

LLOYD'S COMPENSATION INSTRUMENT 2003**Powers exercised**

- A. The Financial Services Authority gives the directions issued under sections 316 and 318 of the Financial Services and Markets Act 2000 ("the Act") as set out in the amendments to the Lloyd's sourcebook in this instrument.
- B. The Financial Services Authority amends the Compensation sourcebook and the Glossary in the exercise of the following powers and related provisions in the Act:
- (1) section 138 (General rule-making power);
 - (2) section 156 (General supplementary powers);
 - (3) section 157 (Guidance);
 - (4) section 213 (The compensation scheme);
 - (5) section 214 (General);
 - (6) section 215 (Rights of the scheme in relevant person's insolvency);
 - (7) section 216 (Continuity of long-term insurance policies);
 - (8) section 217 (Insurers in financial difficulties); and
 - (9) section 223 (Management expenses).
- C. The rule-making powers listed in B above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

Commencement

- D. This instrument comes into force as follows:
- (1) Annex B (Amendments to the Compensation Sourcebook) and Annex C (Amendments to the Glossary) to this instrument come into force on 1 January 2004;
 - (2) the remainder of this instrument comes into force immediately.

Amendments to the Lloyd's sourcebook

- E. The Lloyd's sourcebook is amended in accordance with Annex A to this instrument.

Amendments to the Compensation sourcebook

- F. The Compensation sourcebook is amended in accordance with Annex B to this instrument.

Amendments to the Glossary

- G. The Glossary is amended in accordance with Annex C to this instrument.

Citation

- H. This instrument may be cited as the Lloyd's Compensation Instrument 2003.

By order of the Board
15 October 2003

Annex A

Amendments to the Lloyd's sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire new section is inserted, the place that it goes is indicated and the text is not underlined.

3.1 (heading) **Application ~~and~~ purpose and enabling provision**

...

Enabling provision

3.1.4 D The directions in this chapter are given under section 318 of the *Act* (Exercise of powers through Council) for the purpose of achieving the objective specified, as required by section 318(2) of the *Act*.

3.1.5 D The directions given in this chapter are given in relation to the exercise of the powers by the *Society* in respect of the *Central Fund* and are given with a view to achieving the objective of ensuring that the *Society* in making payments or in providing any other financial assistance from the *Central Fund* does so on a basis which takes no account of amounts of compensation which policyholders may receive under the provisions of the *compensation scheme* in respect of *protected claims* against *members*.

...

3.2.1 G The *Society* should seek to ensure that the *Central Fund* provides protection for policyholders ~~at least equivalent to that available to other policyholders under the *compensation scheme*~~ so as to minimise the need for Lloyd's policyholders to have recourse to the *compensation scheme*.

...

3.2.3 D The *Society* must, in the exercise of its powers to make payments from the *Central Fund* or to provide other forms of financial assistance from the *Central Fund*, ensure that in calculating and determining the amount of any such payment or the amount of any other financial assistance, it takes no account of the amounts of compensation which policyholders may receive under the provisions of the *compensation scheme* in respect of *protected claims* against *members*.

...

After LLD 8 insert the following new chapter:

- 8A (heading) **Compensation Arrangements for policyholders**
- 8A.1 (heading) Enabling provision, application and purpose.**
- 8A.1.1 G **Enabling provision and application**
- The *insurance market direction* in this chapter is given under section 316(1) of the *Act* (Direction by Authority) and applies to *members*.
- Purpose**
- 8A.1.2 G The *insurance market direction* in this chapter is intended to protect the interests of *policyholders* and potential *policyholders* by:
- (1) providing for the application of the *compensation scheme* in respect of *contracts of insurance* issued by *members*; and
 - (2) providing for the application of such other provisions of the *Act* as will enable the application of the *compensation scheme* to be effective in relation to insurance market activities carried on by *members*.
- 8A.2 **Insurance market direction on policyholder compensation.**
- 8A.2.1 D With effect from 15 October 2003 the following *core provisions* of the *Act* apply to the carrying on of *insurance market activities* by *members*:
- (1) Part X (Rules and guidance) for the purpose of applying the rules in *COMP* and relevant interpretative provisions; and
 - ..
 - (2) Part XV (Financial Services Compensation Scheme).
- 8A.2.2G Section 317(2) of the *Act* (The core provisions) provides that references in an applied *core provision* to an *authorised person* are to be read as references to a *person* in the class to which the *insurance market direction* applies. In particular, with effect from 15 October 2003, references to a *relevant person* in Part XV of the *Act* include a person who was a *member* at the time the act or omission giving rise to the claim against him took place.

Annex B

Amendments to the Compensation Sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire new section is inserted, the place that it goes is indicated and the text is not underlined.

After Transitional Provision 8, insert the following new Transitional Provision.

Table Transitional Provisions Table

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook Provisions coming into force
...					
9	<i>COMP</i> 13.6.8R	R	<p>With regard to a <i>member, relevant net premium income</i> is to include the premium income in respect of <i>contracts of insurance</i>:</p> <p>(a) Entered into by the <i>member</i> in the year preceding that in which the date for submission of the information under <i>COMP</i> 13.6.11R falls; and</p> <p>(b) Which would have been <i>protected contracts of insurance</i> if entered into on or after 1 January 2004;</p> <p>net of any relevant rebates or refunds.</p>	1 January 2004 to 1 January 2005	<i>Commencement</i>

After *COMP* 1.4, insert the following new section:

1.5 (heading) **Application to Lloyd's**

1.5.1 G The *FSA* has exercised its power under section 316 of the *Act* (Direction by Authority) to direct in *LLD* 8A (Compensation Arrangements for policyholders) that certain *core provisions* in the *Act* should apply to *members* of the *Society* of Lloyd's (an “*insurance market direction*”). The effect of the direction is that the *FSA* may, in relation to *members*, and in respect of *insurance market activities* carried on by them, exercise any of the statutory powers conferred by the provisions which are applied by the direction. Those include the powers in Part X to make general *rules* and give *guidance* and also the powers in Part XV to make *rules* for the establishment and operation of a compensation scheme. Accordingly this sourcebook makes provision for the payment of compensation by the *FSCS* in certain cases arising from *insurance business* carried on by *members*, and for raising levies on the *Society*.

1.5.2 R Notwithstanding anything to the contrary in this sourcebook, in relation to the *Society*, *members* and *Lloyd's policies* *FSCS* must act, so far as is reasonably practicable, to ensure that:

- (1) *Eligible claimants* have protection under this sourcebook in relation to *Lloyd's policies* equivalent to that otherwise afforded to *eligible claimants* by the *FSCS*;
- (2) *FSCS* does not meet *claims* in relation to *Lloyd's policies* unless the *Central Fund* is unlikely to be able to meet them;
- (3) *Claims* against *members* under the *compensation scheme* which arise from the same loss under the same *Lloyd's policy* must be treated as a single *claim*;
- (4) any recovery resulting from the exercise of any rights assigned to the *FSCS* in connection with the payment of compensation to an *eligible claimant*, is treated by the *FSCS* in accordance with *COMP* 7.2.4R, and any such recovery which is not paid to the claimant in accordance with that rule, is used for the benefit of *FSCS* in priority to any interest that the *Society* may have.

1.5.3 G The effect of *COMP* 1.5.2 R(4) and *COMP* 7.2.4AR, and subject to 7.2.4 R(2), is that any recovery obtained by *FSCS* is retained by *FSCS* up to an amount equal to the cost to *FSCS* of paying compensation. To the extent that the *Society* is entitled to any part of the recovery (for example by agreement with *FSCS*) it is only paid out of any excess up to a maximum amount equal to that paid out of the *Central Fund*. Any recovery in excess of the compensation (including payment from the *Central Fund*) received by the policyholder is paid to the claimant in accordance with *COMP* 7.2.4R regardless of whether the *Society* receives the full amount paid from the *Central Fund*.

...

3.3.1 R The *FSCS* must make arrangements to secure continuity of insurance for an *eligible complainant* under a *protected contract of insurance* which is a *long term insurance contract* with a *relevant person*, if:

...

- (2) it is reasonably practical to do so; ~~and~~
- (3) the cost of doing so would, in the opinion of the *FSCS* at the time it proposes to make the arrangements, be likely to be no more than the cost of paying compensation under *COMP 3.2*; and
- (4) where the *relevant person* is a *member*, the *FSCS* is satisfied that the amounts which the *Society* is able to provide from the *Central Fund* are or are likely to be insufficient to ensure that *claims* against the *member* under a *protected contract of insurance* will be met to the level of protection which would otherwise be available under this sourcebook.

...

3.3.6 R For the purpose of *COMP 3.3.3R*, a *relevant person*, who is an *insurance undertaking* is in financial difficulties if:

...

- (4) the *FSA* determines that the *relevant person* who is an *insurance undertaking* is likely to be unable to satisfy *protected claims* against it; or

...

- (9) any of (1) to (8) or anything equivalent occurs in respect of the *relevant person* in a jurisdiction outside England and Wales; or
- (10) in the case of an *insurance undertaking* which is a *member*, the *FSCS* is satisfied that any of sub-paragraphs (1) to (9) apply to the *member*, and the amounts which the *Society* is able to provide from the *Central Fund* are or are likely to be insufficient to ensure that *claims* against the *member* under a *protected contract of insurance* will be met to the level of protection which would otherwise be available under this sourcebook.

...

5.4.2 R A *contract of insurance* issued after *commencement* which:

...

- (2) is issued by the *relevant person* through an establishment in the Channel Islands or the Isle of Man; ~~and~~
- (3) is a *long-term insurance contract* or a *relevant general insurance*

contract; and

- (4) is not a reinsurance contract; and
- (5) if it is a contract of insurance entered into by a member, was entered into on or after 1 January 2004;

is a *protected contract of insurance*.

...

- 5.4.5 R (1) If after *commencement*, a relevant person is subject to one or more of the proceedings listed in *COMP 6.3.3R* or is declared *in default*, then a *contract of insurance* issued by that *relevant person* before *commencement* which is within *COMP 5.4.2R(2)* is a *protected contract of insurance*, provided that the relevant person was not a member at the time the contract of insurance was issued, and:
- (a) (unless it comes within (b)) at the earlier of the events in (1) it was a “United Kingdom policy” for the purposes of the Policyholders Protection Act 1975;

...

...

- 6.3.2 R Subject to *COMP 3.3.3R* to *COMP 3.3.6 R* and *COMP 6.3.6R*, the *FSCS* (or, where *COMP 6.3.1R(2)(a)* applies, the *FSA*) may determine a *relevant person* to be *in default* when it is, in the opinion of the *FSCS* or the *FSA*:

...

- 6.3.3 R Subject to *COMP 6.3.6R*, the *FSCS* may determine a *relevant person* to be in default if it is satisfied that a *protected claim* exists (other than an *ICD claim* or *DGD claim*), and *the relevant person* is the subject of one or more of the following proceedings in the *United Kingdom* (or of equivalent or similar proceedings in another jurisdiction):

...

...

Members in default and the Central Fund of the Society

- 6.3.6 R The *FSCS* may not declare a *member* to be in default unless it is satisfied that the amounts which the *Society* may provide from the *Central Fund* are or are likely to be insufficient to ensure that *claims* against the *member* under a *protected contract of insurance* will be met to the level of protection which would otherwise be available under this sourcebook.

- 6.3.7 G If a *member* is unable fully to meet *protected claims* against it then in the first instance any shortfall will be avoided by payments by the *Society* from the assets of the *Central Fund*. The *FSCS* will not consider *claims* for compensation unless it is satisfied that the amounts which the *Society*

will make available from the *Central Fund* are or are likely to be insufficient to ensure that *claims* against the *member* under a *protected contract of insurance* will be met to the level of protection which would otherwise be available under this sourcebook. The amount which the *FSCS* may pay in respect of any such *claim* will be limited to the difference between the amount which the claimant will receive, or is expected to receive, from the *member* and the *Society* together and the maximum amount of compensation payable in accordance with *COMP 10* and *COMP 12*.

...

7.2.4A R For the purposes of *COMP 7.2.4R* compensation received by *eligible claimants* in relation to *Lloyd's policies* may include payments made from the *Central Fund*.

...

10.2.8 R **Claims against more than one member in respect of a single protected contract of insurance to be treated as a single claim**

In applying the financial limits in *COMP 10.2*, and in calculating the amount of a *claim* in respect of a *protected contract of insurance* arising from the default of one or more *members*, a *policyholder* is to be treated as having a single *claim* for the aggregate of all such amounts as may be payable on the *claim* in respect of the *protected contract of insurance*.

...

12.2.9 R In calculating the claimant's overall net *claim* the *FSCS* must take into account the amounts paid by, or expected to be paid by, the *Society* from the *Central Fund* to meet a *member's* liabilities under the contract which gives rise to the *claim*.

...

13.1.1 R This chapter applies to:

- (1) every *participant firm*; and
- (2) the *FSCS*; and
- (3) the *Society*.

13.1.2 G Although a *member* is a *participant firm* for the purposes of most provisions of *COMP*, a *member* is excluded from the definition of *participant firm* for the purposes of *COMP 13* (see definition of *participant firm* in the *Glossary*). This is because the fees levied in relation to the carrying on of *insurance market activities* by *members* will be imposed on the *Society* rather than individually on each *member* (see *COMP 13.4.21R*).

...

Levies on the Society of Lloyd's

13.4.21 R

The FSCS may impose a levy on the Society to be calculated as the aggregate of the levies that would be imposed on each member if this chapter applied to members, as follows:

- (a) a share of any un-expired portion of an establishment costs levy;
- (b) a proportionate share of a base costs levy in respect of the compensation scheme's costs for the period from 1 January 2004 to the end of the compensation scheme's financial year and a share of such levies for all subsequent financial years;
- (c) a specific costs levy and a compensation costs levy in respect of costs arising out of a relevant person being in default, arrangements made under COMP 3.3.1R or measures taken under COMP 3.3.3R where the default occurs or the circumstances giving rise to the arrangements being made or the measures being taken, as the case may be, occur after 1 January 2004.

Annex C

Amendments to the Glossary

Insert the following new definition in the appropriate alphabetical position:

insurance market activity means a *regulated activity* relating to *contracts of insurance* written at Lloyd's.

Amend the following definitions as shown (underlining indicated new text and striking through indicates deleted text):

insurance undertaking an undertaking, or (in COMP) a member, whether or not an *insurer*, which carries on *insurance business*.

participant firm (1) (except in COMP 13) a *firm* or a member other than:

- (a) (in accordance with section 213(10) of the *Act* (The compensation scheme) and regulation 2 of the *Electing Participants Regulations* (Persons not to be regarded as relevant persons) an incoming *EEA firm* which is:
 - (i) a *credit institution*;
 - (ii) an *ISD investment firm*; or
 - (iii) both (i) and (ii);in relation to its *passported activities*, unless it has *top-up cover*;
- (b) a *service company*;
- (c) ~~[deleted] the Society, in respect of activities included in its permission under section 315(2) of the Act (The Society: authorisation and permission);~~
- (d) ~~[deleted] a member, in respect of effecting or carrying out Lloyd's policies;~~
- (e) an *underwriting agent*, or *members' adviser*, in respect of *advising on syndicate participation at Lloyd's* or *managing the underwriting capacity of a Lloyd's syndicate as a managing agent at Lloyd's*;
- (f) an *authorised professional firm* that is subject to the rules of the Law Society (England and Wales) or the Law Society of Scotland;
- (g) an *ICVC*;
- (h) a *UCITS qualifier*;
- (i) an *ELMI* in relation to *issuing e-money*.

(2) (in COMP 13) a *firm* specified in paragraph (1) above that is not a *member*.

relevant general insurance contract (in COMP) any *general insurance contract* other than:

- (a) a reinsurance contract;
- (b) ~~[deleted]~~ a *Lloyd's policy*;
- (c) a contract falling within any of the following classes:
 - (i) *aircraft*;
 - (ii) *ships*;
 - (iii) *goods in transit*;
 - (iv) *aircraft liability*;
 - (v) *liability of ships*;
 - (vi) *credit*.