liabilities £000	Revenues £000	Profit after tax £000
2008				
Ins-sure Holdings Limited	**34,200**	**(19,782)**	**60,356**	**7,145**
Xchanging Claims Services Limited	**19,042**	**(12,810)**	**40,521**	**5,047**
	53,242	**(32,592)**	**100,877**	**12,192**
2007				
Ins-sure Holdings Limited	43,968	(22,791)	61,052	7,530
Xchanging Claims Services Limited	15,385	(10,401)	35,789	3,876
	59,353	(33,192)	96,841	11,406

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. In 2008 it has been assessed that there is no change in valuation.

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.

	2008 Lioncover Insurance Company Limited £000	2008 Other insurance activities £000	2008 Total £000	2007 Total £000
Insurance claims				
Gross claims:				
Claims paid	**(17,713)**	**(17,705)**	**(35,418)**	(22,656)
Change in provision for claims	**22,768**	**(64,664)**	**(41,896)**	38,986
	5,055	**(82,369)**	**(77,314)**	16,330
Claims recoverable from reinsurers:				
Claims recovered from reinsurers	**17,713**	**10,323**	**28,036**	21,592
Change in reinsurance contract assets	**(22,768)**	**37,538**	**14,770**	(38,633)
	(5,055)	**47,861**	**42,806**	(17,041)

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.

13. INSURANCE ACTIVITIES CONTINUED

LIONCOVER INSURANCE COMPANY LIMITED CONTINUED

Lioncover's long-term insurance liabilities include pollution and asbestos. Lioncover does not underwrite any new policies.

Insurance contract liabilities may be analysed as follows:

	2008 Insurance contract liabilities £000	2008 Reinsurer's share of liabilities £000	2008 Net £000	2007 Insurance contract liabilities £000	2007 Reinsurer's share of liabilities £000	2007 Net £000
Provision for claims reported	**212,131**	**(212,131)**	**–**	194,447	(194,447)	–
Provision for IBNR claims	**302,006**	**(302,006)**	**–**	192,993	(192,993)	–
Insurance contract liabilities	**514,137**	**(514,137)**	**–**	387,440	(387,440)	–

The movement in provision for insurance contract liabilities can be analysed as follows:

	2008 Insurance contract liabilities £000	2008 Reinsurer's share of liabilities £000	2008 Net £000	2007 Insurance contract liabilities £000	2007 Reinsurer's share of liabilities £000	2007 Net £000
At 1 January	**387,440**	**(387,440)**	**–**	432,405	(432,405)	–
Claims (released)/incurred	**(5,055)**	**5,055**	**–**	(17,126)	17,126	–
Claims paid (see below)	**(17,713)**	**17,713**	**–**	(21,592)	21,592	–
Effect of exchange rates	**149,465**	**(149,465)**	**–**	(6,247)	6,247	–
At 31 December	**514,137**	**(514,137)**	**–**	387,440	(387,440)	–

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.

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.

13. INSURANCE ACTIVITIES CONTINUED

POLLUTION AND HEALTH HAZARD CLAIMS CONTINUED

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 2008 were to underwrite the Lloyd's Members' Estate Protection Plan, to reinsure individual members of Lloyd's participations on syndicates for underwriting years of account which have not been closed and to provide reinsurance to close to syndicates with no successor syndicate.

Centrewrite has a structured approach to pricing, which is approved by the Centrewrite board in respect of the insurance contracts it underwrites. For reinsurance to close contracts, prior to the contract being quoted Centrewrite considers and does actuarial analysis upon the underlying historical data in respect of the performance of the syndicate. This data will include that in respect of claims development, major claims outstanding, exposure to further claims development, future run off costs and reinsurance cover. The reinsurance to close contract written in 2008 mainly relates to liability and energy risks written between 1993 and 2001.

Centrewrite continually monitors the performance of its business, including that in respect of outstanding claims exposure and reinsurance recoveries through a sub-committee of the Board.

Due to the uncertainty in the timing of large claims payments, Centrewrite, as part of its investment strategy, ensures investments are made in assets that can be readily realised at short notice to meet these payments as they fall due. Centrewrite regularly reviews the security of its reinsurance assets and makes provision for amounts which are not considered to be recoverable, based on default rates used by the Lloyd's market.

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 operating costs.

The insurance contract liabilities may be analysed as follows:

	2008 Insurance contract liabilities £000	**2008 Reinsurer's share of liabilities £000**	**2008 Net £000**	2007 Insurance contract liabilities £000	2007 Reinsurer's share of liabilities £000	2007 Net £000
Provision for claims reported	**57,627**	**(34,244)**	**23,383**	14,148	(300)	13,848
Provision for IBNR claims	**39,375**	**(14,657)**	**24,718**	171	(81)	90
Insurance contract liabilities	**97,002**	**(48,901)**	**48,101**	14,319	(381)	13,938

The movement in provision for insurance contract liabilities can be analysed as follows:

	2008 Insurance contract liabilities £000	**2008 Reinsurer's share of liabilities £000**	**2008 Net £000**	2007 Insurance contract liabilities £000	2007 Reinsurer's share of liabilities £000	2007 Net £000
At 1 January	**14,319**	**(381)**	**13,938**	14,148	–	14,148
Claims incurred/(released)	**82,369**	**(47,861)**	**34,508**	1,235	(381)	854
Claims paid	**(17,705)**	**10,323**	**(7,382)**	(1,064)	–	(1,064)
Effect of exchange rates	**18,019**	**(10,982)**	**7,037**	–	–	–
At 31 December	**97,002**	**(48,901)**	**48,101**	14,319	(381)	13,938

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 differences between the provision and subsequent settlements are dealt with in the group income statements of later years.

13. INSURANCE ACTIVITIES CONTINUED

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, together with cumulative claims at the current balance sheet date.

LIONCOVER INSURANCE COMPANY LIMITED

	2004 £000	2005 £000	2006 £000	2007 £000	**2008 £000**	**Total £000**
At end of underwriting year	848,850	–	–	–	**–**	
One year later	942,492	–	–	–		
Two years later	934,311	–	–			
Three years later	910,938	–				
Four years later	1,055,348					
Current estimate of cumulative claims	1,055,348	–	–	–		
Cumulative payments to date	(541,211)	–	–	–		
Insurance contract liabilities	514,137	–	–	–	**–**	**514,137**

The impact of exchange rate movements has increased the claims provision by £149.5m (2007: decrease in claims provision of £6.2m). This is represented in the movement in claims in the table above.

OTHER INSURANCE ACTIVITIES

	2004 and prior £000	2005 £000	2006 £000	2007 £000	**2008 £000**	**Total £000**
At end of underwriting year	75,193	3,407	2,647	1,873	**105,625**	
One year later	72,173	3,001	2,337	1,348		
Two years later	69,013	2,940	1,302			
Three years later	68,511	1,668				
Four years later	66,882					
Current estimate of cumulative claims	66,882	1,668	1,302	1,348	**105,625**	
Cumulative payments to date	(61,613)	(762)	(630)	(707)	**(16,111)**	
Insurance contract liabilities	5,269	906	672	641	**89,514**	**97,002**

The incurred claims for 2008 include amounts relating to the reinsurance of members of Syndicate 535.

14. LOANS RECOVERABLE

	2008 £000	2007 £000
At 1 January	**61,826**	62,201
Recoveries during the year	**(761)**	(1,873)
Change in valuation	**(3,524)**	1,498
At 31 December	**57,541**	61,826

None of the change in valuation of loans recoverable during 2008 or 2007 relates to changes in credit risk.

15. FINANCIAL INVESTMENTS

	2008 £000	2007 £000
Statutory insurance deposits (note 15A)	**154,576**	108,615
Other investments (note 15B)	**2,075,580**	1,872,861
	2,230,156	1,981,476

A. STATUTORY INSURANCE DEPOSITS

	2008 Securities £000	**2008 Deposits £000**	**2008 Total £000**	2007 Total £000
Market value at 1 January	**39,270**	**69,345**	**108,615**	126,742
Additions at cost	**18,951**	**282,183**	**301,134**	216,424
Disposal proceeds	**(25,440)**	**(275,119)**	**(300,559)**	(237,884)
Surplus on the sale and revaluation of investments	**15,396**	**29,990**	**45,386**	3,333
Market value at 31 December	**48,177**	**106,399**	**154,576**	108,615

15. FINANCIAL INVESTMENTS CONTINUED
A. STATUTORY INSURANCE DEPOSITS CONTINUED

Analysis of securities at year end:	**2008 Cost £000**	**2008 Valuation £000**	2007 Cost £000	2007 Valuation £000
Government	**21,885**	**28,599**	16,860	16,934
Corporate securities (see below)	**13,439**	**19,578**	22,778	22,336
Market value at 31 December	**35,324**	**48,177**	39,638	39,270

Analysis of corporate securities:				
AAA		**17,052**		20,011
AA		**2,526**		2,325
		19,578		22,336

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. Book cost is stated at historical exchange rates, current valuation is quoted at year end exchange rates.

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

	2008 Corporation of Lloyd's £000	**2008 Lloyd's Central Fund £000**	**2008 Insurance activities £000**	**2008 Total £000**	2007 Total £000
Market value at 1 January	**59,470**	**1,763,837**	**49,554**	**1,872,861**	1,371,601
Additions at cost	**–**	**1,054,493**	**222,749**	**1,277,242**	1,895,467
(Decrease)/increase in short-term deposits	**(59,470)**	**(113,647)**	**2,242**	**(170,875)**	121,069
Disposal proceeds	**–**	**(930,931)**	**(204,189)**	**(1,135,120)**	(1,554,640)
Surplus on the sale and revaluation of investments	**–**	**214,057**	**17,415**	**231,472**	39,364
Market value at 31 December	**–**	**1,987,809**	**87,771**	**2,075,580**	1,872,861
Analysis of securities at year end:					
Listed securities					
Fixed interest:					
Government	**–**	**1,269,048**	**65,913**	**1,334,961**	1,052,840
Corporate securities (see below)	**–**	**332,733**	**16,818**	**349,551**	259,109
Emerging markets	**–**	**22,487**	**–**	**22,487**	17,491
High yield	**–**	**24,916**	**–**	**24,916**	19,101
	–	**1,649,184**	**82,731**	**1,731,915**	1,348,541
Equities:					
Global	**–**	**136,578**	**–**	**136,578**	185,949
Emerging markets	**–**	**19,994**	**–**	**19,994**	18,656
	–	**156,572**	**–**	**156,572**	204,605
Total listed securities	**–**	**1,805,756**	**82,731**	**1,888,487**	1,553,146
Unlisted securities					
Hedge funds	**–**	**78,464**	**–**	**78,464**	65,162
Short-term deposits	**–**	**82,589**	**5,040**	**87,629**	233,553
Security deposits (see below)	**–**	**21,000**	**–**	**21,000**	21,000
Total unlisted securities	**–**	**182,053**	**5,040**	**187,093**	319,715
Market value at 31 December	**–**	**1,987,809**	**87,771**	**2,075,580**	1,872,861
Analysis of corporate securities:					
AAA	**–**	**230,990**	**12,129**	**243,119**	95,881
AA	**–**	**22,817**	**3,463**	**26,280**	83,848
A	**–**	**77,408**	**1,226**	**78,634**	79,380
Other	**–**	**1,518**	**–**	**1,518**	–
	–	**332,733**	**16,818**	**349,551**	259,109

The valuation of hedge funds is based on the net asset value provided by the asset manager.

15. FINANCIAL INVESTMENTS CONTINUED

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 2008, will be reviewed again in June 2010. 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.

Lioncover Insurance Company Limited

In October 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

	2008 £000	2007 £000
Cash at banks	**102,133**	30,274
Short-term deposits	**99,142**	151,415
	201,275	181,689

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 £201.3m (2007: £181.7m).

17. SUBORDINATED NOTES AND PERPETUAL SUBORDINATED CAPITAL SECURITIES

	2008 £000	2007 £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	**290,023**	220,345
7.421% perpetual subordinated capital securities of £500m redeemable on 21 June 2017	**500,000**	500,000
	1,090,023	1,020,345
Less: issue costs to be charged in future years	**(6,409)**	(6,980)
Less: discount on issue to be unwound in future years	**(1,591)**	(1,611)
	1,082,023	1,011,754

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).

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 (liabilities)/assets of the schemes at 31 December 2008 are as follows:

	2008 £000	2007 £000
Lloyd's Pension Scheme	**(31,985)**	16,500
Overseas pension schemes	**(801)**	(667)

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:

	2008 £000	2007 £000
Group income statement:		
Lloyd's Pension Scheme	**6,601**	17,833
Overseas pension schemes	**807**	224
	7,408	18,057
Group statement of recognised income and expense:		
Lloyd's Pension Scheme	**67,855**	(52,452)
Overseas pension schemes	**245**	–
	68,100	(52,452)

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.

The total market value of the scheme's assets at the date of valuation was £391m, which equated 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.

18. PENSION SCHEMES CONTINUED

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 2008 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 (2007: 25 years to 29 years).

→For non-pensioners currently aged 45: ranging from 27 years to 30 years (2007: 27 years to 30 years).

The other major financial assumptions used by the actuary as at 31 December 2008 for the purposes of IAS 19 were:

	2008 % per annum	2007 % per annum	2006 % per annum	2005 % per annum
General salary and wage inflation	**4.9%**	5.20%	4.80%	4.60%
Rate of increase in pensions in payment				
– pre 6 April 1997 (in excess of Guaranteed Minimum Pension)	**–**	–	–	–
– 6 April 1997 to 5 April 2005	**3.00%**	3.40%	3.00%	2.80%
– post 5 April 2005	**2.50%**	2.50%	2.50%	2.80%
Increases to deferred pensions	**3.00%**	3.40%	3.00%	2.80%
Discount rate	**6.40%**	5.90%	5.10%	4.80%
Price inflation	**3.00%**	3.40%	3.00%	2.80%
Expected rate of return – Bonds	**5.80%**	5.20%	4.70%	4.40%
– Equities	**8.10%**	8.10%	7.80%	7.90%
– Cash and net current assets	**3.80%**	5.30%	4.90%	3.80%

An allowance is made for members commuting 20% (2007: 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.

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 2008 would result in a change to the pension liabilities at that date of around 2%, or approximately £7m.

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	**2008 Fair value £000**	2007 Fair value £000	2006 Fair value £000	2005 Fair value £000
Bonds	**127,304**	162,611	135,839	126,363
Equities	**198,037**	238,734	215,386	193,226
Cash and net current assets	**22,306**	22,569	437	203
Total market value of assets	**347,647**	423,914	351,662	319,792
Actuarial value of scheme liabilities	**(379,632)**	(407,414)	(396,775)	(372,001)
(Deficit)/surplus in the scheme	**(31,985)**	16,500	(45,113)	(52,209)

18. PENSION SCHEMES CONTINUED

Changes in the present value of the defined benefit obligation are:

	2008 £000	2007 £000
Actuarial value of scheme liabilities at 1 January	**407,414**	396,775
Interest cost on pension scheme liabilities	**23,553**	20,616
Current service cost (net of employee contributions)	**6,173**	6,823
Past service cost	**5,400**	14,400
Employee contributions	**2,092**	1,946
Benefits paid	**(16,426)**	(16,738)
Experience losses arising in scheme liabilities	**2,170**	12,070
Change in assumptions underlying the present value of the scheme liabilities	**(50,744)**	(58,778)
LPSO Limited and other companies (see below)	**–**	30,300
Actuarial value of scheme liabilities at 31 December	**379,632**	407,414

Changes in the fair value of plan assets are:

	2008 £000	2007 £000
Fair value of scheme assets at 1 January	**423,914**	351,662
Expected return on pension scheme assets	**28,525**	23,896
Employer contributions – normal	**5,571**	4,094
– special	**20,400**	22,900
Employee contributions	**2,092**	1,946
Benefits paid	**(16,426)**	(16,738)
Actuarial (loss)/gain on scheme assets	**(116,429)**	5,744
LPSO Limited and other companies (see below)	**–**	30,410
Fair value of scheme assets at 31 December	**347,647**	423,914

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. 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 in 2007.

Under the participation terms, any debt payable on cessation became a liability of the Society. As a result the Society paid £8.6m during 2007 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 £5.1m in normal contributions to the pension scheme in 2009.

ANALYSIS OF THE AMOUNT RECOGNISED IN THE GROUP STATEMENT OF RECOGNISED INCOME AND EXPENSE (SORIE)

	2008 £000	2007 £000
Actual return on pension scheme assets	**(87,904)**	29,640
Less expected return on pension scheme assets	**(28,525)**	(23,896)
Actual return less expected return on pension scheme assets	**(116,429)**	5,744
Experience losses arising on scheme liabilities	**(2,170)**	(12,070)
Changes in the assumptions underlying the present value of the scheme liabilities	**50,744**	58,778
Actuarial (loss)/gain recognised in the SORIE	**(67,855)**	52,452

The cumulative actuarial loss recognised in the group statement of recognised income and expense since 1 January 2004 is £20.5m (2007: £47.4m actuarial gain).

ANALYSIS OF THE AMOUNT CHARGED TO THE GROUP INCOME STATEMENT (RECOGNISED IN OTHER GROUP OPERATING EXPENSES)

	2008 £000	2007 £000
Current service cost	**6,173**	6,823
Past service cost	**5,400**	14,400
Expected return on pension scheme assets	**(28,525)**	(23,896)
Interest on pension scheme liabilities	**23,553**	20,616
Settlement/curtailment	**–**	(110)
Total operating charge	**6,601**	17,833

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 £5.4m represent the costs of an increase for 2009. In 2007 the society provided £10.0m to meet future discretionary increases, this amount 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. As at 31 December 2008, the value of the notional fund was £8.1m.

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.

18. PENSION SCHEMES CONTINUED

HISTORY OF EXPERIENCE GAINS AND LOSSES

	2008 £000	2007 £000	2006 £000	2005 £000
Difference between the expected and actual return on scheme assets:				
Amount	**(116,429)**	5,744	7,426	31,904
Percentage of scheme assets	**(33.5%)**	1.4%	2.1%	10.0%
Experience (losses)/gains on scheme liabilities:				
Amount	**(2,170)**	(12,070)	(6,509)	606
Percentage of the present value of the scheme liabilities	**(0.6%)**	(3.0%)	(1.6%)	0.2%
Total amount recognised in the SORIE:				
Amount	**(67,855)**	52,452	(1,613)	(2,354)
Percentage of the present value of the scheme liabilities	**(17.9%)**	12.9%	(0.4%)	(0.6%)

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 2008 were £0.8m (2007: £0.7m). The total expense recognised in other operating expenses of £0.8m (2007: £0.2m) represents the related current service cost of these schemes. An actuarial loss of £0.2m has been recognised in the group statement of recognised income and expense (2007: nil).

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 (2007: £0.5m) represents contributions payable to these plans by the Society at rates specified in the rules of these plans.

19. PROVISIONS

	2008 Undertakings given to insolvent members £000	2008 Limited Financial Assistance Agreements £000	2008 Income support schemes £000	2008 Lloyd's performance plan £000	2008 Other £000	2008 Total £000	2007 Total £000
Balance at 1 January	**123,186**	**5,732**	**1,741**	**1,210**	**357**	**132,226**	162,160
Provision released	**(27,309)**	**–**	**–**	**(151)**	**(357)**	**(27,817)**	(42,495)
Charged in the year	**12,723**	**5,448**	**1,700**	**6,793**	**–**	**26,664**	32,965
Decrease in value of supporting commitments	**–**	**–**	**–**	**–**	**–**	**–**	(6,057)
Paid during the year	**(15,551)**	**(1,775)**	**(1,679)**	**(2,204)**	**–**	**(21,209)**	(14,347)
Balance at 31 December	**93,049**	**9,405**	**1,762**	**5,648**	**–**	**109,864**	132,226

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.

	2008 £000	2008 £000	2007 £000	2007 £000
Provisions for amounts payable at 1 January		**123,186**		147,362
Undertakings released in the year		**(14,586)**		(14,828)
Analysis of paid undertakings by member:				
Crowe Corporate Capital Limited	**(2,520)**		(1,564)	
Crowe Dedicated Limited	**(921)**		(2,904)	
Dreason Underwriting Limited	**(80)**		(92)	
Euclidian (No 6) Ltd	**(9,012)**		(1,673)	
Grenville Underwriting I/II/III Limited	**(644)**		–	
Margent Capital Management	**(117)**		(767)	
SOC Corporate Member No.1 Limited	**(910)**		(225)	
SOC Corporate Member No.3 Limited	**(456)**		(945)	
SCC at Lloyd's Ltd	**(146)**		(783)	
Winford Company Limited	**(57)**		(27)	
Other corporate members	**(688)**		(368)	
Paid during the year		**(15,551)**		(9,348)
Undertakings given to insolvent members at 31 December		**93,049**		123,186

The aggregate amount of all undertakings (excluding the supporting commitments) given by the Council at 31 December 2008 was £1.3bn of which £1.2bn 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 were provided in 2008. 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.

19. PROVISIONS CONTINUED

LLOYD'S PERFORMANCE PLAN (LPP)

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 91 to 92. The provision, including employers' National Insurance, for estimated contribution amounts due in respect of the plan is as follows:

	2008 Balance at 1 January £000	2008 Provision released £000	2008 Charged in the year £000	2008 Paid in the year £000	2008 Balance at 31 December £000
2005	**167**	**(29)**	**–**	**(138)**	**–**
2006	**357**	**–**	**27**	**(384)**	**–**
2007	**686**	**(122)**	**–**	**(564)**	**–**
2008	**–**	**–**	**6,766**	**(1,118)**	**5,648**
Total	**1,210**	**(151)**	**6,793**	**(2,204)**	**5,648**

Included within the charge for the year and provision released are National Insurance contributions of £0.7m (2007: £0.1m).

20. TRADE AND OTHER PAYABLES

	2008 £000	2007 £000
Due within one year:		
Trade and other creditors	**32,804**	21,969
Members' subscriptions and contributions repayable (see note 3B)	**19,565**	–
Taxation and social security	**2,198**	1,714
Arbitration awards	**3,420**	2,543
Contribution to Equitas – Berkshire Hathaway transaction	**18,000**	18,000
Interest payable on subordinated notes	**24,479**	23,793
	100,466	68,019

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 101 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 109 and 110.

The fair value (based on the quoted offer prices) of subordinated debt is £743.8m (2007: £1,031.3m) against a carrying value measured at amortised cost of £1,082.0m (2007: £1,011.8m). All other financial instruments are either held at fair value or at an amount that approximates to quoted prices.

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. Exposures under guarantees entered into by the Society are detailed in note 25.

IMPAIRMENT LOSSES

Trade receivables

The ageing of trade receivables as at 31 December 2008 was as follows:

	2008 Gross £000	2008 Impairment £000	2008 Net £000	2007 Gross £000	2007 Impairment £000	2007 Net £000
Not past due	**15,639**	**–**	**15,639**	16,584	–	16,584
Past due 31–120 days	**415**	**(10)**	**405**	222	(4)	218
More than 120 days	**1,350**	**(1,293)**	**57**	1,597	(1,581)	16
Total	**17,404**	**(1,303)**	**16,101**	18,403	(1,585)	16,818

The Society's normal credit terms are 30 days.

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:

	2008 £000	2007 £000
Balance at 1 January	**1,585**	1,687
Additional allowances during the year charged to the group income statement	**257**	73
Allowances released during the year credited to the group income statement	**(520)**	(146)
Recoveries during the year	**(19)**	(29)
Balance at 31 December	**1,303**	1,585

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. The Society's exposure to the risk of changes in the foreign exchange rates relates primarily to retranslating foreign currency subordinated notes and perpetual subordinated capital securities, revaluation of loans recoverable and changes in the fair value of foreign currency denominated investments and forward contracts.

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 the financial markets. As at 31 December 2008, a consistent increase of 100 basis points in the yields applicable to all relevant securities would have reduced the surplus before tax by approximately £99m (2007: £80m). This analysis assumes that all other variables, in particular foreign currency exchange rates, remain constant. In practice, actual results may differ.

Equity price risk

Equity price risk is the risk that the market values of equity investments fall. At 31 December 2008, a 15% fall in the value of all the Society's equity investments would have reduced the surplus before tax by approximately £23m (2007: £30m). This analysis assumes that all other variables, in particular foreign currency exchange rates, remain constant. In practice, actual results may differ.

21. FINANCIAL INSTRUMENTS CONTINUED

LIQUIDITY RISK

The table below summarises the maturity profile of the Society's non-derivative financial liabilities as at 31 December 2008 based on undiscounted contractual cash flows:

As at 31 December 2008	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 notes	**585,828**	**(832,281)**	**(36,939)**	**(36,939)**	**(110,817)**	**(647,586)**
Perpetual subordinated capital securities	**496,195**	**(833,945)**	**(37,105)**	**(37,105)**	**(111,315)**	**(648,420)**
Loans funding statutory insurance deposits	**148,310**	**(148,310)**	**(148,310)**	**–**	**–**	**–**
Trade and other payables	**100,466**	**(100,466)**	**(100,466)**	**–**	**–**	**–**
	1,330,799	**(1,915,002)**	**(322,820)**	**(74,044)**	**(222,132)**	**(1,296,006)**

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 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)	–	–	–
	1,181,335	(1,812,736)	(239,705)	(70,124)	(210,373)	(1,292,534)

Forward currency contracts are settled gross; notional amounts are a close proxy for cash flow amount. Further details regarding the subordinated notes and the perpetual subordinated capital securities can be found in note 17 on pages 125 and 126.

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:	2008 £000	2007 £000
Outstanding forward foreign exchange gains	**32,646**	9,440
Outstanding forward foreign exchange losses	**(79,966)**	(20,760)

The fair value and their notional amounts of forward currency contracts, all of which mature within one year, are analysed as follows:

	2008	**2008**	**2008**	**2008**
	Assets		**Liabilities**	
As at 31 December 2008	**Fair value £000**	**Notional £000**	**Fair value £000**	**Notional £000**
Currency Conversion Service (CCS)	**10,312**	**182,394**	**(9,974)**	**(182,056)**
Other forward foreign exchange contracts	**22,334**	**835,836**	**(69,992)**	**(883,494)**
	32,646	**1,018,230**	**(79,966)**	**(1,065,550)**

	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)

22. RECONCILIATION OF MOVEMENT IN EQUITY

	Accumulated reserve £000	Syndicate loans £000	Revaluation reserve £000	Total equity £000
At 1 January 2007	733,666	213,560	9,710	956,936
Total recognised income and expense for the year	200,385	–	1,138	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	927,726	–	10,848	938,574
Total recognised income and expense for the year	**51,519**	**–**	**–**	**51,519**
Other	**24**	**–**	**(24)**	**–**
At 31 December 2008	**979,269**	**–**	**10,824**	**990,093**

ACCUMULATED RESERVES

	2008 £000	2007 £000
Attributable to:		
Corporation of Lloyd's and non-insurance related subsidiary undertakings	**72,442**	116,798
Central Fund	**852,384**	768,117
Insurance related subsidiary undertakings	**47,978**	35,307
Associates	**6,465**	7,504
	979,269	927,726

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.

23. COMMITMENTS

A. CAPITAL EXPENDITURE COMMITMENTS

Capital expenditure commitments contracted but not provided in the accounts totalled £640,000 (2007: £nil).

B. OPERATING LEASE COMMITMENTS

	2008 £000	2007 £000
Non-cancellable operating lease rentals are payable as follows:		
Within one year	**23,272**	19,257
After one year but not more than five years	**80,125**	74,163
More than five years	**136,403**	152,860

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 to the first break in the lease. These arrangements do not impose any significant restrictions on the Society.

During the year ended 31 December 2008, £19.8m (2007: £19.1m) 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 2008 included operating systems support and development, premises and other administrative services. The total value of the services provided was £631,000 (2007: £615,000). In addition, Ins-sure Holdings Limited group have charged the Society £2,069,000 for services provided in the same year (2007: £2,680,000) .

At 31 December 2008, there was a balance of £90,000 (2007: £101,000) owing from Ins-sure Holdings Limited group to the Society.

Services provided to Xchanging Claims Services Limited group in the year ended 31 December 2008 included premises and other administrative services. The total value of the services provided was £113,000 (2007: £107,000).

At 31 December 2008, there was a balance of £8,000 (2007: £5,000) owing from Xchanging Claims Services Limited group to the Society.

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 2008 to meet unpaid cash calls. No amounts were paid under these undertakings in 2008.

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 2008 amounted to £22.6m (31 December 2007: £11.9m).

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:

	2008 £000	2007 £000
Guarantees provided by the Society:		
USA US$1,500,000 (2007: US$1,500,000)	**1,043**	754
Guarantees provided by the Society including Additional Securities Limited:		
Cayman Islands:		
Letter of credit US$1,250,000 (2007: US$1,250,000)	**869**	628

25. CONTINGENT LIABILITIES CONTINUED

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) 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.

In respect of all contingent liabilities disclosed as at 31 December 2008, 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.

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 2008 recognised a reinsurance asset due from ERL of £514m (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 a specially authorised new insurance company, Speyford Limited. 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 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 accounted for that part of the return premium due to it in the group financial statements.

FIVE YEAR SUMMARY

	2008 £000	2007 £000	2006 £000	2005 £000	2004 £000
Operating income	**177,542**	177,853	171,498	162,353	169,166
Central Fund contributions	**84,294**	168,346	152,226	70,077	190,657
General insurance net premium income	**37,937**	2,046	2,834	2,769	3,428
Other group income	**32,397**	81,478	23,477	18,637	28,979
Total income	**332,170**	429,723	350,035	253,836	392,230
Central Fund claims and provisions released/(incurred)	**6,349**	18,208	(115,735)	(223,889)	(125,540)
Contribution to Equitas – Berkshire Hathaway transaction	**–**	(90,000)	–	–	–
Gross insurance claims (incurred)/released	**(77,314)**	16,330	(55,461)	(30,039)	(47,735)
Insurance claims recoverable from/(payable to) reinsurers	**42,806**	(17,041)	56,804	29,844	52,053
Other group operating expenses:					
Employment (including pension costs)	**(86,491)**	(82,752)	(72,996)	(72,201)	(68,415)
Premises	**(36,637)**	(35,371)	(34,629)	(32,074)	(31,668)
Legal and professional	**(16,944)**	(16,580)	(18,442)	(21,596)	(22,768)
System and communications	**(21,267)**	(19,293)	(20,394)	(23,608)	(22,604)
Other	**(26,364)**	(33,827)	(24,334)	(22,618)	(27,961)
Total other group operating expenses	**(187,703)**	(187,823)	(170,795)	(172,097)	(173,416)
Operating surplus/(deficit)	**116,308**	169,397	64,848	(142,345)	97,592
Profit on sale of Lloyd's buildings	**–**	–	–	–	23,638
Surplus/(deficit) before finance, associates and tax	**116,308**	169,397	64,848	(142,345)	121,230
Finance costs	**(74,405)**	(53,752)	(32,921)	(39,951)	(4,547)
Finance income	**165,008**	128,468	52,942	129,033	45,875
Unrealised exchange (losses)/gains on borrowings	**(69,233)**	(18,059)	3,842	6,298	(2,630)
Share of profits of associates	**3,930**	4,395	1,867	2,006	1,872
Surplus/(deficit) before tax	**141,608**	230,449	90,578	(44,959)	161,800
Tax (charge)/credit	**(39,620)**	(65,994)	(7,012)	17,343	(38,959)
Surplus/(deficit) for the year	**101,988**	164,455	83,566	(27,616)	122,841

MANAGING AGENTS AND SYNDICATES

The table shows the key characteristics for managing agents and syndicates active as at 31 December 2008. In 2008, Lloyd's wrote gross premiums of £17,985m.

MANAGING AGENT	MANAGED SYNDICATE(S)	2008 GWP* £M	2007 GWP* £M	OWNED SHARE OF SYNDICATE(S) %
ACE Underwriting Agencies Limited	2488	437	393	100%
Advent Underwriting Limited	0780	163	137	100%
AEGIS Managing Agency Limited	1225	246	240	100%
Amlin Underwriting Limited	2001	842	901	100%
Argenta Syndicate Management Limited	1965	12	8	100%
	2121	132	95	40%
	6101	90	77	0%
	6102	49	42	0%
Ark Syndicate Management Limited	4020	226	89	100%
	6105	23	–	0%
Ascot Underwriting Limited	1414	506	538	100%
Aspen Managing Agency Limited	4711	78	–	100%
Atrium Underwriters Limited	0570	133	117	25%
	0609	194	173	25%
Beaufort Underwriting Agency Limited	0318	159	130	47%
Beazley Furlonge Limited	0623	197	179	6%
	2623	837	753	100%
	3623	0	–	100%
Brit Syndicates Limited	2987	714	647	100%
Canopius Managing Agents Limited	4444	484	469	93%
Capita Syndicate Management Ltd	5500	28	21	87%
Cathedral Underwriting Limited	2010	229	212	58%
	3010	16	4	100%
Catlin Underwriting Agencies Limited	2003	1,318	1,215	100%
Chaucer Syndicates Limited	1084	642	526	100%
	1176	26	22	56%
	1274	150	–	0%
	1301	78	69	0%
	4242	64	38	14%
Equity Syndicate Management Limited	0218	555	569	64%
	4455	12	12	95%
Faraday Underwriting Limited	0435	258	258	100%
Hardy (Underwriting Agencies) Limited	0382	116	108	100%
	3820	56	41	100%
HCC Underwriting Agency Ltd	4040	47	51	87%
	4141	19	–	100%
Heritage Managing Agency Limited	1200	409	325	78%
Hiscox Syndicates Limited	0033	885	996	73%
	6104	23	–	0%
Jubilee Managing Agency Limited	Life 0779	34	29	14%
	1231	47	51	100%
	5820	56	64	14%
KGM Underwriting Agencies Limited	0260	63	49	60%
R J Kiln & Co. Limited	Life 0308	15	14	50%
	0510	757	678	53%
	0557	38	35	0%
	0807	126	145	51%
Liberty Syndicate Management Limited	4472	951	1,045	100%
Managing Agency Partners Limited	2791	282	342	43%
	6103	16	18	0%
Markel Syndicate Management Limited	3000	238	197	100%

*See Glossary on page 140.

MANAGING AGENT	MANAGED SYNDICATE(S)	2008 GWP* £M	2007 GWP* £M	OWNED SHARE OF SYNDICATE(S) %
Marketform Managing Agency Limited	2468	122	110	29%
Marlborough Underwriting Agency Limited	1861	80	97	100%
Max at Lloyd's Ltd	1400	48	64	100%
	2525	43	42	2%
	2526	30	30	36%
S. A. Meacock & Company Limited	0727	68	63	9%
Mitsui Sumitomo Insurance Underwriting at Lloyd's Limited	3210	353	360	100%
Montpelier Underwriting Agencies Limited	5151	62	8	100%
Munich Re Underwriting Limited	0457	333	309	100%
Navigators Underwriting Agency Limited	1221	174	149	100%
Newline Underwriting Management Limited	1218	104	90	100%
Novae Syndicates Limited	2007	315	274	94%
Omega Underwriting Agents Limited	0958	329	282	16%
Pembroke Managing Agency Limited	4000	66	59	0%
QBE Underwriting Limited	0386	412	436	70%
	2999	852	978	100%
RITC Syndicate Management Limited	5678	1	–	100%
Sagicor at Lloyd's Limited	Life 0044	1	2	0%
	1206	127	56	100%
Shelbourne Syndicate Services Limited	2008	221	–	100%
Spectrum Syndicate Management Limited	2112	14	12	0%
Sportscover Underwriting Limited	3334	15	13	0%
Starr Managing Agents Limited	1919	233	91	100%
	2243	32	2	0%
Talbot Underwriting Ltd	1183	383	344	100%
Travelers Syndicate Management Limited	5000	320	295	100%
Whittington Capital Management Ltd	1910	90	–	0%
	1955	66	–	0%
XL London Market Ltd	1209	265	210	100%
All other syndicates and RITC adjustment		(250)	(132)	
Total		17,985	16,366	

As at 31 December 2008.

Name changes and managing agent changes during 2008 or after:
Imagine Syndicate Management Limited changed to Max at Lloyd's Ltd
Argenta 3334 managed by Sportscover Underwriting Limited
Canopius 0044 managed by Sagicor at Lloyd's Limited
Diagonal 4455 managed by Equity Syndicate Management Limited
Marlborough 1919 and 2243 managed by Starr Managing Agents Ltd
Spectrum 5151 managed by Montpelier Underwriting Agencies Limited

AS AT 1 MARCH 2009
The following syndicates commenced trading for the 2009 year of account:
Beaufort 1318
Hiscox 3624
Kiln 1880
Beazley Life 3622
Amlin SPS 6106

The following syndicates merged:
Hardy 3820 and 382

The following syndicates ceased trading at 31 December 2008:
Diagonal 4455
Catlin SPS 6101 and 6102

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.

Gross Written Premiums (GWP) 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.

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 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 One Lime Street London EC3M 7HA Telephone +44 (0)20 7327 1000 Fax +44 (0)20 7626 2389 www.lloyds.com