

LLOYD'S

**THE SOCIETY OF LLOYD'S***(a statutory corporation incorporated by Lloyd's Act 1871)***£300,000,000 Fixed to Floating Rate Callable Subordinated Notes due 2047****Issue Price 99.944 per cent.**

The £300,000,000 Fixed to Floating Rate Subordinated Callable Notes due 2047 (the "Notes") will be issued by the Society of Lloyd's (the "Issuer") on 7 February 2017 (the "Issue Date"). The Notes will bear interest from (and including) the Issue Date to (but excluding) 7 February 2027 (the "First Call Date") at a fixed rate of 4.875 per cent. per annum payable annually in arrear on each Fixed Interest Payment Date (as defined in the Terms and Conditions of the Notes (the "Conditions")) commencing on 7 February 2018, and thereafter at a floating rate of interest equal to 3-month LIBOR plus the Margin (as defined in the Conditions), payable quarterly in arrear on each Floating Interest Payment Date (as defined in the Conditions) (each Floating Interest Payment Date, together with the Fixed Interest Payment Dates, the "Interest Payment Dates"). The Notes will constitute subordinated obligations of the Issuer. Payments of interest on the Notes may be deferred by the Issuer on any Optional Interest Payment Date (as defined in the Conditions) and must be deferred by the Issuer (i) on each Mandatory Interest Deferral Date (as defined in the Conditions) or (ii) if such payment could not be made in compliance with Condition 3.2(a), as more particularly described in the Conditions. Any interest which is deferred will, for so long as it remains unpaid, constitute "Arrears of Interest". Arrears of Interest will not themselves bear interest, and will be payable as provided in Condition 5.5. Payments in respect of the Notes will be made without withholding or deduction for, or on account of, taxes of the United Kingdom, unless such withholding or deduction is required by law. If any such withholding or deduction is made, additional amounts may be payable by the Issuer, subject to certain exceptions as are more fully provided for in "Terms and Conditions of the Notes — Taxation".

The Notes will (unless previously redeemed or purchased and cancelled) mature on the Interest Payment Date falling in February 2047 (the "Maturity Date"), and may be redeemed prior to such date, subject to certain conditions described below, (i) on the First Call Date or any Floating Interest Payment Date thereafter, or (ii) in the event of certain circumstances affecting the tax treatment applicable to the Notes or payments thereunder or (iii) following the occurrence of (or if the Issuer satisfies the Trustee that there will occur within six months) a Capital Disqualification Event or a Ratings Methodology Event; provided that in the case of any redemption prior to the fifth anniversary of the Issue Date, the Notes are exchanged for, or redeemed out of the proceeds of, capital of the same or higher quality. The redemption of the Notes on the Maturity Date or any other date set for redemption of the Notes shall be deferred if (a) a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing on such date, or would occur if the Notes were to be redeemed or (b) the Notes could not be redeemed in compliance with Condition 3.2(a) or (c) the Regulatory Clearance Condition is not satisfied on such date. The Issuer may, alternatively, following the occurrence of (or if the Issuer satisfies the Trustee that there will occur within six months) a Capital Disqualification Event or a Ratings Methodology Event or in the event of certain circumstances affecting the tax treatment applicable to the Notes or payments thereunder, vary or substitute the Notes in the circumstances described in Condition 7. Any substitution or variation of the Notes, and any redemption or purchase of the Notes prior to the Maturity Date, will be subject to satisfaction of the Regulatory Clearance Condition and the Issuer being in continued compliance with applicable Regulatory Capital Requirements (as defined in the Conditions), all as more particularly provided for in Condition 7.8.

Application has been made to the Financial Conduct Authority under Part VI of the Financial Services and Markets Act 2000 ("FSMA") (the "UK Listing Authority") for the Notes to be admitted to the official list of the UK Listing Authority (the "Official List") and to the London Stock Exchange plc (the "London Stock Exchange") for such Notes to be admitted to trading on the London Stock Exchange's regulated market (the "Market"). References in this Prospectus to the Notes being "listed" (and all related references) shall mean that the Notes have been admitted to the Official List and have been admitted to trading on the Market. The Market is a regulated market for the purposes of Directive 2004/39/EC of the European Parliament and of the Council on markets in financial instruments.

An investment in the Notes involves certain risks. For a discussion of these risks see "Risk Factors" below.

**PROHIBITION OF SALES TO EEA RETAIL INVESTORS** – The Notes are not intended from the date of application of Regulation (EU) No 1286/2014 (the "PRIIPs Regulation"), to be offered, sold or otherwise made available to and, with effect from such date, should not be offered, sold or otherwise made available to any retail investor in the European Economic Area ("EEA"). For these purposes, a retail investor means a person who is one (or more) of: (i) a retail client as defined in point (11) of Article 4(1) of Directive 2014/65/EU ("MiFID II"); (ii) a customer within the meaning of Directive 2002/92/EC, where that customer would not qualify as a professional client as defined in point (10) of Article 4(1) of MiFID II; or (iii) not a qualified investor as defined in Directive 2003/71/EC (as amended, the "Prospectus Directive"). Consequently no key information document required by the PRIIPs Regulation for offering or selling the Notes or otherwise making them available to retail investors in the EEA has been (or is intended to be) prepared and therefore offering or selling the Notes or otherwise making them available to any retail investor in the EEA may be unlawful under the PRIIPs Regulation (once in force).

The Notes are expected to be assigned a rating of A- by Standard & Poor's Credit Market Services Europe Limited ("Standard & Poor's"), a- by A.M. Best Europe – Rating Services Limited ("A.M. Best") and A- by Fitch Ratings Limited ("Fitch") (each a "Rating Agency"). Each Rating Agency is established in the European Union and is registered under Regulation (EC) No. 1060/2009 (as amended) of the European Parliament and of the Council of 16 September 2009 on credit rating agencies (the "CRA Regulation"). A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency.

**JOINT LEAD MANAGERS**

**Citigroup**  
*(Structuring Advisor)*

**Lloyds Bank**

**NatWest Markets**

3 February 2017

This Prospectus comprises a prospectus for the purposes of Directive 2003/71/EC (as amended, including by Directive 2010/73/EC), and including any relevant implementing measure in a relevant Member State of the EEA (the “**Prospectus Directive**”) and for the purpose of giving information with regard to the Issuer and the Notes which, according to the particular nature of the Issuer and the Notes, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses and prospects of the Issuer. The Issuer accepts responsibility for the information contained in this Prospectus. To the best of the knowledge of the Issuer (which has taken all reasonable care to ensure that such is the case), the information contained in this Prospectus is in accordance with the facts and does not omit anything likely to affect the import of such information.

This Prospectus is to be read in conjunction with all the documents which are incorporated herein by reference (see “*Documents Incorporated by Reference*”).

This Prospectus does not constitute an offer of, or an invitation by or on behalf of the Issuer, the Joint Lead Managers (as defined in “*Subscription and Sale*” below) or any other person to subscribe or purchase, any of the Notes. The distribution of this Prospectus and the offering of the Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Prospectus comes are required by the Issuer and the Joint Lead Managers to inform themselves about and to observe any such restrictions. For a description of certain further restrictions on offers and sales of the Notes and distribution of this Prospectus, see “*Subscription and Sale*”.

No person has been authorised to give any information or to make any representation other than those contained in this Prospectus in connection with the issue or sale of the Notes and, if given or made, such information or representation must not be relied upon as having been authorised by or on behalf of the Issuer, the Trustee or the Joint Lead Managers. Neither the delivery of this Prospectus nor any sale made in connection herewith shall, under any circumstances, create any implication that there has been no change in the affairs of the Issuer since the date hereof or the date upon which this Prospectus has been most recently amended or supplemented or that there has been no adverse change in the financial position of the Issuer since the date hereof or the date upon which this Prospectus has been most recently amended or supplemented or that any other information supplied in connection with the Notes is correct as of any time subsequent to the date on which it is supplied or, if different, the date indicated in the document containing the same.

To the fullest extent permitted by law, neither the Joint Lead Managers nor the Trustee accept any responsibility whatsoever for the contents of this Prospectus or for any other statement, made or purported to be made by a Joint Lead Manager, the Trustee or on their behalf in connection with the Issuer or the issue and offering of the Notes. Each Joint Lead Manager and the Trustee accordingly disclaim all and any liability whether arising in tort or contract or otherwise which it might otherwise have in respect of this Prospectus or any such statement.

The Notes have not been and will not be registered under the U.S. Securities Act of 1933, as amended (the “**Securities Act**”) or with any securities regulatory authority of any state or other jurisdiction of the United States. Subject to certain exceptions, Notes may not be offered, sold or delivered within the United States or to U.S. persons.

None of the Issuer, the Trustee or the Joint Lead Managers is providing any advice or recommendation in this Prospectus on the merits of the purchase, subscription for, or investment in, the Notes or the exercise of any rights conferred by the Notes.

The Notes are securities which, because of their nature, are normally bought and traded by a limited number of investors who are particularly knowledgeable in investment matters. This Prospectus has been prepared on the basis that any purchaser of Notes is a person or entity having sufficient knowledge and experience of financial matters as to be capable of evaluating the merits and risks of the purchase. Before making any investment decision with respect to the Notes, prospective investors should consult their own counsel, accountants or other advisers and carefully review and consider their investment decision in the light of the foregoing. An investment in the Notes is only suitable for financially sophisticated investors who are capable

of evaluating the merits and risks of such an investment and who have sufficient resources to be able to bear any losses which may result therefrom.

**In connection with the issue of the Notes, Citigroup Global Markets Limited (the “Stabilising Manager(s)”) (or any person acting on behalf of any Stabilising Manager(s)) may over-allot Securities or effect transactions with a view to supporting the market price of the Notes at a level higher than that which might otherwise prevail. However, stabilisation may not necessarily occur. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the Notes is made and, if begun, may cease at any time, but it must end no later than the earlier of 30 days after the issue date of the Notes and 60 days after the date of the allotment of the Notes. Any stabilisation action or over-allotment must be conducted by the relevant Stabilising Manager(s) (or any person acting on behalf of any Stabilising Manager(s)) in accordance with all applicable laws and rules.**

In this Prospectus, unless otherwise specified or the context otherwise requires, references to “£”, “pounds sterling”, “pounds” or “pence” are to the lawful currency of the United Kingdom and references to “U.S.\$” or “U.S. dollars” are to United States dollars.

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## OVERVIEW

*This overview must be read as an introduction to this Prospectus and any decision to invest in the Notes should be based on a consideration of this Prospectus as a whole, including the documents incorporated by reference herein. Capitalised terms which are defined in “Terms and Conditions of the Notes” have the same meaning when used in this overview.*

<b>Issuer</b> .....	The Society of Lloyd’s
<b>Notes</b> .....	£300,000,000 Fixed to Floating Rate Callable Subordinated Notes due 2047.
<b>Issue Date</b> .....	7 February 2017.
<b>Issue Price</b> .....	99.944 per cent.
<b>Status and Subordination</b> .....	<p>The Notes constitute direct, unsecured and subordinated obligations of the Issuer, and will at all times rank <i>pari passu</i> without any preference among themselves. The rights and claims of the holders of Notes (“<b>Noteholders</b>”) against the Issuer are subordinated in a winding-up of the Issuer as provided for in Condition 3.2.</p> <p>In addition, other than in the circumstances set out in Condition 3.2(b) and without prejudice to Condition 10.1 all payments under or arising from the Notes and the Trust Deed shall be mandatorily deferred unless the Issuer is Solvent at the time for payment by the Issuer, and unless and until such time as the Issuer could make such payment and still be Solvent immediately thereafter.</p>
<b>Interest</b> .....	<p>The Notes will bear interest from (and including) the Issue Date to (but excluding) 7 February 2027 (the “<b>First Call Date</b>”) at the rate of 4.875 per cent. per annum, payable (subject as provided under “<i>Deferral of Interest</i>”) annually in arrear on each Fixed Interest Payment Date, commencing on 7 February 2018.</p> <p>From (and including) the First Call Date to (but excluding) the Maturity Date, the Notes will bear interest at a floating rate equal to the sum of (i) 3-month LIBOR, and (ii) a margin of 4.479 per cent., payable (subject as provided under “<i>Deferral of Interest</i>” below) quarterly in arrear on each Floating Interest Payment Date.</p>
<b>Deferral of Interest</b> .....	<p><b>Optional deferral:</b> In respect of any Interest Payment Date that is not a Compulsory Interest Payment Date or a Mandatory Interest Deferral Date, the Issuer may in its discretion elect to defer payment of all (but not some only) of the accrued but unpaid interest to that Interest Payment Date, and in such circumstances the relevant interest payment shall not fall due on such Interest Payment Date and the Issuer shall have no obligation to make such payment on that date.</p> <p><b>Mandatory deferral:</b> The Issuer is required to defer any payment of interest on the Notes on each Mandatory Interest Deferral Date (being an Interest Payment Date in respect of which a Regulatory Deficiency Interest Deferral Event has</p>

occurred and is continuing or would occur if payment of interest was made on such Interest Payment Date).

**Arrears of Interest**..... Any interest which is deferred by the Issuer pursuant to Conditions 3.2(a), 5.1 or 5.2 will, for so long as it remains unpaid, constitute Arrears of Interest. Arrears of Interest will not themselves bear interest, and will be payable by the Issuer as provided in Condition 5.5.

**Redemption at maturity** ..... Unless previously redeemed or purchased and cancelled, the Issuer will (subject as provided under “*Deferral of redemption*” below) redeem the Notes on the Interest Payment Date falling in February 2047.

**Optional redemption** ..... The Issuer may elect, subject as provided under “*Deferral of redemption*” and “*Preconditions to redemption, variation substitution or purchase*” below and subject to it being in compliance with Condition 3.2(a), to redeem all (but not some only) of the Notes on the First Call Date or any Floating Interest Payment Date thereafter at their principal amount together with any Arrears of Interest, and any other accrued and unpaid interest thereon to (but excluding) the date of redemption.

**Redemption, substitution or variation upon a relevant tax event** ..... If:

(a) (i) as a result of a change or proposed change in, or amendment to, certain tax laws or regulations or the official interpretation thereof, on the next Interest Payment Date, the Issuer would be required to pay additional amounts on the Notes as provided in Condition 8 or the Issuer would otherwise suffer adverse tax consequences; or (ii) in respect of the Issuer’s obligation to make any payment of interest on the Notes on the next following Interest Payment Date, the Issuer would not be entitled to claim a deduction in respect of computing its taxation liabilities in the United Kingdom, or such entitlement is materially reduced; and

(b) in each case, the effect of the foregoing cannot be avoided by the Issuer taking reasonable measures available to it, the Issuer may, in accordance with Condition 7.5, upon notice to Noteholders either:

(A) redeem all (but not some only) of the Notes at any time up to, and including, the First Call Date, or on any Floating Interest Payment Date thereafter at their principal amount together with any Arrears of Interest and any other accrued and unpaid interest to (but excluding) the date of redemption (subject as provided under “*Deferral of redemption*” below); or

(B) substitute all (but not some only) of the Notes for, or vary the terms of the Notes so that they become or remain, Qualifying Tier 2 Securities,

all as more particularly described in Condition 7.5.

**Redemption, substitution or variation upon a Capital Disqualification Event**

If a Capital Disqualification Event or a Ratings Methodology Event has occurred and is continuing, or the Issuer satisfies the

**or a Ratings Methodology Event.....** Trustee that, as a result of any change in, or amendment to, or any change in the application or official interpretation of, any applicable law, regulation, ratings methodology or other official publication, the same will occur within a period of six months, the Issuer may upon notice to Noteholders either:

- (a) redeem all (but not some only) of the Notes at any time up to, and including, the First Call Date, or on any Floating Interest Payment Date thereafter at their principal amount, together with any Arrears of Interest and any other accrued and unpaid interest to (but excluding) the date of redemption (subject as provided under “*Deferral of redemption*” below); or
- (b) substitute all (but not some only) of the Notes at any time for, or vary the terms of the Notes so that they become or remain, Qualifying Tier 2 Securities (in the case of a Capital Disqualification Event) or Rating Agency Compliant Securities (in the case of a Ratings Methodology Event),

all as more particularly described in Condition 7.6.

**Deferral of redemption.....** No Notes shall be redeemed by the Issuer on the Maturity Date or on any other date set for redemption pursuant to Conditions 7.1, 7.2, 7.5 or 7.6 if (i) a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing or would occur if the Notes were to be redeemed, or (ii) such redemption could not be made in compliance with Condition 3.2(a) or (iii) the Regulatory Clearance Condition is not satisfied on such date.

If redemption of the Notes is deferred, the Issuer will redeem the Notes as provided in Condition 7.3.

**Preconditions to redemption, variation, substitution or purchase .....** Prior to publishing any notice (a) that the Issuer intends to redeem the Notes before the Maturity Date or (b) of any proposed substitution, variation or purchase of the Notes, the Issuer will be required to have complied with the Regulatory Clearance Condition with respect to such redemption, variation, substitution or purchase and be in continued compliance with Regulatory Capital Requirements as published by the Relevant Regulator.

In addition, in the case of any redemption prior to the fifth anniversary of the Issue Date, such redemption will only be made on the condition that the Notes are exchanged for, or redeemed out of the proceeds of a new issue of, capital of the same or higher quality.

<b>Withholding tax and additional amounts</b> .....	All payments in respect of the Notes by or on behalf of the Issuer will be made without withholding or deduction for, or on account of, any Taxes imposed by a Relevant Jurisdiction, unless the withholding or deduction is required by law. In that event, the Issuer will pay such additional amounts as may be necessary in order that the net payment received by each Noteholder in respect of the Notes, after withholding or deduction will equal the amount which would have been received in the absence of any such withholding or deduction, subject to customary exceptions as set out in Condition 8.
<b>Events of Default</b> .....	<p>If default is made by the Issuer for a period of 14 days or more in the payment of any interest (including Arrears of Interest) or principal or premium due in respect of the Notes or any of them, the Trustee on behalf of the Noteholders may (and, subject to certain conditions, if so directed by the requisite majority of Noteholders shall) institute proceedings for the winding-up of the Issuer in England and Wales (but not elsewhere), and/or prove in the winding-up of the Issuer (whether in England or elsewhere) but may take no further action to enforce, prove or claim for any payment by the Issuer in respect of the Notes or the Trust Deed.</p> <p>Upon the occurrence of a winding-up of the Issuer, the Trustee may (and, subject to certain conditions, if so directed by the requisite majority of the Noteholders shall) give notice to the Issuer that the Notes are, and they shall accordingly become, immediately due and payable by the Issuer at their principal amount together with any Arrears of Interest and any other accrued and unpaid interest and/or prove in the winding-up of the Issuer.</p>
<b>Form</b> .....	<p>The Notes will be issued in registered form and represented upon issue by a registered global certificate (the “<b>Global Certificate</b>”) which will be registered in the name of a nominee for a common depository (the “<b>Common Depository</b>”) for Clearstream Banking S.A. (“<b>Clearstream, Luxembourg</b>”) and Euroclear Bank SA/NV (“<b>Euroclear</b>”) on or about the Issue Date.</p> <p>Save in limited circumstances, Notes in definitive form will not be issued in exchange for interests in the Global Certificate.</p>
<b>Denomination</b> .....	The Notes will be issued in denominations of £100,000 each and integral multiples of £1,000 in excess thereof.
<b>Listing</b> .....	Admission to listing on the UK Listing Authority’s Official List and to trading on the regulated market of the London Stock Exchange.
<b>Ratings</b> .....	<p>The Notes are expected to be assigned ratings of A- by Standard &amp; Poor’s, A- by Fitch and a- by A.M. Best.</p> <p>A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency.</p>
<b>Governing law</b> .....	The Notes and the Trust Deed, and any non-contractual obligations arising out of or in connection with the Notes or the Trust Deed, will be governed by, and construed in accordance with, English law.

<b>Trustee</b> .....	Citicorp Trustee Company Limited.
<b>Principal Paying Agent</b> .....	Citibank, N.A., London Branch.
<b>Registrar</b> .....	Citigroup Global Markets Deutschland AG.
<b>Selling restrictions</b> .....	Customary selling restrictions in the U.S. and UK.
<b>Use of Proceeds</b> .....	The net proceeds of the issue of the Notes will be used to provide the Issuer with additional solvency capital to meet regulatory capital requirements and for general corporate purposes.

## RISK FACTORS

*The Issuer believes that the following factors may affect its ability to fulfil its obligations under the Notes. Most of these factors are contingencies which may or may not occur and the Issuer is not in a position to express a view on the likelihood of any such contingency occurring.*

*In addition, factors which the Issuer believes may be material for the purpose of assessing the market risks associated with the Notes are described below.*

*The Issuer believes that the factors described below represent the principal risks inherent in investing in the Notes, but the inability of the Issuer to pay interest, principal or other amounts on or in connection with the Notes may occur for other reasons. The Issuer does not represent that the statements below regarding the risks of holding the Notes are exhaustive. Prospective investors should also read the detailed information set out elsewhere in this Prospectus (including any documents incorporated by reference herein) and reach their own views prior to making any investment decision.*

*Capitalised terms which are defined in “Terms and Conditions of the Notes” have the same meaning when used herein.*

### **Factors that may affect the Issuer’s ability to fulfil its obligations under the Notes**

#### ***The Issuer is indirectly exposed to a range of insurance risks assumed by its members***

The Issuer does not itself underwrite insurance and its principal activities include authorising and monitoring market participants (including members of Lloyd’s and managing agents) and agreeing syndicate business plans and capital and monitoring syndicate level systems and controls. The Issuer does not have liability for the risks underwritten by its members, although it may, at its discretion, make its assets (in particular, the Central Fund (as defined in the Conditions)) available to meet the underwriting liabilities of certain Lloyd’s members where those members are unable to meet these liabilities in full. See “*The Society of Lloyd’s – Resources within the Lloyd’s market and Protection of Policyholders*”.

As a result, the Issuer is indirectly exposed to insurance risk, which includes the risks arising from the underwriting, reinsurance, claims and reserving activities of the Lloyd’s market. This covers the inherent uncertainties about the occurrence, amount and timing of insurance liabilities and premiums and also includes the risk of loss arising from prospective underwriting and the claims development in respect of the reserves established for previous events. These risks are each described in more detail below.

The assessment of reinsurance as part of insurance risk relates to the potential for exhaustion of cover as well as risk of reinsurer dispute or default.

In the event that any one or more members of the Lloyd’s market are materially adversely affected by insurance risk, including each of the separate aspects of insurance risk described below, this could reduce the Issuer’s assets through making available the Central Fund, damage the Issuer’s reputation or lead to a rating downgrade, all of which could result in the loss of existing members or deter potential new members and so reduce the Issuer’s income and the capacity of the Lloyd’s market.

#### ***Lloyd’s members maintain reserves for their insurance business which are estimates of the expected future cost of the ultimate settlement of claims and any insufficiency in reserves could adversely affect their income and profitability***

Lloyd’s members maintain reserves for their insurance business to cover their estimated ultimate liability for claims and claim adjustment expenses for reported and unreported claims incurred as at the end of each accounting period. Reserving risk arises where the reserves established are not adequate to meet eventual claims arising. The level of uncertainty varies significantly among different classes of insurance business but can arise from inadequate case estimates for reported claims or inadequate provisions for incurred but not reported claims. These shortfalls can arise from inadequate reserving processes or from the naturally uncertain progress of insurance events, including the impact of legislative changes or adverse court decisions.

The Issuer's oversight of reserves at class and syndicate levels includes regular reviews and analyses such as a relative reserve benchmarking exercise. The Issuer actively engages with managing agents to identify exposure. Where the Issuer perceives that a syndicate may have an inadequate reserving process or practice, then it may impose additional requirements on the managing agent of the syndicate, for example explicit capital loadings or more stringent reporting. The Issuer also briefs the Lloyd's market on issues it believes need to be considered, including risks relating to macro influences such as inflation, the general economic environment or changes in legislation, which are currently considered to be the main risks. In the reserving process, managing agents use a variety of statistical analyses including projections of historical loss development patterns, with results adjusted for expert judgement. There are limits to the effectiveness of these tools, including, in particular, the fact that analysis based on historical trends is unlikely to prove accurate when historically anomalous conditions occur. Lloyd's syndicates have significant exposure to volatile classes of business which carry material inherent risk that the ultimate claims settlement will vary from previous assessments of reserves.

Although the Lloyd's market is currently experiencing only limited specific reserving issues, there is no certainty that this will remain the case.

***Lloyd's members are exposed to underwriting risk which could result in their incurring significant losses***

Underwriting risk relates to future periods of cover and includes the risk that a policy will be written for too low a premium, provide inappropriate cover or that the frequency or severity of the events insured against will be higher than expected. Underwriting risk includes the risk of catastrophes covered separately below.

Underwriting strategy is agreed by the board of each managing agent and set out in the syndicate business plan which is submitted to the Issuer each year. Approval of business plans and setting capital requirements needed to support those plans are the key controls the Issuer uses to manage underwriting risk. In addition, the Issuer uses a number of other mechanisms for controlling and monitoring insurance risk. These include:

- (i) the use of a risk management framework to manage key risk issues at both Issuer and syndicate level;
- (ii) setting underwriting managements guidelines which cover, inter alia, business planning, underwriting controls and catastrophe exposure;
- (iii) establishing and monitoring underwriting standards, including claims and exposure management principles; and
- (iv) determining appropriate capital requirements for members.

For further detail on these controls, see "*The Society of Lloyd's – Managing the Lloyd's market*".

However, these controls may not be sufficient to ensure all risks are adequately covered. The controls seek to manage risk partly through the use of observed historical market behaviour and statistics based on historical models. These methods may not fully predict future risk exposures, which may be significantly greater than the historical measures indicate. Other risk management methods depend upon the evaluation of information regarding markets, clients, catastrophe occurrence or other available information. This information may not always be accurate, complete, up-to-date or properly evaluated. In addition, certain risks could be greater than the available empirical data would otherwise indicate.

***Lloyd's members could be exposed to unexpectedly large losses as a result of catastrophic occurrences***

Lloyd's members are subject to losses from unpredictable events that may affect multiple covered risks and give rise to unexpected losses which have a material adverse effect on their financial condition, results of operations and cash flows. These events include both natural and man-made events, such as, but not limited to, earthquakes, windstorms, coastal inundation, floods, severe hail, severe winter weather, severe prolonged dry weather, other weather-related events, pandemics, large-scale fires, industrial explosions and other man-made disasters such as civil unrest and terrorist attacks.

The extent of a Lloyd's member's losses from such catastrophic events is a function of their frequency, the severity of each individual event and the reinsurance arrangements the Lloyd's market has in place. Some catastrophes, such as explosions, occur in small geographic areas, while others, including windstorms and floods, may produce significant damage to large, heavily populated and/or widespread areas.

The Issuer and Lloyd's managing agents typically use catastrophe modelling software, where appropriate, to monitor aggregate exposure to catastrophe losses and to estimate exceedance probabilities. Such models are based on generally accepted scientific and engineering theories. The Issuer has also developed a suite of Realistic Disaster Scenarios ("RDSs") to measure syndicate level and aggregate market exposure to both natural catastrophes and man-made losses. See generally "*The Society of Lloyd's - Managing the Lloyd's market*".

However, Lloyd's members' efforts to reduce their exposure to, or appropriately price, or set appropriate underwriting terms for, catastrophic exposure still result in some events producing claims that significantly exceed the reserves held. The frequency and severity of catastrophes are inherently unpredictable and subject to long term external influences, such as climate change, and a single catastrophe or multiple catastrophes in any period could have a material adverse effect on the business, results of operations and financial position of one or more Lloyd's members.

***Lloyd's members obtain reinsurance against certain risks and are exposed to any reduced availability of reinsurance and failure by their reinsurers to perform their obligations***

Lloyd's members systematically transfer their exposure to certain risks to third parties through reinsurance arrangements which may include inter-syndicate reinsurances. Under these arrangements, other insurers (including members of other Lloyd's syndicates) assume a portion of the relevant member's losses and expenses associated with reported and unreported losses in exchange for a portion of policy premiums.

The availability, amount and cost of reinsurance depend on general market conditions and may vary significantly from time to time. Any increase in a Lloyd's member's reinsurance costs may reduce its net underwriting result if it is unable to pass the increased costs on to its customers and any decrease in the amount of its ceded reinsurance, whether as a result of non-availability of cover or a high cost of cover, will increase its risk of losses. When it obtains reinsurance, a Lloyd's member could still be liable for reinsured risks, in particular if the relevant reinsurance policy is poorly worded, there is a mismatch with the gross loss or the reinsurer is unwilling and/or unable to meet its obligations. Accordingly, Lloyd's members bear risk with respect to their reinsurers and could be faced with a reinsurer's inability or unwillingness to meet its financial obligations when falling due. The Issuer monitors the level of reinsurance risk transfer (and also specifically intra-Lloyd's market reinsurance risk transfer) at market level and has set risk appetite metrics to ensure that the Issuer is able to consider whether it needs to engage with managing agents about any specific issues or concerns.

Lloyd's members are also exposed to credit risk in their investment portfolio (see "*The Issuer and Lloyd's members are exposed to a range of investment risks including market and credit related risks*") and their premium debtors.

***The nature of the general insurance industry may cause fluctuations in the Lloyd's market's results***

Historically, the general insurance industry has been subject to cyclical patterns, particularly since demand for property and casualty insurance is usually price-sensitive because of the limited degree of product differentiation inherent in the industry. In the past, this has caused significant cyclical fluctuations and volatility in the results of operations of the general insurance industry. Many of the factors contributing to these cyclical patterns are beyond the direct control of any insurer and therefore unpredictable as to timing and consequence, such as: changes in the macroeconomic environment (including economic downturns) as well as conditions in the credit and other capital markets, which can affect the Issuer's returns on its investments; the timing and/or severity of weather-related or other catastrophic events, which can affect the Lloyd's market's claims and/or losses; changes in the levels of insurance and reinsurance underwriting capacity; and changes in the level and effect of competition.

Current market conditions are driven by a number of factors including extremely high levels of insurance capital (both traditional and alternative capital supporting, for example, insurance linked securities which have gained mainstream acceptance, reducing reinsurance prices), the challenging global macro-economic environment (including low interest rates and investment income) and a low level of major insured catastrophes. These conditions affect insurance rates and cause weakening terms and conditions as well as increase the level of competition which the Lloyd's market faces in key markets and as such could affect the Lloyd's market's overall profitability.

***The Issuer is facing increased regulation, both within the United Kingdom and overseas***

The Issuer is subject to regulation by the Prudential Regulation Authority (“PRA”) and the Financial Conduct Authority (“FCA”) (see “*The Society of Lloyd's – External Regulation of the Lloyd's market*”).

The PRA and the FCA have adopted a more intrusive and direct style of regulation, which means that PRA and/or FCA authorised firms, including the Issuer, are facing increasing supervisory scrutiny. The PRA and the FCA have the power to take a range of investigative, disciplinary and enforcement actions, penalties for which can include public censure, restitution, fines and sanctions. The regulators may also make enquiries of the firms which they regulate and require the provision of particular information or documents. The regulators may take such action or make such enquiries in relation to aspects of the Issuer's business and operations, including its governance, systems and controls, IT systems, capital requirements, capital adequacy and permitted investments. Regulatory action may be specific to the Issuer or part of more general action in respect of firms that operate in the Issuer's sector.

As a result of the authorisations which the Lloyd's market has worldwide, there is also a risk of regulatory action from overseas regulators in the event that the Lloyd's market does not comply with international regulatory requirements. In addition, fundamental changes to prudential regulatory frameworks internationally may affect how the Issuer and the Lloyd's market is supervised as well as affecting the level of assets required to be held locally. There is an increasing regulatory trend to require insurers to hold local capital which may result in increased overseas funding requirements for the Issuer and the Lloyd's market in places where the market is already licenced or as part of negotiating and agreeing new licence arrangements with local regulators as the Issuer implements its strategic plans for increasing the market's share of insurance business in developing markets.

In addition to financial and insurance regulation, the Issuer and the Lloyd's market must comply with anti-money laundering, anti-bribery and corruption and sanctions laws and regulations. The Issuer is committed to working with international organisations, governments, law enforcement agencies, regulators and its industry peers to assist the Lloyd's market with identifying and addressing money laundering, bribery and corruption and sanctions issues. In addition to implementing its own policies and controls, the Issuer also requires managing agents to implement appropriate policies and procedures to ensure compliance with anti-money laundering, anti-bribery and corruption and sanctions laws. Regulatory investigations and/or enforcement actions against the Issuer or the Lloyd's market in relation to anti-money laundering, anti-bribery and corruption and sanctions laws or regulations could result in fines, immediate reputational and regulatory risks, and materially adversely impact the Lloyd's market's business, operations and financial position.

Whilst the Issuer believes that its systems, policies, controls and operations are compliant with applicable laws and regulations, there is a risk that one or more authorities could find that the Issuer has failed to fully comply with all relevant legal and regulatory requirements, or has not undertaken any corrective action as required.

Any regulatory action could have a negative impact upon the Issuer. Regulatory action against the Issuer could result in adverse publicity for, or negative perceptions regarding, the Issuer, or could have an adverse effect on the business of the Lloyd's market, its results of operations or its financial condition. It is not possible to predict the significance of any proceedings that may be brought against, or any investigations that may be conducted into, the Issuer nor is it possible to predict the financial impact of a successful claim, fine or penalty to which the Issuer may become subject.

The Issuer's activities and strategies are based upon prevailing legislation and regulation. Changes in legislation, and differing interpretation and application of regulation, may have a detrimental effect on the Lloyd's market's strategy and profitability.

### ***Impact of the UK's vote to leave the European Union (Brexit)***

On 23 June 2016, a referendum was held on the UK's membership of the EU, the outcome of which was a vote in favour of leaving the EU. The potential outcome of the negotiations on UK withdrawal and any subsequent negotiations on trade and access to the country's major trading markets, including the European Single Market, is currently unknown.

It is not yet possible to predict the manner and extent to which the UK's departure from the EU may affect the Issuer, however the Issuer remains committed to its European markets following the 'Brexit' vote and is now working on plans to maintain its ability to trade freely with, and provide services within, the European Union should the UK's access to the European Single Market, and the passporting rights under which the Issuer currently operates, be revoked.

The risk to Lloyd's of losing passporting rights to the European Single Market is that Lloyd's members will either write less business, or that business written at Lloyd's from the European Single Market will be more expensive as a result – which could ultimately reduce Lloyd's profitability and revenue. However, the uncertainty over European market access does not materially increase the risk of breaching the Issuer's Solvency Capital Requirements ("SCR") under Solvency II (as defined below) or its ability to repay or service its debt. While there can be no assurance that it will do so, Lloyd's is endeavouring to maintain competitive access to the European Single Market including by considering establishing a subsidiary model within the European Union.

### ***Any failure by the Issuer to comply with competition legislation could have a material adverse effect on its reputation and prospects***

The Issuer is subject to competition legislation and any failure to comply with this legislation could result in the imposition of fines or sanctions or a requirement to make significant changes to the Issuer's business model. The Issuer is required to comply with competition laws and regulations enforced by the Office of Fair Trading (OFT), the UK Competition and Markets Authority and the European Competition Commission. The competition laws and regulations applicable to the Issuer relate to matters such as price fixing, collusion and other forms of anti-competitive behaviour. The FCA also has amongst its objectives the promotion of competition in the UK.

A determination that the Issuer has failed to comply with any applicable laws and/or regulations relating to matters of competition or consumer protection, or any regulatory action in respect thereof could result in fines and losses as well as adverse publicity for the Issuer. This could have a material impact on the Issuer's reputation and its business, financial condition and future prospects.

### ***Capital Adequacy Requirements***

The Issuer and its members are required by the PRA to maintain a minimum level of assets in excess of their liabilities (referred to as regulatory capital) (see "*The Society of Lloyd's – Managing the Lloyd's market*"). The Issuer and its members satisfy all of their current regulatory requirements in this regard and as at 30 June 2016, the Issuer had a surplus over central SCR (as defined below) (i.e. surplus of central assets over liabilities calculated in accordance with Solvency II) of £1,772 million, and a surplus over MWSCR (as defined below) of £6,999 million. The Issuer and its members' future regulatory capital requirements depend on many factors, including their operational results, capital market developments, the volume of newly generated business and regulatory changes to capital requirements or other regulatory developments. The Issuer may also need to increase its capital as a result of market perceptions of adequate capitalisation levels and the perceptions of rating agencies.

Any inability on the part of the Issuer to meet its regulatory capital requirements in the future would be likely to lead to intervention by the PRA, which could be expected to require the Issuer to take steps to restore the

level of regulatory capital held to acceptable levels. Such capital may not be available on commercially favourable terms, or at all. Moreover, should the Issuer's capital fall close to regulatory minimum levels or the Issuer's own internal minimum levels, the Issuer may need to adjust its business practices to preserve its capital. If the Issuer is unable to maintain satisfactory capital adequacy ratios, its credit ratings may also be lowered which could materially adversely affect its business.

### ***Ongoing Solvency II Compliance***

A new solvency regime applicable to the EU insurance sector, known as “**Solvency II**”, has codified and harmonised prudential regulation for insurers and applied more consistent risk sensitive standards to insurers' capital requirements. Directive 2009/138/EC, as amended by Directive 2014/51/EU (the “**Solvency II Directive**”) took effect from January 2016 and covers areas such as regulatory capital, the valuation of assets and liabilities, calculating technical provisions and regulatory reporting.

Under Solvency II, insurers and reinsurers may make use of internal economic capital models (an “**internal model**”) when calculating their capital requirements, provided the prior approval of the relevant regulator has been obtained. The Issuer received formal full internal model approval from the PRA on 5 December 2015.

Changes to the internal model are subject to a robust governance and approval process. Changes that exceed a certain threshold are required to be submitted to the PRA for approval. Should the Issuer fail to maintain internal model approval or the PRA perceives the internal model to require adjustment, the capital requirements of the Issuer could increase, potentially substantially, and could have a material adverse effect on its reputation.

Regulators may continue to issue guidance and other interpretations of applicable requirements, which could require further adjustments by the Issuer to its internal model and/or capital requirements in the future. A failure by the Issuer to implement the measures required by Solvency II in a timely manner could also lead to regulatory action and have a material adverse effect on the Issuer's business, results of operations and financial condition.

There is also a risk that the Notes and any capital instruments issued by the Issuer will cease to qualify as regulatory capital for Solvency II purposes (see “*Factors which are material for the purpose of assessing the market risks associated with the Notes - Early redemption*” below). This could require the Issuer to raise additional capital in order to meet its regulatory capital requirements under Solvency II and failure to do so could have a significant impact on the Issuer's business, results of operations and financial condition.

### ***Central Fund***

The Issuer holds the Central Fund as mutualised assets available for the protection of Lloyd's policyholders and for complying with regulatory capital requirements.

Application of the Central Fund to protect policyholders by meeting the underwriting liabilities of members (including the funding of overseas trust funds where required) is at the discretion of the Council. In the event of a significant failure or failures on the part of members to meet their underwriting liabilities, it is possible that the level of assets in the Central Fund (and therefore the assets available to satisfy policyholder claims) would be substantially reduced and that the level of Lloyd's members' liabilities could exceed the resources available to them.

Equitas was established in 1995 as part of the Reconstruction and Renewal process described in “*The Society of Lloyd's – Reconstruction and Renewal and Equitas*”. Equitas is not owned by the Issuer and is independent of the Issuer in its management, operation and structure and it is separately regulated by the PRA. Nevertheless, in the event that Equitas is unable to meet its liabilities in full, this may result in certain Lloyd's members and/or the Issuer becoming financially exposed. In such circumstances the Issuer may decide or be required to apply the Central Fund to protect policyholders by covering any resulting financial exposure.

See “*The Society of Lloyd's – Reconstruction and Renewal and Equitas*” for further information.

***The Issuer and Lloyd's members are exposed to a range of investment risks including market and credit related risks***

**Market risk** is the risk that the value of financial instruments will fluctuate because of movements in interest rates, foreign currency and asset values; it also captures the risk of investment default and liquidity risk where, although solvent, the obligations of the Issuer or members cannot be met as they fall due.

These risks apply to the Issuer and Lloyd's members and are addressed individually below. As noted in "Central Fund" above, where members' liabilities exceed the assets available to meet them, the Central Fund could be substantially reduced.

The Issuer has substantial holdings of fixed income securities and equity securities in the Central Fund (see "The Society of Lloyd's – Resources within the Lloyd's market and the Protection of Policyholders"). Fluctuations in the value of such fixed income securities and equity securities, whether as a result of changes in interest rates, currency exchange rates or other factors such as the credit quality of the issuer of a fixed income security or the performance of the issuer of an equity security, will directly or indirectly affect the reported financial results and capital requirements of the business. A significant reduction in the market values of the Issuer's investments may also adversely affect the Issuer's regulatory solvency position.

The Issuer has an Investment Committee which is a committee of the Franchise Board responsible for setting the investment objectives and parameters of centrally managed assets. This committee also monitors the Issuer's investment operations in respect of funds under management and approves all investment counterparties.

Lloyd's members provide capital to support underwriting at Lloyd's, which is held in trust for the benefit of policyholders that are specific to that member only. Premiums received by syndicates are held in premium trust funds and are the first resource for paying policyholder claims. Both member capital and premium trust funds are subject to the asset rules set out in the PRA's Rulebook. Typically, member capital and premium trust funds are invested in money-market and short to medium dated fixed-interest securities of high credit quality. As a result, the value of these assets is also affected by fluctuations in interest rates and currency exchange rates, as well as other factors such as changes in the credit quality of those underlying issuers.

The Issuer has a Financial Risk Committee which is responsible for the oversight of investments and related risks generated by all market participants, including the Central Fund, member capital and premium trust funds. Oversight is supported through the implementation and monitoring of minimum standards for investment governance (for more information on these standards see "The Society of Lloyd's - Managing the Lloyd's market").

**Interest rate risk** is the risk that the value and future cash flows of a financial instrument will fluctuate because of changes in interest rates. Changes in prevailing capital market interest rates (including changes in the difference between the levels of prevailing short and long-term rates) may adversely affect the Issuer's results and the results of individual Lloyd's members. Movements in both short and long-term interest rates may affect the level and timing of recognition of gains and losses on the debt securities held in the Issuer's investment portfolio or in premium trust funds. An increase in interest rates could substantially decrease the value of the Issuer's fixed-income portfolio and adversely affect the Issuer's investment income and could have a similar effect on premium trust funds. A prolonged decline in interest rates could also adversely affect the Issuer's interest income, or the income derived from premium trust funds, as existing instruments mature and are replaced by lower yielding debt securities. In addition, where corporate bonds are held in an investment portfolio, a credit spread widening, in particular as a result of a credit downgrade, will decrease the market value of the corporate bonds.

**Exchange rate risk** is the risk of fluctuations in the value of assets and the investment income deriving from them due to changes in foreign exchange rates.

The Issuer actively hedges its exposure to changes in foreign exchange rates, but there can be no assurance that such hedging will be effective in protecting the Issuer from such risk.

Managing agents must also identify the main currencies in which each syndicate transacts its business and holds assets in each of those currencies to match the relevant liabilities. The Issuer also reviews the matching of assets to liabilities at the syndicate level as well as at the market level. Members also deposit capital to broadly match their exposures by currency. However, asset and liability matching is an imperfect tool and may not be effective in all circumstances. At 31 December 2015 and at 30 June 2016, more than half of all capital deployed at Lloyd's was provided in U.S. dollars.

**Liquidity risk** is the risk that the Issuer or its members, though solvent, either do not have sufficient financial resources available to enable them to meet their obligations as they fall due, or can secure them only at excessive cost.

The value and term of short term assets are carefully monitored against the Issuer's liabilities in order to ascertain its likely cash requirements at any given time. The Issuer utilises a liquidity risk framework which includes, by reference to its liabilities plus an additional buffer amount, a minimum requirement for high quality liquid assets. As at the date of this Prospectus, liquidity risk is within the Issuer's risk appetite. In addition, the Issuer maintains committed bank facilities to accommodate unforeseen cash requirements.

However, even a perception among investors that a financial institution is experiencing greater liquidity risk can cause significant damage to the institution. The Issuer's ability to sell assets at a commercially desirable price or at all may be impaired if other investors are seeking to sell similar assets at the same time or are not in a position to finance themselves, or when the market value of assets is difficult to ascertain, as occurred at certain times during and since the global financial crisis.

The availability to the Issuer of any additional financing it may need will depend on a variety of factors, such as market conditions, the availability of credit generally, the Issuer's financial condition, its credit ratings and credit capacity, as well as the possibility that lenders could develop a negative perception of the Issuer's financial prospects if, for example, the Issuer or the Lloyd's market incurs large losses, experiences a significant loss of members or if the level of insurance activity decreases materially due to a market downturn or other economic shock. In particular, the Issuer's access to funds may be impaired if regulatory authorities or rating agencies impose additional regulatory capital requirements or downgrade the Issuer's credit ratings. The Issuer's internal sources of liquidity may prove to be insufficient and, in such case, the Issuer may not be able to successfully obtain additional financing on favourable terms or at all. Any of these developments may limit the Issuer's ability to raise additional capital to support business growth or to counterbalance the consequence of losses or increased regulatory capital requirements, and could have a material adverse effect on the Issuer's business, financial condition, results of operations, liquidity and prospects.

Liquidity risk also arises where a syndicate has insufficient funds to meet its liabilities, particularly claims. Managing agents are required to manage the cash needs of their syndicates on an ongoing basis and to avoid becoming forced sellers of assets. They are required to match the duration of their syndicates' investments with the liabilities to policyholders. Generally syndicates have a high concentration of liquid assets, namely cash and government securities. Managing agents can request that members of syndicates make funds available to enable them to meet their underwriting liabilities. Members meet these cash call requests from their own resources or from their funds at Lloyd's or, at the Council's discretion, the Central Fund (see "*The Society of Lloyd's – Managing Agents*" and "*The Society of Lloyd's - Resources within the Lloyd's market and the Protection of Policyholders*").

The Issuer centrally monitors syndicate liquidity both in terms of asset mix and future funding needs and conducts stress tests to monitor the impact on liquidity of significant claims events. However, no assurance is provided that these measures will be effective in all circumstances.

**Credit risk** is the risk of exposure to loss if another party fails to perform its financial obligations to the Issuer, particularly where proceeds from its investments are not available as expected.

As at 30 June 2016, the Issuer's cash and cash equivalent with banks amounted to £289 million. Although the Issuer has risk management controls in place which are designed to ensure that its counterparties are credit worthy and its assets are appropriately diversified, these controls may not always prove to be effective in

practice. As a result, the Issuer could experience losses, which could be significant, in the event of a default by one or more of its counterparties on their obligations due to bankruptcy, lack of liquidity, downturns in the economy, operational failure or other reasons, or even in the event of rumours about potential defaults by one or more of these counterparties or regarding the financial services industry. These losses could include actual losses from defaults, market value losses due to credit deterioration or other reasons and impairment losses.

The Issuer centrally monitors the quality of syndicate assets. However, no assurance is provided that these measures will be effective in all circumstances and Lloyd's members have in the past and are expected in the future to continue to experience losses as a result of credit deterioration, impairment or default from their financial investment counterparties.

***The Issuer's internal controls may not be sufficient in certain circumstances to adequately monitor the size and type of operations carried out by the Issuer***

Operational risk and losses can result from fraud, errors by employees, failure to document transactions properly or to obtain proper internal authorisation, failure to comply with regulatory requirements and conduct of business rules, systems and equipment failures, natural disasters or the failure of external systems (for example, those of the Issuer's counterparties or vendors). Key risks include the potential for major operational disruption to impact the Issuer, damage to the Lloyd's building, risks associated with human resources, information systems, supplier management and the provision of adequate processing functions to the Lloyd's market. The Issuer has implemented risk controls and loss mitigation strategies, and substantial resources are devoted to developing efficient procedures and to staff training, but it is not possible to eliminate entirely each of the potential operational risks the Issuer faces. Losses from the failure of the Issuer's system of internal controls could have a material adverse effect on its business, financial condition, results of operations and prospects and could materially adversely affect its reputation.

***The failure of any of the Issuer's or Lloyd's market's key outsource providers could lead to significant business disruption for the Lloyd's market and lead to the market being unable to maintain operations and services to policyholders***

Managing agents outsource the majority of premium and claims processing services to Xchanging Ins-sure Services ("XIS"). The Issuer also has contracts with XIS in relation to the provision of information to support the Issuer's tax and regulatory processes. A sustained failure of XIS or major disruption of those services, for example as a result of an outage of key IT systems, could lead to significant business disruption for the Lloyd's market (for example, managing agents' ability to submit and process premiums and claims) and lead to the market being unable to maintain operations and services to policyholders.

***The Lloyd's market faces strong competition which could adversely impact its profitability***

In line with other participants in the global insurance industry, the Lloyd's market faces strong competition in all of its main areas of business. Its continuing profitability depends upon an adequate response to such competition. The Lloyd's market's ability to generate an appropriate return depends upon its capacity to anticipate and respond appropriately to these competitive pressures, and a failure to do so may have a material adverse effect on the market's business, results of operations and financial condition.

***Lloyd's market acquisition expense ratio has been increasing in recent years***

The Lloyd's market's acquisition expense ratio (being the ratio of net acquisition costs to net earned premium) has increased in recent years as brokers consolidate and offer more services. Lloyd's market business mix is also changing as it writes more direct business rather than reinsurance and more of the direct business is sourced through delegated authority arrangements, which have a higher acquisition expense ratio. If this trend in increasing costs of acquiring business persists without counter-acting measures, it could pose a threat to the long-term profitability of the Lloyd's market.

***International tax legislation is becoming increasingly complex, raising the risk of breaching applicable regimes***

Following the OECD review of international tax rules, the UK has introduced legislation requiring the disclosure of profit and taxes paid on a country by country basis. In addition, increasing complexity, public scrutiny and Lloyd's focus on international market access and licence development will increase the potential for this risk to crystallise.

***The Lloyd's market is exposed to unstable economic, financial and political developments***

Like other general insurers, the Lloyd's market is affected by changes in the economic, financial and political climate. For example, the Lloyd's market is exposed to a general economic downturn in its major markets which could result in an increase in reported claims, policy lapses and policy withdrawals. In addition, in times of adverse economic conditions, the Lloyd's market is exposed to an increase in fraudulent claims by customers, all of which could increase claims costs and reduce premium income. This could cause the Lloyd's market's results to deteriorate and could affect the Issuer's financial condition and ability to meet its solvency requirements in the event that the Issuer applies the Central Fund to meet members' underwriting liabilities.

Growth and expansion into developing markets are a core part of the Issuer's strategy, see "*The Society of Lloyd's – Managing the Lloyd's market*". In addition to continuing to access cross-border reinsurance from London, the Issuer is considering how it may increase the Lloyd's market's share of insurance business in developing markets. However, political and economic instability is increasing across some of the Issuer's target developing economies and this may pose a threat to the Issuer's market access as it looks for alternative areas for market growth.

***The Issuer may not be successful in pursuing its strategy***

The Issuer has developed Vision 2025, which sets out the strategic direction for the Lloyd's market in the context of long-term industry trends and the challenges which the Lloyd's market faces in the current global economy. The Issuer's strategic plan identifies the steps that are being taken to deliver Vision 2025 and identifies eight major priorities which are market oversight, global market access, ease of doing business, capital, innovation, brand, global corporate social responsibility and talent. However, in pursuing this strategy the Issuer faces risks arising from changes in evolving market conditions, particularly distribution and non-traditional capital. In relation to the former, to access the widest range of potential business, the breadth of distribution options available to the Lloyd's market needs to increase through growth in all existing channels (brokers; coverholders; service companies and Lloyd's local underwriting offices) as well as managing agents giving consideration to new options (such as joint ventures with local reinsurers). In relation to the latter, the growth of non-traditional products and capital and continued concentration in the broker market are now established features of the reinsurance industry and the Lloyd's market will need to understand the risks and opportunities this represents and react appropriately. The Issuer's business model could be impacted if it fails to respond to these changing market conditions, in particular business being transacted differently or not reaching the Lloyd's market.

The Lloyd's market continues to make significant progress towards Vision 2025. On modernisation, the Target Operating Model ("**TOM**") has progressed and the market continues to embrace new technology. The global market access and licence network continues to expand thanks to the approval of new licences and the opening of new offices.

***Changes in the Issuer's insurer financial strength credit ratings may adversely affect Lloyd's members***

Credit ratings are an important factor in the Issuer's competitive position. Rating organisations assign ratings based upon a variety of factors according to published criteria, while most of the factors relate to the rated entity including the level of capital, diversity of insurance risk and mix of insurance assets, some of the factors relate to general economic conditions and other circumstances outside the rated entity's control.

Currently, the Issuer's insurer financial strength ratings are A+ (Strong) with a stable outlook from Standard & Poor's, AA- (Very Strong) with a stable outlook from Fitch and A (Excellent) with a stable outlook from A.M. Best (see "*The Society of Lloyd's*"). These ratings reflect the current opinions of the rating agencies and remain subject to change. There can be no assurance that the Issuer will be able to maintain its current credit ratings.

A downgrade of any of the Issuer's insurer financial strength ratings could lead brokers to stop recommending the Lloyd's market to their clients and lead to the loss of other customers whose confidence in the Issuer may be affected or whose policies require insurance with a certain minimum rating.

A downgrade could also impact the terms and availability of the Issuer's financing and access to the debt capital markets.

A downgrade of any of the Issuer's financial strength credit ratings, and the related consequences described above, could have a material adverse effect on the Issuer's business, prospects, financial condition and results of operations.

***Loss of business reputation or negative publicity could negatively impact the Issuer's business and results of operations***

The Issuer's success is dependent on the strength and reputation of the Issuer and its brand. The Issuer is vulnerable to adverse market perception because it operates in an industry where integrity and customer trust and confidence are paramount. The Issuer is exposed to the risk that litigation, employee misconduct, operational failures, regulatory or other investigations or actions, press speculation and negative publicity, whether or not well founded, could damage its brand or reputation. The Issuer's reputation may also be adversely affected by negative publicity associated with those that it insures and by the actions of members of the Lloyd's market.

Any damage to the Issuer's brand or reputation could cause existing customers, partners or intermediaries to withdraw their business from the Issuer or the Lloyd's market and potential customers, partners or intermediaries to elect not to do business with the Issuer or the Lloyd's market and could also make it more difficult for the Issuer to attract and retain qualified employees. Such damage to the Issuer's brand or reputation could cause disproportionate damage to the Issuer's business, even if the negative publicity is factually inaccurate or unfounded.

***Changes in taxation law may adversely impact the Issuer***

UK and overseas taxation law includes rules governing company taxes, business taxes, personal taxes, capital taxes, value added taxes and other indirect taxes. The Issuer's management cannot predict accurately the impact of future changes in UK and overseas tax law on its business. From time to time, changes in the interpretation of existing UK and overseas tax laws, amendments to existing tax rates, changes in the practice of tax authorities, or the introduction of new tax legislation in the UK or overseas may adversely impact the Group's business, results, financial condition and prospects.

The UK Government has concluded its consultations on the Tax Deductibility of Corporate Interest Expense. Draft legislation was published on 5 December 2016. Based on the draft legislation it is not currently expected that this reform will materially impact the ability of the Issuer to claim tax deductions for all or part of its interest expenses. However, the draft legislation that has been published is incomplete (further detail is expected at the end of January 2017) and is subject to change prior to enactment. The potential impact of these reforms on the Issuer therefore remains uncertain. See also "*Optional early redemption*" below.

## **Factors which are material for the purpose of assessing the market risks associated with the Notes**

### ***Risks related to the structure of the Notes***

#### *The Issuer's obligations under the Notes are subordinated*

The Issuer's obligations under the Notes will constitute direct, unsecured and subordinated obligations of the Issuer and rank *pari passu* and without any preference among themselves. In the event of a winding-up of the Issuer the payment obligations of the Issuer under the Notes will be subordinated to the claims of all Senior Creditors of the Issuer but will rank at least *pari passu* with all other subordinated obligations of the Issuer which constitute, or would but for any applicable limitation on the amount of such capital constitute, Tier 2 Capital and will rank in priority to the claims of holders of all obligations of the Issuer which constitute, or would but for any applicable limitation on the amount of such capital constitute, Tier 1 Capital and the distribution of any central assets to members of Lloyd's generally.

Although the Notes may pay a higher rate of interest than comparable notes which are not subordinated, there is a significant risk that an investor in the Notes will lose all or some of its investment should the Issuer become insolvent.

Holders of the Notes are advised that unsubordinated liabilities of the Issuer may also arise out of events that are not reflected on the balance sheet of the Issuer including, without limitation, the issuance of guarantees on an unsubordinated basis. Claims made under such guarantees will become unsubordinated liabilities of the Issuer that in a winding-up of the Issuer will need to be paid in full before the obligations under the Notes may be satisfied.

#### *Payments by the Issuer are conditional upon satisfaction of solvency requirements*

Other than in the circumstances set out in Condition 3.2(b) and without prejudice to Condition 10.1(b), all payments by the Issuer under or arising from the Notes and the Trust Deed shall be conditional upon the Issuer being Solvent at the time for payment by the Issuer, and no amount shall be payable under or arising from the Notes and the Trust Deed unless and until such time as the Issuer could make such payment and still be Solvent immediately thereafter. For these purposes, the Issuer will be Solvent if (i) it is able to pay its debts owed to Senior Creditors and *Pari Passu* Creditors of the Issuer as they fall due and (ii) its Assets exceed its Liabilities (other than Liabilities to persons who are not Senior Creditors). If any payment of interest, Arrears of Interest and/or principal cannot be made by the Issuer in compliance with Condition 3.2(a), payment of such amounts will be deferred, and such deferral will not constitute a default under the Notes for any purpose.

#### *Interest payments under the Notes may be deferred at the option of the Issuer and must be deferred under certain circumstances*

The Issuer may elect to defer payments of interest on the Notes pursuant to Condition 5.1 for any reason on any Optional Interest Payment Date.

In addition, payment of interest on the Notes by the Issuer will be mandatorily deferred on any Mandatory Interest Deferral Date, being an Interest Payment Date in respect of which a Regulatory Deficiency Interest Deferral Event has occurred and is continuing or would occur if payment of interest was made on such Interest Payment Date. In addition, the Issuer is required to defer any payment of interest on the Notes in the event that it cannot make such payment in compliance with Condition 3.2(a). A Regulatory Deficiency Interest Deferral Event means any event (including, without limitation, any event which causes the Solvency Capital Requirement or the Minimum Capital Requirement to be breached and such breach is an event) which under the Relevant Rules would require the Issuer to defer payment of interest in respect of the Notes, and Solvency Capital Requirement includes the Solvency Capital Requirement referred to in, or any other capital requirement howsoever described in, the Relevant Rules in relation to either (i) the Lloyd's market as a whole (but not individual syndicates or members) or (ii) to the Central Assets of the Issuer.

The deferral of interest as described above does not constitute a default under the Notes for any purpose. Any interest so deferred shall, for so long as the same remains unpaid, constitute Arrears of Interest. Arrears of

Interest do not themselves bear interest. Arrears of Interest may, subject to certain conditions, be paid by the Issuer at any time upon notice to Noteholders, but in any event shall be payable, subject, in the case of (a) and (c) below, to Condition 3.2(a) and satisfaction of the Regulatory Clearance Condition, on the earliest to occur of (a) the next Interest Payment Date which is not a Mandatory Interest Deferral Date and on which a scheduled payment of interest in respect of the Notes is made or is required to be made (other than a voluntary payment by the Issuer of any Arrears of Interest), (b) the date on which a winding-up of the Issuer occurs or (c) any redemption or purchase of the Notes pursuant to Condition 7 (subject to any deferral of such redemption date pursuant to Condition 7.3) or Condition 10.

Any actual or anticipated deferral of interest payments will likely have an adverse effect on the market price of the Notes. In addition, as a result of the interest deferral provision of the Notes, the market price of the Notes may be more volatile than the market prices of other debt securities on which interest accrues that are not subject to such deferral and may be more sensitive generally to adverse changes in the Issuer's financial condition.

*Redemption payments under the Notes must be deferred, under certain circumstances*

Notwithstanding the expected maturity of the Notes on the Maturity Date, the Issuer must defer redemption of the Notes on the Maturity Date or on any other date set for redemption of the Notes pursuant to Conditions 7.2, 7.5 and 7.6 (i) in the event that it cannot make the redemption payments in compliance with Condition 3.2(a) or (ii) if a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing or would occur if the Notes were redeemed by the Issuer on such date or (iii) in the event that it cannot make the redemption payments in compliance with the Regulatory Clearance Condition.

The deferral of redemption of the Notes does not constitute a default under the Notes for any purpose. Where redemption of the Notes is deferred, subject to certain conditions, the Notes will be redeemed by the Issuer on the earliest of (A)(i) the date falling 10 Business Days following the day that the Issuer is Solvent and the redemption of the Notes will not result in the Issuer ceasing to be Solvent, or (ii) the date falling 10 Business Days (x) following cessation of the Regulatory Deficiency Redemption Deferral Event, or (y) after the Relevant Regulator has agreed to the repayment or redemption of the Notes or (iii) the date falling 10 Business Days following the day on which the Regulatory Clearance Condition is satisfied and (B) the date on which a winding-up of the Issuer occurs.

Any actual or anticipated deferral of redemption of the Notes will likely have an adverse effect on the market price of the Notes. In addition, as a result of the redemption deferral provision of the Notes, including with respect to deferring redemption on the scheduled Maturity Date, the market price of the Notes may be more volatile than the market prices of other debt securities without such deferral feature, including dated securities where redemption on the scheduled maturity date cannot be deferred, and the Notes may accordingly be more sensitive generally to adverse changes in the Issuer's financial condition.

*Optional early redemption*

The Notes may, subject as provided in Condition 7 (including the Relevant Regulator's approval or prior consent), at the option of the Issuer, be redeemed at their principal amount, together with any Arrears of Interest and any other accrued but unpaid interest to (but excluding) the date of redemption, before the Maturity Date (i) on the First Call Date or any Floating Interest Payment Date thereafter, (ii) in the event of certain circumstances affecting the tax treatment of the Notes or payments thereunder or (iii) following the occurrence of (or if the Issuer satisfies the Trustee that there will occur within six months) a Capital Disqualification Event or a Ratings Methodology Event; provided that, in the case of any redemption prior to the fifth anniversary of the Issue Date, the Relevant Rules are complied with and the Notes are exchanged for, or redeemed out of the proceeds of a new issue of, capital of the same or higher quality.

An investor may not be able to reinvest the redemption proceeds at an effective interest rate as high as the interest rate on the Notes being redeemed and may only be able to do so at a significantly lower rate. Potential investors should consider reinvestment risk in light of other investments available at that time.

As discussed in the risk factor entitled “*Changes in taxation law may adversely impact the Issuer*”, the UK rules relating to the tax deductibility of interest expense are being reformed with effect from 1 April 2017. Although it is not currently expected that this reform will materially impact the ability of the Issuer to claim deductions for all or part of its interest expenses, the potential impact of this reform remains uncertain as the draft legislation that has been published is incomplete and is subject to change prior to enactment. If these rules, once implemented, were to restrict the Issuer’s ability to claim deductions for its interest expenses in respect of the Notes, this may in certain circumstances entitle the Issuer to redeem the Notes before their Maturity Date, subject to the conditions set out in Condition 7.

#### *Variation or substitution of the Notes without Noteholder consent*

Subject as provided in Condition 7, the Issuer may, at its option and without the consent or approval of the Noteholders, elect to substitute the Notes for, or vary the terms of the Notes so that they become or remain, Qualifying Tier 2 Securities or Rating Agency Compliant Securities (as the case may be) at any time in the event of certain circumstances affecting the tax treatment of the Notes or payments thereunder due to a change in applicable law or regulation or the official interpretation thereof, or following the occurrence of (or if the Issuer satisfies the Trustee that there will occur within six months) a Capital Disqualification Event or a Ratings Methodology Event.

#### *Restricted remedy for non-payment when due*

The sole remedy against the Issuer available to the Trustee or (where the Trustee has failed to proceed against the Issuer as provided in the Conditions) any Noteholder for recovery of amounts which have become due in respect of the Notes will be the institution of proceedings for the winding-up in England (but not elsewhere) of the Issuer and/or proving in any winding-up of the Issuer.

#### *Modification and waivers*

The Conditions contain provisions for calling meetings of Noteholders to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Noteholders including Noteholders who did not attend and vote at the relevant meeting and Noteholders who voted in a manner contrary to the majority. The Conditions also provide that the Trustee may, without the consent of Noteholders, agree to any modification of, or to the waiver or authorisation of any breach or proposed breach of, any of the Conditions or any of the provisions of the Trust Deed in the circumstances described in Condition 13.2.

#### *No limitation on issuing senior or pari passu securities*

There is no restriction on the amount of securities which the Issuer may issue, which securities rank senior to, or *pari passu* with, the Notes. The issue of any such securities may reduce the amount recoverable by Noteholders on a winding-up of the Issuer and/or may increase the likelihood of a deferral of interest and/or redemption payments under the Notes. Accordingly, in the winding-up of the Issuer and after payment of the claims of their respective senior ranking creditors, there may not be a sufficient amount to satisfy the amounts owing to the Noteholders.

#### *Change of law*

The Conditions are based on English law in effect as at the date of issue of the Notes. No assurance can be given as to the impact of any possible judicial decision or change to English law or administrative practice after the date of issue of the Notes.

#### ***Risks related to the market generally***

##### *Absence of public markets for the Notes*

The Notes constitute a new issue of securities by the Issuer. Prior to this issue, there will have been no public market for the Notes. Although application has been made for the Notes to be admitted to the Official List and to trading on the Market, there can be no assurance that an active public market for the Notes will develop and, if such a market were to develop, the Joint Lead Managers are under no obligation to maintain such a market. The liquidity and the market prices for the Notes can be expected to vary with changes in market and

economic conditions, the financial condition and prospects of the Issuer and other factors that generally influence the market prices of securities.

*Exchange rate risks and exchange controls*

Payments of principal and interest on the Notes will be made in sterling. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the "**Investor's Currency**") other than sterling. These include the risk that exchange rates may significantly change (including changes due to devaluation of sterling or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to sterling would decrease (1) the Investor's Currency equivalent yield on the Notes, (2) the Investor's Currency equivalent value of the principal payable on the Notes and (3) the Investor's Currency equivalent market value of the Notes. Government and monetary authorities may impose (as some have done in the past) exchange controls that could adversely affect an applicable exchange rate. As a result, investors may receive less interest or principal than expected, or no interest or principal.

*Interest rate risks*

The Notes bear interest at a fixed rate until the First Call Date. An investment in the Notes involves the risk that subsequent changes in market interest rates until the First Call Date may adversely affect the value of the Notes.

*Credit ratings may not reflect all risks*

The credit ratings assigned to the Notes may not reflect the potential impact of all risks related to structure, market, additional factors discussed above, and other factors that may affect the value of the Notes. In addition, credit rating methodologies for rating subordinated debt, in particular, may change in the future. Any such change in methodology may lead to a reduction in the rating assigned to the Notes or an increase in the rating assigned to unsubordinated debt instruments by comparison. A credit rating is not a recommendation to buy, sell or hold securities and may be revised or withdrawn by the rating agency at any time.

*Legal investment considerations may restrict certain investments*

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (1) the Notes are legal investments for it, (2) the Notes can be used as collateral for various types of borrowing and (3) other restrictions apply to its purchase or pledge of the Notes. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of the Notes under any applicable risk-based capital or similar rules.

*Investors must rely on the procedures of Euroclear and Clearstream, Luxembourg for transfer, payment and communication with the Issuer*

The Notes will be represented by the Global Certificate upon issue. The Global Certificate will be registered in the name of a nominee for the Common Depository for Euroclear and Clearstream, Luxembourg. Except in the circumstances described in the Global Certificate, investors will not be entitled to receive definitive Notes. Euroclear and Clearstream, Luxembourg will maintain records of the beneficial interests in the Global Certificate. While the Notes are represented by the Global Certificate, investors will be able to trade their beneficial interests only through Euroclear or Clearstream, Luxembourg and will receive and provide any notices only through Euroclear or Clearstream, Luxembourg.

While the Notes are represented by the Global Certificate, the Issuer will discharge its payment obligations under the Notes by making payments to or to the order of the registered holder as nominee for the Common Depository for Euroclear or Clearstream, Luxembourg for distribution to their accountholders. A holder of a beneficial interest in the Global Certificate must rely on the procedures of Euroclear and Clearstream, Luxembourg to receive payments under the Notes. The Issuer has no responsibility or liability for the records relating to, or payments made in respect of, beneficial interests in the Global Certificate.

***Investors who hold less than £100,000 in principal amount of Notes may be unable to sell their Notes and may be adversely affected if definitive Notes are subsequently required to be issued.***

The Notes are issued in registered form for minimum amounts of £100,000 and higher integral multiples of £1,000. Accordingly, it is possible that Notes may be traded in amounts in excess of £100,000 that are not integral multiples of £100,000. In such a case a holder who, as a result of trading such amounts, holds an amount which is less than £100,000 in his account with the relevant clearing system would not be able to sell the remainder of such holding without first purchasing a principal amount of Notes at or in excess of £100,000. Further, a holder who, as a result of trading such amounts, holds an amount which is less than £100,000 in his account with the relevant clearing system at the relevant time may not receive a definitive Certificate in respect of such holding (should definitive Certificates be issued) and would need to purchase a principal amount of Notes at or in excess of £100,000 in order to receive a definitive Certificate.

## DOCUMENTS INCORPORATED BY REFERENCE

References are made below to the Society's pro forma financial statements (the "**Pro Forma Financial Statements**" or "**PFFS**"). The Pro Forma Financial Statements provide financial information in relation to the Lloyd's market (also taking account of the Society's own assets). Investors should have regard to the Society's audited accounts for information on the Society's own financial position. The Pro Forma Financial Statements, the Society's 2014 and 2015 financial statements and the Society's financial statements for the six month period ending 30 June 2016 and the interim management statement of the Issuer's group for the nine months ended 30 September 2016 are available on [www.lloyds.com](http://www.lloyds.com) and incorporated by reference herein.

This Prospectus should be read and construed in conjunction with:

- (a) the annual financial statements of the Issuer's group for the financial year ended 31 December 2014 audited by PricewaterhouseCoopers LLP, together with the audit report thereon (which appear at pages 122 to 171 (inclusive) of the Issuer's Annual Report 2014);
- (b) the annual financial statements of the Issuer's group for the financial year ended 31 December 2015 audited by PricewaterhouseCoopers LLP, together with the audit report thereon (which appear at pages 138 to 189 (inclusive) of the Issuer's Annual Report 2015);
- (c) the pro forma financial statements of the Lloyd's market for the financial year ended 31 December 2014, together with the report of PricewaterhouseCoopers LLP thereon carried out in accordance with the International Standard on Assurance Engagements, ISAE 3000 (which appear at pages 57 to 69 (inclusive) of the Issuer's Annual Report 2014);
- (d) the pro forma financial statements of the Lloyd's market for the financial year ended 31 December 2015, together with the report of PricewaterhouseCoopers LLP thereon carried out in accordance with the International Standard on Assurance Engagements, ISAE 3000 (Revised) (which appear at pages 62 to 89 (inclusive) of the Issuer's Annual Report 2015);
- (e) the interim financial statements of the Issuer's group for the six months ended 30 June 2016 (which appear at pages 23 to 49 (inclusive) of the Issuer's interim report for the six months ended 30 June 2016);
- (f) the pro forma financial statements of the Lloyd's market for the six months ended 30 June 2016 (which appear at pages 8 to 18 (inclusive) of the Issuer's interim report for the six months ended 30 June 2016); and
- (g) the interim management statement of the Issuer's group for the nine months ended 30 September 2016,

which have been previously published or are published simultaneously with this Prospectus and which have been approved by the FCA or filed with it. Such documents shall be incorporated in, and form part of, this Prospectus, save that any statement contained in a document which is incorporated by reference herein shall be modified or superseded for the purpose of this Prospectus to the extent that a statement contained herein modifies or supersedes such earlier statement (whether expressly, by implication or otherwise). Any statement so modified or superseded shall not, except as so modified or superseded, constitute a part of this Prospectus. Those parts of the documents incorporated by reference in this Prospectus which are not specifically incorporated by reference in this Prospectus are either not relevant for prospective investors in the Notes or the relevant information is included elsewhere in this Prospectus. Any documents themselves incorporated by reference in the documents incorporated by reference in this Prospectus shall not form part of this Prospectus.

Copies of documents incorporated by reference in this Prospectus (including the PFFS) may be obtained (without charge) from the website of the Regulatory News Service operated by the London Stock Exchange at: <http://www.londonstockexchange.com/exchange/prices-and-news/news/market-news/market-news-home.html> and the website of the Issuer <http://www.lloyds.com/lloyds/investor-relations/financial-performance/financial-results>.

## TERMS AND CONDITIONS OF THE NOTES

*The following is the text (save for paragraphs in italics) of the Terms and Conditions of the Notes which (subject to modification and except for the paragraphs in italics) will be endorsed on the Certificates issued in respect of the Notes:*

The issue of the £300,000,000 Fixed to Floating Rate Callable Subordinated Notes due 2047 (the “**Notes**”, which expression shall in these Conditions, unless the context otherwise requires, include any further notes issued pursuant to Condition 15 and forming a single series with the Notes) of the Society of Lloyd’s (the “**Issuer**”) was authorised by a resolution of the Council of Lloyd’s passed on 7 December 2016. The Notes are constituted by a Trust Deed dated 7 February 2017 (the “**Trust Deed**”) made between the Issuer and Citicorp Trustee Company Limited (the “**Trustee**”, which expression shall include its successor(s)) as trustee for the holders of the Notes.

The statements in these Conditions include summaries of, and are subject to, the detailed provisions of and definitions in the Trust Deed. Copies of the Trust Deed and the Agency Agreement dated 7 February 2017 (the “**Agency Agreement**”) made between the Issuer, Citigroup Global Markets Deutschland AG (the “**Registrar**”, which expression shall include its successor(s)) as registrar, Citibank, N.A., London Branch (the “**Principal Paying Agent**”, which expression shall include its successor(s)) as principal paying agent and agent bank), the other Agents, Citibank, N.A., London Branch (the “**Transfer Agent**”, which expression shall include its successor(s)) as transfer agent and the Trustee are available for inspection during normal business hours by the Noteholders at the principal office for the time being of the Trustee (being, as at the Issue Date, at Citigroup Centre, Canada Square, Canary Wharf, London E14 5LB) and at the specified office of each of the Agents. The Noteholders are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Trust Deed and the Agency Agreement applicable to them.

*The owners shown in the records of each of Euroclear Bank SA/NV and Clearstream Banking S.A. of book-entry interests in Notes are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Trust Deed and the Agency Agreement applicable to them.*

### 1 Form, Denomination and Title

#### 1.1 Form and Denomination

The Notes are issued in registered form in amounts of £100,000 and higher integral multiples of £1,000 (referred to as the “**principal amount**” of a Note, and references in these Conditions to “**principal**” in relation to a Note shall be construed accordingly). A note certificate (each a “**Certificate**”) will be issued to each Noteholder in respect of its registered holding of Notes. Each Certificate will be numbered serially with an identifying number which will be recorded on the relevant Certificate and in the register of Noteholders which the Issuer will procure to be kept by the Registrar (the “**Register**”).

#### 1.2 Title

Title to the Notes passes only by registration in the Register. The holder of any Note will (except as otherwise required by law) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest in it or any writing on, or the theft or loss of, the Certificate issued in respect of it) and no person will be liable for so treating the holder. In these Conditions, “**Noteholder**” and (in relation to a Note) “**holder**” means the person in whose name a Note is registered in the Register.

## **2 Transfers of Notes and Issue of Certificates**

### **2.1 Transfers**

A Note may be transferred by depositing the Certificate issued in respect of that Note, with the form of transfer on the back duly completed and signed, at the specified office of the Registrar or the Transfer Agent.

### **2.2 Delivery of new Certificates**

Each new Certificate to be issued upon a transfer of Notes will, within five Business Days of receipt by the Registrar or the relevant Agent of the duly completed form of transfer endorsed on the relevant Certificate, be mailed by uninsured mail at the risk of the holder entitled to the Note to the address specified in the form of transfer.

*Except in the limited circumstances described in this Prospectus (see “The Global Certificate—Transfers and Exchange”), owners of interests in the Notes will not be entitled to receive physical delivery of Certificates.*

Where some but not all of the Notes in respect of which a Certificate is issued are to be transferred, a new Certificate in respect of the balance of Notes not so transferred will, within five Business Days of receipt by the Registrar or the relevant Agent of the original Certificate, be mailed by uninsured mail at the risk of the holder of the Notes not so transferred to the address of such holder appearing on the Register or as specified in the form of transfer.

### **2.3 Formalities free of charge**

Registration of transfer of any Notes will be effected without charge by or on behalf of the Issuer or any Agent but upon payment (or the giving of such indemnity as the Issuer or any Agent may reasonably require) in respect of any tax or other governmental charges which may be imposed in relation to such transfer.

### **2.4 Closed periods**

No Noteholder may require the transfer of a Note to be registered during the period of 15 days ending on the due date for any payment of principal, interest or Arrears of Interest on that Note.

### **2.5 Regulations**

All transfers of Notes and entries on the Register will be made subject to the detailed regulations concerning transfer of Notes scheduled to the Agency Agreement. The regulations may be changed by the Issuer with the prior written approval of the Registrar and the Trustee. A copy of the current regulations will be mailed (free of charge) by the Registrar to any Noteholder who requests one.

## **3 Status of the Notes**

### **3.1 Status**

The Notes constitute direct, unsecured and subordinated obligations of the Issuer and shall at all times rank *pari passu* and without any preference among themselves. The rights and claims of the Noteholders are subordinated as described in Condition 3.2.

### **3.2 Solvency and Subordination**

- (a) Other than in the circumstances set out in Condition 3.2(b) and without prejudice to Condition 10.1, payments of all amounts by the Issuer under or arising from the Notes and the Trust Deed (other than payments made to the Trustee acting on its own account under the Trust Deed) shall be mandatorily deferred unless the Issuer is Solvent at the time for payment by the Issuer and unless and until such time as the Issuer could make such payment and still be Solvent immediately thereafter.

A certificate as to solvency of the Issuer signed by two Authorised Signatories of the Issuer or, if there is a winding-up of the Issuer, by two authorised signatories of the liquidator of the Issuer shall be treated and accepted by the Issuer, the Trustee, the Noteholders and all other interested parties as correct and sufficient evidence thereof, shall be binding on all such persons and the Trustee shall be entitled to rely on such certificate without liability to any person.

- (b) The claims of the Noteholders will, in the event of the winding-up of the Issuer, rank junior to the claims of all Senior Creditors, in the manner provided in the Trust Deed and thus will rank:
- (i) junior to (A) any payment (other than an Excluded Payment) made for the purpose of extinguishing or reducing any liability of a member of Lloyd's arising out of or in connection with insurance business carried on at Lloyd's by that member of Lloyd's or (B) any payment made to a member of Lloyd's in its capacity as a Senior Creditor or (C) any other Senior Creditors;
  - (ii) at least *pari passu* with all claims of holders of all other subordinated obligations of the Issuer which constitute, and all claims relating to a guarantee or other like or similar undertaking or arrangement given or undertaken by the Issuer in respect of any obligations of any other person which constitute, or (in either case) would but for any applicable limitation on the amount of such capital constitute Tier 2 Capital (including, without limitation, by virtue of the operation of any applicable grandfathering provisions under the Relevant Rules, and as of the Issue Date includes the T2 Notes) and all obligations which rank, or are expressed to rank, *pari passu* therewith ("**Pari Passu Securities**"); and
  - (iii) in priority to (A) the claims of holders of all obligations of the Issuer which constitute, and all claims relating to a guarantee or other like or similar undertaking or arrangement given or undertaken by the Issuer in respect of any obligations of any other person which constitute, or (in either case) would but for any applicable limitation on the amount of such capital constitute Tier 1 Capital (including, without limitation, by virtue of the operation of any applicable grandfathering provisions under the Relevant Rules, and as of the Issue Date includes the T1 Notes) and all obligations which rank, or are expressed to rank, *pari passu* therewith, and the claims of holders of any other instruments or obligations of the Issuer which rank, or are expressed to rank, junior to the Notes (together, "**Junior Securities**"); and (B) the distribution of any Central Assets to members of Lloyd's generally.

*In the event of the winding-up of the Issuer, the amount in respect of a Note that a holder will receive will be less than the principal amount of such Note, together with any accrued and unpaid interest and any additional amounts payable pursuant to Condition 8, unless the Issuer has Assets remaining after payment of and/or provision for the claims of all Senior Creditors in full and such Assets are sufficient to pay and/or provide for any claims ranking pari passu with the claims of the Noteholders and the payments required to be made in respect of the Notes, in each case in full.*

Nothing in this Condition 3.2 shall affect or prejudice the payment of the fees, costs, charges, expenses, liabilities or remuneration of the Trustee or the rights and remedies of the Trustee in respect thereof.

### **3.3 Set-off**

Subject to applicable law, no Noteholder may exercise, claim or plead any right of set-off, counterclaim, compensation or retention in respect of any amount owed to it by the Issuer in respect of, or arising from, the Notes whether prior to or in a winding-up and each Noteholder and the Trustee, on behalf of each Noteholder, shall, by virtue of his holding of any Notes, be deemed to have waived all such rights of set-off, counterclaim, compensation or retention. Notwithstanding the preceding sentence, if any of the amounts owing to any Noteholder by the Issuer in respect of, or arising from,

the Notes is discharged by set-off, counterclaim, compensation or retention, such set-off, counterclaim, compensation or retention will be deemed not to have taken place and such Noteholder shall, subject to applicable law, immediately pay an amount equal to the amount of such discharge to the Issuer (or, if appropriate, the liquidator in the Issuer's winding-up).

## **4 Interest**

### **4.1 Interest Rate**

Each Note bears interest on its principal amount at the applicable Interest Rate from (and including) the Issue Date in accordance with provisions of this Condition 4.

Subject to Conditions 3.2(a) and 5, interest shall be payable on the Notes:

- (a) annually in arrear on each Fixed Interest Payment Date up to (and including) the First Call Date; and
- (b) after the First Call Date, quarterly in arrear on each Floating Interest Payment Date.

### **4.2 Interest Accrual**

Interest shall cease to accrue on each Note on the due date for redemption (which due date shall, in the case of deferral of a redemption date in accordance with Condition 7.3, be the latest date to which redemption of the Notes is so deferred) unless payment is improperly withheld or refused, in which event interest shall continue to accrue (in each case, both before and after judgment) as provided in the Trust Deed.

### **4.3 Calculation of Interest**

Subject to Conditions 3.2(a) and 5, the amount of interest payable on each Fixed Interest Payment Date will be equal to £48.75 per Calculation Amount (as defined below).

Where, in relation to any period ending prior to the First Call Date, it is necessary to compute an amount of interest in respect of any Note during an Interest Period, such interest shall be calculated on the basis of (a) the actual number of days in the period from and including the date from which interest in respect of such Interest Period begins to accrue (the "**Accrual Date**") to but excluding the date on which it falls due divided by (b) the actual number of days from and including the Accrual Date to but excluding the next following Fixed Interest Payment Date. Where interest is to be calculated in respect of any period commencing on or after the First Call Date, the applicable day count fraction will be the actual number of days in the relevant Interest Period divided by 365.

Interest shall be calculated per £1,000 in principal amount of the Notes (the "**Calculation Amount**") by applying the applicable Interest Rate to such Calculation Amount, multiplying the resulting figure by the relevant day count fraction described above in this Condition 4.3 for the relevant period and rounding the resultant figure to two decimal places (with 0.005 being rounded up).

### **4.4 Fixed Interest Rate**

The rate of interest on the Notes from (and including) the Issue Date to (but excluding) the First Call Date is 4.875 per cent. per annum (the "**Fixed Interest Rate**").

### **4.5 Floating Interest Rate**

The rate of interest on the Notes for an Interest Period commencing on or after the First Call Date (each a "**Floating Interest Rate**") shall be equal to the sum of (i) the 3-month LIBOR Rate applicable to such Interest Period, determined as provided below, and (ii) the Margin, all as determined by the Agent Bank on the Interest Determination Date applicable to such Interest Period.

#### **4.6 Determination of Floating Interest Rates**

The Agent Bank will on each Interest Determination Date determine the Floating Interest Rate applicable to the Interest Period commencing on such Interest Determination Date and calculate the amount of interest (subject to Conditions 3.2(a) and 5) payable per Calculation Amount in respect of such Interest Period.

#### **4.7 Publication of Floating Interest Rates**

Unless the Notes are to be redeemed on the relevant Interest Determination Date, the Agent Bank shall cause notice of each Floating Interest Rate and the related amount of interest payable as determined in accordance with this Condition 4 to be given to the Noteholders in accordance with Condition 12, the Trustee, the Principal Paying Agent and any stock exchange or other relevant authority on which the Notes are for the time being listed or admitted to trading, in each case as soon as practicable after its determination but in any event not later than the fourth Business Day thereafter.

#### **4.8 Agent Bank**

So long as any of the Notes remain outstanding, the Issuer will maintain an Agent Bank. The Issuer may, with the prior written approval of the Trustee, from time to time replace the Agent Bank with another leading financial institution in London. If the Agent Bank is unable or unwilling to continue to act as the Agent Bank, the Issuer shall forthwith appoint another leading financial institution in London approved in writing by the Trustee to act as such in its place. The Agent Bank may not resign its duties or be removed without a successor having been appointed as aforesaid.

*As of the Issue Date, the initial Agent Bank appointed by the Issuer will be the initial Principal Paying Agent, as identified in the preamble to these Conditions.*

#### **4.9 Determinations of Agent Bank Binding**

All notification, opinions, determinations, certificates, calculation, quotations and decisions given, expressed, made (or deemed to be made) or obtained for the purposes of this Condition 4 by the Agent Bank shall (in the absence of wilful default or manifest error) be binding on the Issuer, the Agent Bank, the Trustee, the Principal Paying Agent, the Registrar and the Transfer Agents and all Noteholders and no liability to the Noteholders shall attach to the Agent Bank in connection with the exercise or non-exercise by it of any of its powers, duties and discretions.

### **5 Deferral of Interest**

#### **5.1 Optional Deferral of Interest**

The Issuer may elect in respect of any Optional Interest Payment Date, by notice to the Noteholders, the Trustee, and the Principal Paying Agent pursuant to Condition 5.6 below, to defer payment of all (but not some only) of the interest accrued to that date and the Issuer shall not have any obligation to make such payment on that date.

#### **5.2 Mandatory Deferral of Interest**

Payment of interest on the Notes by the Issuer will be mandatorily deferred on each Mandatory Interest Deferral Date. The Issuer shall notify the Noteholders, the Trustee and the Principal Paying Agent of any Mandatory Interest Deferral Date as provided in Condition 5.6 (provided that failure to make such notification shall not oblige the Issuer to make payment of such interest, or cause the same to become due and payable, on such date).

A certificate signed by two Authorised Signatories confirming that (a) a Regulatory Deficiency Interest Deferral Event has occurred and is continuing, or would occur if payment of interest on the Notes were to be made on the relevant Interest Payment Date or (b) a Regulatory Deficiency Interest Deferral Event has ceased to occur and/or payment of interest on the Notes on the relevant Interest Payment Date would not result in a Regulatory Deficiency Interest Deferral Event occurring, shall be treated

and accepted by the Issuer, the Trustee, the Noteholders and all other interested parties as correct and sufficient evidence thereof, shall be binding on all such persons and the Trustee shall be entitled to rely on such certificate without liability to any person.

### **5.3 No default**

Notwithstanding any other provision in these Conditions or the Trust Deed, any payment which for the time being is not made by virtue of Conditions 3.2(a), 5.1 or 5.2 shall not constitute a default for any purpose (including, but without limitation, Condition 10.1) on the part of the Issuer and will not give the Noteholders or the Trustee any right to accelerate the Notes.

### **5.4 Arrears of Interest**

Any interest on the Notes not paid on an Interest Payment Date as a result of: (i) the exercise by the Issuer of its discretion to defer such payment of interest pursuant to Condition 5.1; (ii) the obligation of the Issuer to defer such payment of interest pursuant to Condition 5.2 or (iii) the inability of the Issuer to make such payment of interest pursuant to Condition 3.2(a), shall (without double-counting), together with any other interest not paid on any earlier Interest Payment Dates, to the extent and so long as the same remains unpaid, constitute “**Arrears of Interest**”. Arrears of Interest shall not themselves bear interest.

### **5.5 Payment of Arrears of Interest**

Any Arrears of Interest may (subject to Condition 3.2(a) and to satisfaction of the Regulatory Clearance Condition) be paid by the Issuer in whole or in part at any time upon the expiry of not less than 14 days’ notice to such effect given by the Issuer to the Trustee, the Principal Paying Agent and the Noteholders in accordance with Condition 12 and in any event will become due and payable by the Issuer (subject, in the case of (a) and (c) below, to Condition 3.2(a) and to satisfaction of the Regulatory Clearance Condition) in whole (and not in part) upon the earliest of the following dates:

- (a) the next Interest Payment Date which is not a Mandatory Interest Deferral Date and on which a scheduled payment of interest in respect of the Notes is made or is required to be made pursuant to these Conditions (other than a voluntary payment by the Issuer of any Arrears of Interest); or
- (b) the date on which an order is made by any competent court or a resolution is passed for the winding-up of the Issuer; or
- (c) the date fixed for any redemption or purchase of Notes pursuant to Condition 7 (subject to any deferral of such redemption date pursuant to Condition 7.3) or Condition 10.

### **5.6 Notice of Deferral**

The Issuer shall notify the Trustee, the Principal Paying Agent and the Noteholders in accordance with Condition 12 not less than five Business Days prior to an Interest Payment Date:

- (i) if that Interest Payment Date is an Optional Interest Payment Date in respect of which the Issuer elects to defer interest as provided in Condition 5.1 above;
- (ii) if that Interest Payment Date is a Mandatory Interest Deferral Date and specifying that interest will not be paid because a Regulatory Deficiency Interest Deferral Event has occurred and is continuing or would occur if payment of interest was made on such Interest Payment Date, provided that if a Regulatory Deficiency Interest Deferral Event occurs less than five Business Days prior to an Interest Payment Date, the Issuer shall promptly give notice of the interest deferral in accordance with Condition 12 following the occurrence of such event; or
- (iii) if payment of interest is to be deferred on that Interest Payment Date only as a result of the non-satisfaction of Condition 3.2(a) and specifying the same, provided that if the Issuer becomes aware of such non-satisfaction of Condition 3.2(a) less than five Business Days prior to an

Interest Payment Date, the Issuer shall promptly give notice of the interest deferral in accordance with Condition 12 following it becoming so aware.

## **6 Payments**

### **6.1 Payments in respect of Notes**

Payment of principal and interest (including Arrears of Interest) will be made by transfer to the registered account of the relevant Noteholder. Payments of principal, and payments of interest and Arrears of Interest due at the time of redemption of the Notes, will only be made against surrender of the relevant Certificate at the specified office of any of the Agents. Save as provided in the previous sentence, interest and Arrears of Interest due for payment on the Notes will be paid to the holder shown on the Register at the close of business on the date (the “**record date**”) being the second day before the due date for the relevant payment.

For the purposes of this Condition 6, a Noteholder’s registered account means the sterling account maintained by or on behalf of it with a bank that processes payments in sterling, details of which appear on the Register at the close of business, in the case of principal, and of interest and Arrears of Interest due at the time of redemption of the Notes, on the second Business Day before the due date for payment and, in the case of any other payment of interest and Arrears of Interest, on the relevant record date.

### **6.2 Payments subject to applicable laws**

Save as provided in Condition 8, payments will be subject in all cases to (i) any other applicable fiscal or other laws and regulations in the place of payment or other laws and regulations to which the Issuer or its Agents agree to be subject and the Issuer will not be liable for any taxes or duties of whatever nature imposed or levied by such laws, regulations or agreements and (ii) any withholding or deduction required pursuant to an agreement described in Section 1471(b) of the U.S. Internal Revenue Code of 1986 (the “**Code**”) or otherwise imposed pursuant to Sections 1471 to 1474 of the Code, any regulations or agreements thereunder, any official interpretations thereof, or any law implementing an intergovernmental approach thereto.

### **6.3 No commissions**

No commissions or expenses shall be charged to the Noteholders in respect of any payments made in accordance with this Condition 6.

### **6.4 Payment on Business Days**

Where payment is to be made by transfer to a registered account, payment instructions (for value the due date or, if that is not a Business Day, for value the first following day which is a Business Day) will be initiated on the Business Day preceding the due date for payment or, in the case of a payment of principal, or of a payment of interest or Arrears of Interest due at the time of redemption of the Notes, if later, on the Business Day on which the relevant Certificate is surrendered at the specified office of an Agent.

Noteholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due if the due date is not a Business Day or if the Noteholder is late in surrendering its Certificate (in circumstances where it is required to do so).

### **6.5 Partial payments**

If the amount of principal or interest (including Arrears of Interest) which is due on the Notes is not paid in full, the Registrar will annotate the Register with a record of the amount of principal or interest in fact paid.

## **6.6 Agents**

The names of the initial Agents and their initial specified offices are set out at the end of these Conditions. The Issuer reserves the right, subject to the prior written approval of the Trustee, at any time to vary or terminate the appointment of any Agent and to appoint additional or other Agents, provided that the Issuer will so long as any Notes remain outstanding maintain:

- (a) a Principal Paying Agent;
- (b) an Agent (which may be the Principal Paying Agent) having a specified office in a European city;
- (c) a Registrar;
- (d) a Transfer Agent; and
- (e) on and from the First Call Date, an Agent Bank.

Notice of any termination or appointment and of any changes in specified offices of any of the Agents will be given to the Noteholders promptly by the Issuer in accordance with Condition 12.

## **7 Redemption, Substitution, Variation and Purchase**

### **7.1 Redemption at Maturity**

Subject to Condition 7.3 and Condition 7.8 and to satisfaction of the Regulatory Clearance Condition, unless previously redeemed or purchased and cancelled as provided below, the Issuer will redeem the Notes at their principal amount on the Maturity Date together with any Arrears of Interest and any other accrued and unpaid interest to (but excluding) the Maturity Date.

### **7.2 Redemption at the Option of the Issuer**

Subject to Conditions 7.3 and 7.8 and to satisfaction of the Regulatory Clearance Condition, the Issuer may, having given not less than 30 nor more than 60 days' notice to the Noteholders in accordance with Condition 13 (which notice shall be irrevocable), the Trustee and the Principal Paying Agent, redeem the Notes at their principal amount on the First Call Date or any Floating Interest Payment Date thereafter, together with any Arrears of Interest and any other accrued and unpaid interest to (but excluding) the relevant date of redemption.

### **7.3 Deferral of redemption date**

*Deferral due to the occurrence of a Regulatory Deficiency Redemption Deferral Event*

- (a) No Notes shall be redeemed on the Maturity Date pursuant to Condition 7.1 or prior to the Maturity Date pursuant to Conditions 7.2, 7.5 or 7.6 if (i) a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing or would occur if redemption was made pursuant to Condition 7 or (ii) redemption would otherwise breach the provisions of the Relevant Rules which apply to obligations eligible to qualify as Tier 2 Capital of the Issuer and, in each case redemption shall instead be deferred in accordance with the provisions of this Condition 7.3.
- (b) The Issuer shall notify the Trustee, the Principal Paying Agent and the Noteholders in accordance with Condition 12 no later than five Business Days prior to any date set for redemption of the Notes if such redemption is to be deferred in accordance with Condition 7.3(a) above, provided that if a Regulatory Deficiency Redemption Deferral Event occurs less than five Business Days prior to the date set for redemption, the Issuer shall promptly give notice of such deferral in accordance with Condition 12 as soon as reasonably practicable following the occurrence of such event.

- (c) If redemption of the Notes does not occur on the Maturity Date or, as applicable, the date specified in the notice of redemption by the Issuer under Condition 7.2, 7.5 or 7.6 as a result of Condition 7.3(a) above, the Issuer shall (subject, in the case of (i) and (ii) below only, to Condition 3.2(a) and to satisfaction of the Regulatory Clearance Condition) redeem such Notes at their principal amount together with any Arrears of Interest and any other accrued and unpaid interest, upon the earliest of:
- (i) the date falling 10 Business Days after the date the Regulatory Deficiency Redemption Deferral Event has ceased (unless on such 10th Business Day a further Regulatory Deficiency Redemption Deferral Event has occurred and is continuing or redemption of the Notes on such date would result in a Regulatory Deficiency Redemption Deferral Event occurring, in which case the provisions of Condition 7.3(a) and this Condition 7.3(c) will apply *mutatis mutandis* to determine the due date for redemption of the Notes); or
  - (ii) the date falling 10 Business Days after the Relevant Regulator has agreed to the repayment or redemption of the Notes; or
  - (iii) the date on which an order is made by any competent court or a resolution is passed for the winding-up of the Issuer.

The Issuer shall notify the Trustee, the Principal Paying Agent and the Noteholders in accordance with Condition 12 no later than five Business Days prior to any such date set for redemption pursuant to (i) or (ii) above.

(d) *Deferral due to non-satisfaction of Condition 3.2(a)*

If, on any date scheduled for redemption of the Notes pursuant to these Conditions, the Issuer is not required to defer redemption of the Notes by virtue of a Regulatory Deficiency Redemption Deferral Event but is required to defer redemption of the Notes as a result of the non-satisfaction of Condition 3.2(a) at such time, then:

- (i) the Issuer shall promptly notify the Trustee, the Principal Paying Agent and the Noteholders in accordance with Condition 12 after it becomes aware that Condition 3.2(a) will not be, or is not, satisfied on the scheduled redemption date and that, accordingly, such redemption of the Notes will be, or has been, deferred; and
- (ii) the Issuer shall (subject in the case of (A) below only, to Condition 3.2(a) and satisfaction of the Regulatory Clearance Condition) redeem the Notes at their principal amount together with any Arrears of Interest and any other accrued and unpaid interest, upon the earliest of:
  - (A) the date falling 10 Business Days immediately following the day that (x) the Issuer is Solvent and (y) the redemption of the Notes would not result in the Issuer ceasing to be Solvent (provided that if on such 10th Business Day a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing, or would occur if the Notes were to be redeemed, then the Notes shall not be redeemed on such date and Conditions 3.2(a) and 7.3(c) shall apply *mutatis mutandis* to determine the due date for redemption of the Notes); and
  - (B) the date on which an order is made by any competent court or a resolution is passed for the winding-up of the Issuer.

The Issuer shall notify the Trustee, the Principal Paying Agent and the Noteholders in accordance with Condition 12 no later than five Business Days prior to any such date set for redemption pursuant to (A) above.

(e) *Deferral of redemption due to non-satisfaction of the Regulatory Clearance Condition*

If, on the Maturity Date or any other date scheduled for redemption of the Notes, the Issuer is required to defer redemption only due to the Regulatory Clearance Condition not being satisfied, redemption of the Notes shall be deferred and the Issuer shall redeem the Notes at their principal amount together with any Arrears of Interest and any other accrued and unpaid interest, upon the earliest of (A) the date falling 10 Business Days immediately following the day on which the Regulatory Clearance Condition is satisfied (but subject always to the foregoing provisions of this Condition 7.3) and (B) the date on which an order is made by any competent court or a resolution is passed for the winding-up of the Issuer. The Issuer will promptly notify the Trustee, the Principal Paying Agent and the Noteholders, in accordance with Condition 12, (i) upon it becoming aware that redemption of the Notes will be deferred due to the Regulatory Clearance Condition not being satisfied and (ii) upon the subsequent satisfaction of the Regulatory Clearance Condition (the latter notice to specify the deferred redemption date).

(f) *Certifications regarding a Regulatory Deficiency Redemption Deferral Event and Regulatory Clearance Condition*

A certificate signed by two Authorised Signatories confirming that :

- (i) (A) a Regulatory Deficiency Redemption Deferral Event has occurred and is continuing, or would occur if redemption of the Notes were to be made or (B) a Regulatory Deficiency Redemption Deferral Event has ceased to occur and/or redemption of the Notes would not result in a Regulatory Deficiency Redemption Deferral Event occurring; or
- (ii) the Regulatory Clearance Condition is not satisfied on the Maturity Date or any other date scheduled for redemption of the Notes,

shall, be treated and accepted by the Issuer, the Trustee, the Noteholders and all other interested parties as correct and sufficient evidence thereof, shall be binding on all such persons and the Trustee shall be entitled to rely on such certificate without liability to any person.

#### **7.4 Deferral of redemption not a default**

Notwithstanding any other provision in these Conditions or in the Trust Deed, the deferral of redemption of the Notes in accordance with Condition 3.2(a) or 7.3 will not constitute a default by the Issuer and will not give Noteholders or the Trustee any right to accelerate the Notes or take any enforcement action under the Notes or the Trust Deed.

#### **7.5 Redemption, variation or substitution at the option of the Issuer for taxation reasons**

Subject to Conditions 7.3 and 7.8, if the Issuer satisfies the Trustee immediately before the giving of the notice referred to below that:

- (a) as a result of any Tax Law Change, the Issuer has, or will on the next Interest Payment Date, become obliged to pay additional amounts as provided or referred to in Condition 8 or the Issuer would otherwise suffer adverse tax consequences; or
- (b) in respect of the Issuer's obligation to make any payment of interest on the Notes on the next following Interest Payment Date, the Issuer would not be entitled to claim a deduction in respect of computing its taxation liabilities in the United Kingdom, or such entitlement is materially reduced,

and

- (c) in each case, the effect of the foregoing cannot be avoided by the Issuer taking reasonable measures available to it,

the Issuer may at its option (without any requirement for the consent or approval of the Noteholders) and having given not less than 30 nor more than 60 days' notice to the Trustee, the Principal Paying Agent and, in accordance with Condition 12, the Noteholders (which notice shall be irrevocable) either:

- (A) redeem all the Notes, but not some only, at any time up to, and including, the First Call Date, or on any Floating Interest Payment Date thereafter at their principal amount together with any Arrears of Interest and any other accrued and unpaid interest to (but excluding) the date of redemption, provided that no such notice of redemption shall be given earlier than 90 days prior to the earliest date on which (i) with respect to (a) above, the Issuer would be obliged to pay such additional amounts; or (ii) with respect to (b) above, the Issuer would not be entitled to claim such deduction in respect of computing its taxation liabilities in the United Kingdom, in each case were a payment in respect of the Notes then due; or
- (B) substitute at any time all (but not some only) of the Notes for, or vary the terms of the Notes so that they become or remain, Qualifying Tier 2 Securities, and the Trustee shall (subject as provided in Condition 7.7 and to the receipt by it of the certificates of the Authorised Signatories referred to in Condition 7.8 below and in the definition of Qualifying Tier 2 Securities) agree to such substitution or variation,

Any such substitution or variation shall not be permitted if such substitution or variation would itself give the Issuer the right to redeem, substitute or vary the terms pursuant to this Condition 7.5 in relation to the Qualifying Tier 2 Securities.

#### **7.6 Redemption, substitution or variation at the option of the Issuer due to a Capital Disqualification Event or Ratings Methodology Event**

- (a) Subject to Conditions 7.3 and 7.8, if a Capital Disqualification Event or a Ratings Methodology Event has occurred and is continuing, or the Issuer satisfies the Trustee that, as a result of any change in, or amendment to, or any change in the application or official interpretation of, any applicable law, regulation, ratings methodology or other official publication, the same will occur within a period of six months, then the Issuer may, having given not less than 30 nor more than 60 days' notice to the Noteholders in accordance with Condition 12, the Trustee and the Principal Paying Agent, which notice must be given during the Notice Period and shall be irrevocable, either:
  - (i) at any time up to, and including, the First Call Date, or on any Floating Interest Payment Date thereafter redeem all (but not some only) of the Notes at their principal amount, together with any Arrears of Interest and any other accrued and unpaid interest to (but excluding) the date of redemption; or
  - (ii) at any time substitute all (and not some only) of the Notes for, or vary the terms of the Notes so that they become or remain (A) in the case of a substitution or variation in connection with a Capital Disqualification Event, Qualifying Tier 2 Securities, or (B) in the case of a substitution or variation in connection with a Ratings Methodology Event, Rating Agency Compliant Securities, and in either case the Trustee shall (subject as provided in Condition 7.7 and to the receipt by it of the certificates of the Authorised Signatories referred to in Condition 7.8 below, in the definition of 'Qualifying Tier 2 Securities' and, in the case of a substitution or variation in connection with a Ratings

Methodology Event, in the definition of ‘Rating Agency Compliant Securities’) agree to such substitution or variation.

- (b) For the purposes of this Condition 7.6, “**Notice Period**” means the period commencing on the date on which the relevant Capital Disqualification Event or relevant Ratings Methodology Event (as the case may be) first occurs (or, as applicable, the date on which the Issuer satisfies the Trustee that the same will occur within a period of six months) and ending on the thirtieth calendar day following satisfaction of the Regulatory Clearance Condition in respect of the redemption, substitution or variation which is the subject of the notice to which the Notice Period relates.
- (c) Any such substitution or variation shall not be permitted if such substitution or variation would itself give rise to a Capital Disqualification Event or Ratings Methodology Event in relation to the Qualifying Tier 2 Securities or Rating Agency Compliant Securities, respectively.

#### **7.7 Trustee role on redemption, variation or substitution; Trustee not obliged to monitor**

The Trustee shall (at the expense of the Issuer) use its reasonable endeavours to co-operate with the Issuer (including, but not limited to, entering into such documents or deeds as may be necessary) to give effect to substitution or variation of the Notes for or into Qualifying Tier 2 Securities pursuant to Condition 7.5 or Qualifying Tier 2 Securities or Rating Agency Compliant Securities (as the case may be) pursuant to Condition 7.6 above provided that the Trustee shall not be obliged to co-operate in or agree to any such substitution or variation of the terms if the securities into which the Notes are to be substituted or are to be varied or the co-operation in such substitution or variation imposes, in the Trustee’s opinion, more onerous obligations upon it or exposes it to liabilities or reduces its protections. If the Issuer does not elect to substitute or vary the Notes, or if a substitution or variation, as provided herein, cannot be made by the Issuer, the Issuer may, subject as provided above, redeem the Notes as provided above.

The Trustee shall not be under any duty to monitor whether any event or circumstance has happened or exists for the purposes of this Condition 7 and will not be responsible to Noteholders for any loss arising from any failure by it to do so. Unless and until the Trustee has actual knowledge of the occurrence of any event or circumstance within this Condition 7, it shall be entitled to assume that no such event or circumstance exists.

When implementing any substitution or variation pursuant to Condition 7.5 or 7.6, the Trustee shall not consider the interests of the Noteholders or any other person. The Trustee shall not be liable to the Noteholders or any other person for so acting or for any losses incurred by any person by reason thereof, irrespective of whether any such modification is or may be materially prejudicial to the interests of any such person and/or is or may be a matter referred to in the proviso in paragraph 3 of Schedule 3 of the Trust Deed.

#### **7.8 Preconditions to redemption, variation, substitution and purchases**

- (a) Prior to the publication of any notice of redemption, variation or substitution pursuant to Condition 7.5 or 7.6, the Issuer shall deliver to the Trustee a certificate signed by two Authorised Signatories stating that, as the case may be:
  - (i) the applicable requirement referred to in Condition 7.5(a) or loss of a benefit referred to in Condition 7.5(b) above will apply on the next Interest Payment Date and cannot be avoided by the Issuer taking reasonable measures available to it, and the Issuer shall deliver to the Trustee an opinion from a nationally recognised law firm or other tax adviser in the UK experienced in such matters to the effect that the relevant event or circumstance referred to in Condition 7.5(a) or Condition 7.5(b) applies (but, for the avoidance of doubt, such opinion shall not be requested to comment on the ability of the

Issuer to avoid such event or circumstance by taking reasonable measures available to it); or

- (ii) a Capital Disqualification Event or a Ratings Methodology Event has occurred and is continuing as at the date of the certificate or, as the case may be, will occur within a period of six months; and
- (iii) in the case of notice of a redemption before (in the case of an event described in Condition 7.5(b)) the First Call Date or (in any other case) the fifth anniversary of the Issue Date, it would have been reasonable for the Issuer to conclude, judged at the Issue Date, that the circumstance entitling the Issuer to exercise the right of redemption was unlikely to occur,

and the Trustee shall accept such certificate (and opinion, if applicable) as sufficient evidence of the satisfaction of the conditions precedent set out above, in which event it shall be conclusive and binding on the Noteholders. The Trustee may rely absolutely on such certification without liability to any person.

- (b) In addition, prior to the publication of any notice of redemption before the Maturity Date or any substitution, variation or purchase of the Notes, the Issuer will be required to have complied with the Regulatory Clearance Condition and be in continued compliance with Regulatory Capital Requirements. A certificate from any two Authorised Signatories to the Trustee confirming such compliance shall be conclusive evidence of such compliance for the purposes of these Conditions. The Trustee may rely absolutely on such certification without liability to any person.
- (c) The Issuer shall not redeem any Notes or purchase any Notes unless at the time of such redemption, payment or purchase it is, and will immediately thereafter remain (i) in compliance with Condition 3.2(a) and (ii) in compliance with all Regulatory Capital Requirements applicable to it. A certificate from any two Authorised Signatories to the Trustee confirming such compliance shall be conclusive evidence of such compliance. The Trustee may rely absolutely on such certification without liability to any person.
- (d) If a redemption of the Notes in accordance with Condition 7.5 or Condition 7.6, is to occur within five years of the Issue Date of the Notes, any such redemption will only be made (i) in compliance with the Relevant Rules and (ii) on the condition that the Notes are exchanged for, or redeemed out of the proceeds of a new issue of, capital of the same or higher quality. A certificate from any two Authorised Signatories to the Trustee confirming such compliance shall be conclusive evidence of such compliance and the Trustee may rely absolutely on such certification without liability to any person.
- (e) Notwithstanding any of the above conditions in this Condition 7.8, if at the time of any redemption, substitution, variation or purchase, the prevailing Relevant Rules permit the redemption, substitution, variation or purchase only after compliance with one or more alternative or additional pre-conditions to those set out above in this Condition 7.8, the Issuer shall comply with such other and/or, as appropriate, additional pre-conditions(s).

## **7.9 Compliance with stock exchange rules**

In connection with any substitution or variation of the Notes in accordance with Condition 7.5 or Condition 7.6, the Issuer shall comply with the rules of any stock exchange or other relevant authority on which the Notes are for the time being listed or admitted to trading, and (for so long as the Notes are listed on the Official List of the FCA in its capacity as competent authority under the FSMA and admitted to trading on the London Stock Exchange's regulated market) shall publish a supplement in

connection therewith if the Issuer is required to do so in order to comply with Section 87G of the FSMA.

#### **7.10 Purchases**

Subject to Condition 7.8, the Issuer may at any time purchase Notes in any manner and at any price. All Notes purchased by or on behalf of the Issuer may be held, reissued, resold or, at the option of the Issuer, surrendered for cancellation to the Principal Paying Agent.

#### **7.11 Cancellations**

All Notes redeemed or substituted by the Issuer pursuant to this Condition 7, and all Notes purchased and surrendered for cancellation pursuant to Condition 7.10, will forthwith be cancelled. Any Notes so surrendered for cancellation may not be reissued or resold and the obligations of the Issuer in respect of any such Notes shall be discharged.

#### **7.12 Notices Final**

Subject and without prejudice to Conditions 3.2(a), 7.3 and 7.8, any notice of redemption, substitution or variation as is referred to in Conditions 7.2, 7.5 or 7.6 above shall be irrevocable and upon expiry of such notice, the Issuer shall be bound to redeem, or as the case may be, vary or substitute, the Notes in accordance with the terms of the relevant Condition.

### **8 Taxation**

#### **8.1 Payment without withholding**

All payments in respect of the Notes by or on behalf of the Issuer shall be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature (“**Taxes**”) imposed or levied by or on behalf of the Relevant Jurisdiction unless the withholding or deduction of the Taxes is required by law. In any such event, the Issuer will pay such additional amounts as may be necessary in order that the net amounts received by the Noteholders after the withholding or deduction shall equal the respective amounts which would have been received in respect of the Notes in the absence of the withholding or deduction; except that no additional amounts shall be payable in relation to any payment in respect of any Note:

- (a) the holder of which is liable to the Taxes in respect of the Note by reason of his having some connection with the Relevant Jurisdiction other than the mere holding of the Note; or
- (b) in circumstances where such withholding or deduction would not be required if the holder or any person acting on his behalf had obtained and/or presented any form or certificate or had made a declaration of non-residence or similar claim for exemption to the relevant tax authority upon the making of which the holder would have been able to avoid such withholding or deduction; or
- (c) surrendered for payment (where surrender is required) more than 30 days after the Relevant Date except to the extent that a holder would have been entitled to additional amounts on surrendering the same for payment on the last day of the period of 30 days assuming (whether or not such is in fact the case) that day to have been a Business Day.

#### **8.2 Additional Amounts**

Any reference in these Conditions to any amounts payable in respect of the Notes shall be deemed also to refer to any additional amounts which may be payable under this Condition or under any undertakings given in addition to, or in substitution for, this Condition pursuant to the Trust Deed.

### **9 Prescription**

Claims in respect of principal and interest (including Arrears of Interest) will become prescribed unless made within 10 years (in the case of principal) and five years (in the case of interest) from the Relevant Date.

## 10 Events of Default

### 10.1 Rights to institute and/or prove in a winding-up of the Issuer

*The right to institute winding-up proceedings in respect of the Issuer is limited to circumstances where a payment of principal, interest or other amount in respect of the Notes by the Issuer under the Notes or the Trust Deed has become due and is not duly paid. For the avoidance of doubt (without prejudice to Condition 10.1(b) below), no amount shall be due from the Issuer in circumstances where payment of such amount could not be made in compliance with Condition 3.2(a) or (in the case of interest) is deferred by the Issuer in accordance with Conditions 5.1 or 5.2, or (in the case of principal) is deferred by the Issuer in accordance with Condition 7.3.*

- (a) If default is made in the payment of any principal or premium in respect of the Notes for a period of 14 days or more after the due date for the same, or in the payment of any interest (including Arrears of Interest) for a period of 14 days or more after an Interest Payment Date (save to the extent and for so long as payment has been deferred in accordance with Conditions 5.1 or 5.2) or any other date on which any payment of interest is due (each an “**Event of Default**”) and the Event of Default is continuing, the Trustee may, subject as provided in Condition 10.3, at its discretion and without further notice, institute proceedings for the winding-up of the Issuer in England and Wales (but not elsewhere) and/or prove in any winding-up of the Issuer (whether in England or elsewhere), but may take no other action in respect of such default.
- (b) In the event of the commencement of the winding-up of the Issuer (other than in accordance with Condition 10.1(a) above) (also an “**Event of Default**”), the Trustee at its discretion may, and if so requested in writing by the holders of at least one-quarter in principal amount of the Notes then outstanding (as defined in the Trust Deed) or so directed by an Extraordinary Resolution (as defined in the Trust Deed) of the Noteholders shall, (subject to it first being indemnified and/or secured and/or prefunded to its satisfaction), (i) give notice to the Issuer that the Notes are immediately due and repayable (and the Notes shall thereby become so due and repayable) at their principal amount together with accrued interest as provided in the Trust Deed, together with all Arrears of Interest, if any and/or (ii) prove in the winding-up of the Issuer.

*The Issuer has undertaken in the Trust Deed forthwith to give notice in writing to the Trustee of the occurrence of any Event of Default referred to in (a) or (b) above.*

### 10.2 Enforcement

Without prejudice to Condition 10.1, the Trustee may at its discretion and without further notice institute such proceedings against the Issuer as it may think fit to enforce any term or condition binding on the Issuer under the Trust Deed or the Notes (other than any payment obligation of the Issuer under or arising from the Notes or the Trust Deed, including any damages awarded for breach of any obligations thereunder) but in no event shall the Issuer, by virtue of the institution of any such proceedings, be obliged to pay any sum or sums, in cash or otherwise, sooner than the same would otherwise have been payable by it. Nothing in this Condition 10.2 shall, however, prevent the Trustee, subject to Condition 10.1, instituting proceedings for the winding-up of the Issuer in England and Wales and/or proving in any winding-up of the Issuer (whether in England and Wales or elsewhere) and/or claiming in any liquidation of the Issuer in respect of any payment obligation of the Issuer (whether in England and Wales or elsewhere) where such payment obligation arises from the Notes or the Trust Deed (including, without limitation, payment of any principal, interest or Arrears of Interest in respect of the Notes or any damages awarded for breach of any obligations under the Notes or the Trust Deed).

*The restriction in this Condition 10.2 on the payment of damages has the effect of limiting the remedies available to the Trustee and the Noteholders in the event of a breach of certain covenants (other than payment covenants) by the Issuer.*

### **10.3 Entitlement of Trustee**

The Trustee shall not be bound to take any of the actions referred to in Condition 10.1 or 10.2 above against the Issuer to enforce the terms of the Trust Deed, the Notes or any other action under or pursuant to the Trust Deed unless (i) it shall have been so directed by an Extraordinary Resolution of the Noteholders or requested in writing by the holders of at least one-quarter in principal amount of the Notes then outstanding and (ii) it shall have been indemnified and/or secured and/or prefunded to its satisfaction.

### **10.4 Right of Noteholders**

No Noteholder shall be entitled to proceed directly against the Issuer or to institute proceedings for the winding-up or claim in the liquidation of the Issuer or to prove in such winding-up unless the Trustee, having become so bound to proceed or being able to prove in such winding-up or claim in such liquidation, fails to do so within a reasonable period and such failure shall be continuing, in which case the Noteholder shall have only such rights against the Issuer as those which the Trustee is entitled to exercise as set out in this Condition 10.

### **10.5 Extent of Noteholders' remedy**

No remedy against the Issuer, other than as referred to in this Condition 10, shall be available to the Trustee or the Noteholders, whether for the recovery of amounts owing in respect of the Notes or under the Trust Deed or in respect of any breach by the Issuer of any of its other obligations under or in respect of the Notes or under the Trust Deed.

## **11 Replacement of Certificates**

If any Certificate is lost, stolen, mutilated, defaced or destroyed it may be replaced at the specified office of the Registrar upon payment by the claimant of the expenses incurred in connection with the replacement and on such terms as to evidence and indemnity as the Issuer may reasonably require. Mutilated or defaced Certificates must be surrendered before replacements will be issued.

## **12 Notices**

All notices to the Noteholders will be valid if mailed to them at their respective addresses in the Register maintained by the Registrar. The Issuer shall also ensure that notices are duly given or published in a manner which complies with the rules and regulations of any stock exchange or other relevant authority on which the Notes are for the time being listed. Any notice shall be deemed to have been given on the second day after being so mailed or on the date of publication or, if so published more than once or on different dates, on the date of the first publication.

## **13 Meetings of Noteholders, Modification, Waiver and Authorisation**

### **13.1 Meetings of Noteholders**

The Trust Deed contains provisions for convening meetings of the Noteholders to consider any matter affecting their interests, including the modification or abrogation by Extraordinary Resolution of any of these Conditions or any of the provisions of the Trust Deed. Such a meeting may be convened by the Issuer, the Trustee or Noteholders holding not less than 10 per cent., in principal amount of the Notes for the time being outstanding. The quorum at any meeting for passing an Extraordinary Resolution will be one or more persons present holding or representing more than 50 per cent., in principal amount of the Notes for the time being outstanding, or at any adjourned such meeting one or more persons present whatever the principal amount of the Notes held or represented by him or them,

except that, at any meeting the business of which includes the modification or abrogation of certain of the provisions of these Conditions and certain of the provisions of the Trust Deed as set out in the proviso in paragraph 3 of Schedule 3 of the Trust Deed, the necessary quorum for passing an Extraordinary Resolution will be one or more persons present holding or representing not less than two-thirds, or at any adjourned such meeting not less than one-third, of the principal amount of the Notes for the time being outstanding. An Extraordinary Resolution passed at any meeting of the Noteholders will be binding on all Noteholders, whether or not they are present at the meeting.

The Trust Deed also provides that (i) a written resolution executed by or on behalf of the holders of not less than 90 per cent. in principal amount of the Notes for the time being outstanding or (ii) consent given by way of electronic consent through the relevant clearing system(s) (in form satisfactory to the Trustee) by or on behalf of holders of not less than 90 per cent., in principal amount of the Notes for the time being outstanding shall, in each case, take effect as if it were an Extraordinary Resolution.

The agreement or approval of the Noteholders shall not be required in the case of any variation of these Conditions and/or the Trust Deed required to be made in connection with the substitution or variation of the Notes pursuant to Conditions 7.5 or 7.6.

### **13.2 Modification, waiver, authorisation and determination**

The Trustee may agree, without the consent of the Noteholders, to any modification of, or to the waiver or authorisation of any breach or proposed breach of, any of these Conditions or any of the provisions of the Trust Deed (provided that, in any such case (save as otherwise provided in the Trust Deed), it is not, in the opinion of the Trustee, materially prejudicial to the interests of the Noteholders) or may agree, without any such consent as aforesaid, to any modification which, in its opinion, is of a formal, minor or technical nature or to correct a manifest error.

Except as provided herein, any modification to these Conditions or any provisions of the Trust Deed will be subject to satisfaction of the Regulatory Clearance Condition.

### **13.3 Trustee to have regard to interests of Noteholders as a class**

In connection with the exercise by it of any of its trusts, powers, authorities and discretions (including, without limitation, any modification, waiver, authorisation, determination or substitution of obligor), the Trustee shall have regard to the general interests of the Noteholders as a class but shall not have regard to any interests arising from circumstances particular to individual Noteholders (whatever their number) and, in particular but without limitation, shall not have regard to the consequences of any such exercise for individual Noteholders (whatever their number) resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory or any political sub-division thereof and the Trustee shall not be entitled to require, nor shall any Noteholder be entitled to claim, from the Issuer, the Trustee or any other person any indemnification or payment in respect of any tax consequence of any such exercise upon individual Noteholders except to the extent already provided for in Condition 8 and/or any undertaking given in addition to, or in substitution for, Condition 8 pursuant to the Trust Deed.

### **13.4 Notification to the Noteholders**

Any modification, abrogation, waiver, authorisation, determination or substitution shall be binding on the Noteholders and, unless the Trustee agrees otherwise, shall be notified by the Issuer to the Noteholders as soon as practicable thereafter in accordance with Condition 12.

## **14 Indemnification of the Trustee and its contracting with the Issuer**

### **14.1 Indemnification of the Trustee**

The Trust Deed contains provisions for the indemnification of the Trustee and for its relief from responsibility, including provisions relieving it from taking action unless indemnified and/or secured and/or prefunded to its satisfaction.

#### **14.2 Trustee contracting with the Issuer**

The Trust Deed also contains provisions pursuant to which the Trustee is entitled, *inter alia*, (i) to enter into business transactions with the Issuer and to act as trustee for the holders of any other securities issued or guaranteed by, or relating to, the Issuer, (ii) to exercise and enforce its rights, comply with its obligations and perform its duties under or in relation to any such transactions or, as the case may be, any such trusteeship without regard to the interests of, or consequences for, the Noteholders, and (iii) to retain and not be liable to account for any profit made or any other amount or benefit received thereby or in connection therewith.

#### **14.3 Regulatory Clearance Condition**

Wherever in these Conditions and/or the Trust Deed there is a requirement for the Regulatory Clearance Condition to be satisfied, the Trustee shall be entitled to assume without enquiry and without liability that such condition has been satisfied unless notified in writing to the contrary by the Issuer.

#### **15 Further Issues**

The Issuer may from time to time, without the consent of the Noteholders, create and issue further notes ranking *pari passu* in all respects (or in all respects save for the first payment of interest thereon) and so that the same shall be consolidated and form a single series with the outstanding Notes. Any further notes which are to form a single series with the outstanding Notes may (subject to the terms of the Trust Deed and with the consent of the Trustee) be constituted by a deed supplemental to the Trust Deed.

#### **16 Governing Law**

The Trust Deed and the Notes, and any non-contractual obligations arising out of or in connection with the Trust Deed and/or the Notes are governed by, and shall be construed in accordance with, English law.

#### **17 Rights of Third Parties**

No rights are conferred on any person under the Contracts (Rights of Third Parties) Act 1999 to enforce any term or condition of the Notes, but this does not affect any right or remedy of any person which exists or is available apart from that Act.

#### **18 Defined Terms**

In these Conditions:

“**3-month LIBOR Rate**” means, with respect to an Interest Period commencing on or after the First Call Date:

- (i) the three-month London interbank offered rate for deposits in sterling which appears on the Screen Page as at 11:00 hours (London time) on the Interest Determination Date applicable to such Interest Period; or
- (ii) if, at such time, no such rate appears or the Screen Page is unavailable, the Reference Bank Rate on such Interest Determination Date;

“**Accrual Date**” has the meaning given in Condition 4.3;

“**Agency Agreement**” has the meaning given in the preamble to these Conditions;

“**Agent Bank**” means the Principal Paying Agent or a financial institution appointed by the Issuer from time to time to the role of agent bank for determining the relevant Floating Interest Rate in respect of the Notes;

“**Agents**” means the Registrar, the Principal Paying Agent, the Agent Bank (save for the purposes of Conditions 2.3, 6.1, 6.2 and 6.4) and the other Paying Agents appointed from time to time under the Agency Agreement;

“**Arrears of Interest**” has the meaning given in Condition 5.4;

“**Assets**” means the unconsolidated gross assets of the Issuer as of the date of the latest published audited financial statements of the Issuer, but adjusted for subsequent events in such manner as the Council of Lloyd’s may determine;

“**Authorised Signatories**” has the meaning given to it in the Trust Deed;

“**Business Day**” means (i) except for the purposes of Condition 2 and 6.4, a day (other than a Saturday, Sunday or public holiday) on which commercial banks and foreign exchange markets are open for general business in London, (ii) for the purposes of Condition 2, a day (other than a Saturday, Sunday or public holiday) on which commercial banks are open for business in the city in which the specified office of the Agent with whom a Certificate is deposited in connection with a transfer is located and (iii) for the purpose of Condition 6.4, a day (other than a Saturday, Sunday or public holiday) on which commercial banks are open for business in London and, in the case of surrender of a Certificate, in the place in which the Certificate is surrendered;

“**Calculation Amount**” has the meaning given in Condition 4.3;

a “**Capital Disqualification Event**” is deemed to have occurred if, as a result of any replacement of or change to (or change to the interpretation by any court or authority entitled to do so of) the Relevant Rules the entire principal amount of the Notes is fully excluded from, or no longer capable of counting as Tier 2 Capital (however such term might be described in the Relevant Rules) for the purposes of the Issuer, except where such non-qualification is only as a result of any applicable limitation on the amount of such capital;

“**Central Assets**” means the Issuer’s own assets, including the assets generated from the issuance of the Notes, any loans made by members from time to time and any other subordinated debt obligations, that are available at its discretion to meet a member’s liabilities in respect of insurance business, including the Issuer’s consolidated reserves, but without taking any account of liabilities to repay subordinated debt obligations, all as shown in or determined by reference to the latest Financial Statements;

“**Central Assets Priority Payment**” means:

- (i) any payment (whether or not such payment is required by applicable law or regulation to be authorised by a specified person or persons or by an order of the court or otherwise) which, in a winding-up of the Issuer is permitted to be made out of Central Assets by the Issuer, or by any other person who under applicable law or regulation has the authority, power or discretion to make payments, or require payments to be made, out of Central Assets after the commencement of a proceeding in respect of a winding-up of the Issuer, and which is or would be made for a Permitted Purpose; and/or
- (ii) any payment which in a winding-up of the Issuer is required to be made out of Central Assets by any applicable law or regulation or by any order the court (whether such order is made pursuant to an application of the Issuer or otherwise) for any purposes in priority to payment of the claims of the Noteholders;

“**Central Fund**” means the fund financed by (among other things) contributions from Lloyd’s members and administered by the Council of Lloyd’s primarily as a fund for the protection of policyholders and includes the fund constituted and governed by the Central Fund Byelaw (No. 4 of 1986) made by the Council of Lloyd’s as amended from time to time, the fund (the “**New Central Fund**”) constituted and governed by the New Central Fund Byelaw (No. 23 of 1996) made by the Council of Lloyd’s as amended from time to time, and any fund constituted and governed by any successor byelaw or byelaws made by the Council of Lloyd’s;

“**Central Fund Undertaking**” means any undertaking which has been duly authorised, prior to the date on which the Issuer is wound-up, by the Council of Lloyd’s in accordance with the relevant byelaws of the Issuer

to make a payment other than an Excluded Payment out of Central Assets for the purpose of directly or indirectly extinguishing any liability of an Insolvent Member to any person (including without limitation to a policyholder under a contract of insurance or reinsurance or to any regulatory authority in respect of any levy imposed by that authority on the Insolvent Member) arising out of or in connection with insurance business carried on at Lloyd's by that Insolvent Member;

“**Certificate**” has the meaning given in Condition 1.1;

“**Companies Act**” means the Companies Act 2006 (as amended or re-enacted from time to time);

“**Compulsory Interest Payment Date**” means any Interest Payment Date: (i) in respect of which during the immediately preceding 6 months a Compulsory Interest Payment Event has occurred, (ii) which is not a Mandatory Interest Deferral Date and (iii) on which the Issuer is Solvent and the relevant payment of interest would not result in the Issuer ceasing to be Solvent;

“**Compulsory Interest Payment Event**” means:

- (i) any distribution of any Central Assets to members of Lloyd's generally;
- (ii) any declaration or payment of any distribution or other payment (including payment in relation to redemption or repurchase) on or in respect of any Junior Securities or Pari Passu Securities by the Issuer; or
- (iii) any redemption or repurchase of any Junior Securities or Pari Passu Securities by the Issuer for cash, save, in the case of (ii) and (iii) above, where the terms of the relevant Junior Securities or Pari Passu Securities do not allow the Issuer to defer, pass on or eliminate the relevant payment;

“**Council of Lloyd's**” means the Council of Lloyd's constituted by Lloyd's Act 1982 and such persons who are for the time being authorised by the Council of Lloyd's to exercise any discretion, power or authority conferred on it;

“**EIOPA**” means the European Insurance and Occupational Pensions Authority;

“**Equitas reinsurance contract**” means a reinsurance contract entered into pursuant to paragraph 4(1) of the Reconstruction and Renewal Byelaw (No. 22 of 1995) made by the Council of Lloyd's;

“**Event of Default**” has the meaning given in Condition 10.1;

“**Excluded Payment**” means any application of the New Central Fund directly for the purpose of extinguishing or reducing any liability of a member in respect of which Equitas Insurance Limited, or any successor thereto, has, under an Equitas reinsurance contract, undertaken to reinsure and indemnify that member other than a payment made by the Issuer to discharge any legally binding obligation of the Issuer arising under a contract entered into or other instrument executed at or before the time at which the New Central Fund Byelaw came into force;

“**Extraordinary Resolution**” has the meaning given in the Trust Deed;

“**Financial Conduct Authority**” or “**FCA**” means the UK Financial Conduct Authority or its successor;

“**Financial Statements**” means the audited or, if not audited, the reviewed and reported upon financial statements of Lloyd's comprising the Lloyd's market aggregate accounts and the accounts of the Issuer and the Central Fund;

“**First Call Date**” means 7 February 2027;

“**Fixed Interest Payment Date**” means 7 February in each year, from (and including) 7 February 2018 up to (and including) the First Call Date;

“**Fixed Interest Rate**” has the meaning given in Condition 4.4;

“**Floating Interest Payment Date**” means 7 February, 7 May, 7 August and 7 November in each year, from (and including) 7 May 2027 up to (and including) the Maturity Date, save that if any such Floating Interest Payment Date would otherwise fall on a day which is not a Business Day, such Floating Interest Payment Date shall be postponed to the following Business Day, unless it would thereby fall into the next calendar month, in which event such Floating Interest Payment Date shall be brought forward to the immediately preceding Business Day;

“**Floating Interest Rate**” has the meaning given in Condition 4.5;

“**FSMA**” means the Financial Services and Markets Act 2000 (as amended or re-enacted from time to time);

“**holder**” has the meaning given in Condition 1.2;

“**Insolvent Member**” means any member of Lloyd’s who or which is determined by the Issuer, or by such other person who under applicable law or regulation has the authority, power or discretion to make payments out of Central Assets in a winding-up of the Issuer, to be unable to pay its liabilities in full arising out of or in connection with its insurance business at Lloyd’s;

“**Interest Determination Date**” means, with respect to an Interest Period commencing on or after the First Call Date, the first day of such Interest Period;

“**Interest Payment Date**” means each Fixed Interest Payment Date and each Floating Interest Payment Date, as the context permits;

“**Interest Period**” means the period from (and including) one Interest Payment Date (or in the case of the first Interest Period, from the Issue Date) to (but excluding) the next (or in the case of the first Interest Period, the first) Interest Payment Date;

“**Interest Rate**” means the Fixed Interest Rate or the Floating Interest Rate, as the case may be;

“**Issue Date**” means 7 February 2017;

“**Issuer**” or “**Lloyd’s**” means the Society of Lloyd’s;

“**Junior Securities**” has the meaning given in Condition 3.2(b);

“**Liabilities**” means the unconsolidated gross liabilities of the Issuer as of the date of the latest published audited financial statements of the Issuer, but adjusted for contingent liabilities and for subsequent events in such manner as the Council of Lloyd’s may determine;

“**Lloyd’s market**” means the “association of underwriters known as Lloyd’s”, as such term is used in Article 8 of Directive 72/239/EEC and Article 8 of Directive 79/267/EEC;

“**London Stock Exchange**” means the London Stock Exchange plc;

“**Mandatory Interest Deferral Date**” means each Interest Payment Date in respect of which a Regulatory Deficiency Interest Deferral Event has occurred and is continuing or would occur if payment of interest was made on such Interest Payment Date;

“**Margin**” means 4.479 per cent. per annum;

“**Maturity Date**” means the Interest Payment Date falling in February 2047;

“**member of Lloyd’s**” or “**member**” means any current or former member of Lloyd’s or the estate of any deceased member of Lloyd’s;

“**Member State**” means a member of the European Economic Area;

“**Minimum Capital Requirement**” means the Minimum Capital Requirement applicable to the Issuer referred to in, or any other minimum capital requirement howsoever described in, the Relevant Rules;

“**New Central Fund**” has the meaning given in the definition of Central Fund;

“**New Central Fund Byelaw**” means the New Central Fund Byelaw (No. 23 of 1996) made by the Council of Lloyd’s, as amended or superseded from time to time;

“**Noteholder**” has the meaning given in Condition 1.2;

“**Notes**” has the meaning given in the preamble to these Conditions;

“**Official List**” means the official list of the UK Listing Authority;

“**Optional Interest Payment Date**” means any Interest Payment Date other than a Compulsory Interest Payment Date or a Mandatory Interest Deferral Date;

“**Paying Agents**” means the Principal Paying Agent and the Registrar (and such term shall include any successor, replacement or additional paying agents appointed under the Agency Agreement);

“**Pari Passu Creditors**” means creditors of the Issuer whose claims rank, or are expressed to rank, *pari passu* with the claims of the Noteholders including holders of Pari Passu Securities;

“**Pari Passu Securities**” has the meaning given in Condition 3.2(b);

“**Permitted Purpose**” means, in relation to a Central Assets Priority Payment, a payment other than an Excluded Payment which is made for the purpose of:

- (i) directly or indirectly extinguishing or reducing any liability of an Insolvent Member to any person (including without limitation to a policyholder under a contract of insurance or reinsurance or to any regulatory authority in respect of any levy imposed by that authority on the Insolvent Member) arising out of or in connection with insurance business carried on at Lloyd’s by that Insolvent Member; or
- (ii) paying the costs or expenses attributable to any insolvency procedure involving the Issuer, the Lloyd’s market or members of Lloyd’s;

“**Principal Paying Agent**” has the meaning given in the preamble to these Conditions;

“**Qualifying Tier 2 Securities**” means securities issued directly or indirectly by the Issuer that:

- (a) have terms not materially less favourable to an investor than the terms of the Notes (as reasonably determined by the Issuer, and provided that a certification to such effect signed by two Authorised Signatories shall have been delivered to the Trustee (upon which the Trustee shall be entitled to rely without liability to any person) prior to the issue of the relevant securities) provided that they shall (1) contain terms which comply with the then current requirements of the Relevant Regulator in relation to Tier 2 Capital; (2) bear at least the same Interest Rate from time to time applying to the Notes and preserve the same Interest Payment Dates; (3) contain terms providing for optional and mandatory deferral of payments of interest and/or mandatory deferral of payments of principal only if such terms are not materially less favourable to an investor than the respective deferral provisions contained in the terms of the Notes; (4) rank senior to, or *pari passu* with, the ranking of the Notes; (5) preserve the obligations (including the obligations arising from the exercise of any right) of the Issuer as to redemption of the Notes, including (without limitation) as to timing of, and amounts payable upon, such redemption; (6) (where the securities are issued prior to the First Call Date) have the same first call date as the Notes; (7) not contain terms providing for, requiring or entitling the Issuer to effect loss absorption through principal write-down; and (8) preserve any existing rights under these Conditions to any accrued interest, any Arrears of Interest and any other amounts payable under the Notes which, in each case, has accrued to Noteholders and not been paid; and
- (b) are listed or admitted to trading on the London Stock Exchange’s regulated market (for the purposes of Directive 2004/39/EC, as amended), the Luxembourg Stock Exchange’s regulated market (for the purposes of Directive 2004/39/EC, as amended) or such other stock exchange as is a Recognised Stock Exchange at that time as selected by the Issuer and approved by the Trustee;

“**Rating Agency**” means Standard & Poor’s Credit Market Services Europe Limited or Fitch Ratings Limited or any of their respective successors thereof;

“**Rating Agency Compliant Securities**” means securities issued directly or indirectly by the Issuer that are:

- (a) Qualifying Tier 2 Securities; and
- (b) assigned by each Rating Agency substantially the same equity content or, at the absolute discretion of the Issuer, a lower equity content (provided such equity content is still higher than the equity content assigned to the Notes after the occurrence of the Ratings Methodology Event) as that which was assigned by the relevant Rating Agency to the Notes on or around the Issue Date and provided that a certification to such effect of two Authorised Signatories shall have been delivered to the Trustee prior to the issue of the relevant securities (upon which the Trustee shall be entitled to rely without liability to any person);

“**Ratings Methodology Event**” will be deemed to occur upon a change in, or clarification to, the methodology of any Rating Agency (or in the interpretation of such methodology) as a result of which the equity content assigned by such Rating Agency to the Notes is, as notified by the relevant Rating Agency to the Issuer or as published by the relevant Rating Agency, reduced when compared to the equity content assigned by the relevant Rating Agency to the Notes on or around the Issue Date;

“**Recognised Stock Exchange**” means a recognised stock exchange as defined in section 1005 of the Income Tax Act 2007 as amended or re-enacted from time to time, and any provision, statute or statutory instrument replacing the same from time to time;

“**Reference Banks**” means the principal London office of four major banks in the London interbank market, as selected by the Issuer, or by the Issuer in consultation with the Agent Bank;

“**Reference Bank Rate**” means, with respect to an Interest Period commencing on or after the First Call Date and its related Interest Determination Date, the percentage rate determined on the basis of the offered quotations provided by the Reference Banks to the Agent Bank at approximately 11:00 hours (London time) on the Interest Determination Date, for deposits for three months in sterling commencing on the relevant Interest Determination Date to prime banks in the London interbank market and in a principal amount that is representative for a single transaction in sterling in that market at that time. If at least two quotations are provided, the Reference Bank Rate will be the arithmetic mean of those quotations provided. If only one quotation is provided, the Reference Bank Rate will be that quotation provided. If no quotation is provided, the Reference Bank Rate for such Interest Period will be the 3-month LIBOR Rate applicable to the immediately preceding Interest Period, or in the case of the Interest Period commencing on the First Call Date, 0.35713 per cent;

“**Register**” has the meaning given in Condition 1.1;

“**Registrar**” has the meaning given in the preamble to these Conditions;

“**Regulatory Capital Requirements**” means any applicable capital resources requirement or applicable overall financial adequacy rule required by the Relevant Regulator, as such requirements or rule are in force from time to time;

“**Regulatory Clearance Condition**” means, in respect of any proposed act on the part of the Issuer, the Relevant Regulator having approved or consented to, or having been given due notification of and having not within any applicable time-frame objected to, such act (in any case only if and to the extent required by the Relevant Rules, the Relevant Regulator or any applicable rules of the Relevant Regulator at the relevant time);

“**Regulatory Deficiency Interest Deferral Event**” means any event (including, without limitation, any event which causes the Solvency Capital Requirement or the Minimum Capital Requirement to be breached and such breach is an event) which under the Relevant Rules would require the Issuer to defer payment of interest

in respect of the Notes (on the basis that the Notes are intended to qualify as Tier 2 Capital of the Issuer under the Relevant Rules);

“**Regulatory Deficiency Redemption Deferral Event**” means any event (including, without limitation, causes the Solvency Capital Requirement or the Minimum Capital Requirement to be breached and such breach is an event) which under the Relevant Rules would require the Issuer to defer or suspend repayment or redemption of the Notes (on the basis that the Notes are intended to qualify as Tier 2 Capital of the Issuer under the Relevant Rules);

“**Relevant Date**” means the date on which the payment first becomes due but, if the full amount of the money payable has not been received by an Agent or the Trustee on or before the due date, it means the date on which, the full amount of the money having been so received, notice to that effect has been duly given to the Noteholders by the Issuer in accordance with Condition 12;

“**Relevant Jurisdiction**” means the United Kingdom or any political subdivision or any authority thereof or therein having power to tax or any other jurisdiction or any political subdivision or any authority thereof or therein having power to tax to which the Issuer becomes subject in respect of payments made by it of principal and interest (including Arrears of Interest) on the Notes;

“**Relevant Regulator**” means the UK Prudential Regulation Authority or such successor or other authority having primary supervisory authority with respect to prudential matters in relation to the Issuer;

“**Relevant Rules**” means, at any time, any legislation, rules or regulations (whether having the force of law or otherwise) then applying to the Issuer relating to own funds, capital resources, capital requirements, financial adequacy requirements or other prudential matters (including, but not limited to, the characteristics, features or criteria of any of the foregoing) and, for the avoidance of doubt and without limitation to the foregoing, includes (to the extent then applying as aforesaid) Solvency II and any legislation, rules or regulations of the Relevant Regulator relating to such matters;

“**Screen Page**” means Reuters screen LIBOR01 or such other page as may replace it on Thomson Reuters, or as the case may be, on such other information service that may replace Thomson Reuters, as may be nominated by the person providing or sponsoring the information appearing there for the purpose of displaying rates comparable to the 3-month LIBOR Rate;

“**Senior Creditors**” means at any time

- (a) all creditors of the Issuer (including prospective creditors and contingent creditors and, without limitation, any persons to whom the costs or expenses attributable to any insolvency procedure involving the Issuer, the Lloyd’s market or any participants within the Lloyd’s market are payable), other than
  - (i) creditors (if any) whose claims rank or are expressed to rank *pari passu* (whether only in the event of a winding-up of the Issuer or otherwise) with the claims of Noteholders;
  - (ii) creditors (if any) with or to whose claims the Notes rank or are expressed to rank *pari passu* or senior (whether only in the event of the winding-up of the Issuer or otherwise); and
  - (iii) creditors, including pursuant to any loans made by members after the Issue Date, whose claims rank or are expressed to rank junior (whether only in the event of the winding-up of the Issuer or otherwise) to the claims of the Noteholders; and
- (b) all persons in respect of whom a Central Fund Undertaking has been made and all persons who in a winding-up of the Issuer may receive or are entitled to receive a Central Assets Priority Payment;

“**Solvency II**” means the Solvency II Directive and any implementing measures adopted pursuant to the Solvency II Directive (for the avoidance of doubt, whether implemented by way of EIOPA guidelines, regulation (including, without limitation, the Solvency II Regulation) or by further directives or otherwise);

“**Solvency II Directive**” means Directive 2009/138/EC of the European Union (as amended) on the taking-up and pursuit of the business of insurance and reinsurance (Solvency II) and transposed by Member States pursuant to Article 309 of Directive 2009/138/EC;

“**Solvency II Regulation**” means Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking up and pursuit of the business of insurance and reinsurance (Solvency II);

“**Solvency Capital Requirement**” means the Solvency Capital Requirement referred to in, or any other capital requirement howsoever described in, the Relevant Rules in relation to (i) the Lloyd’s market as a whole (but not individual syndicates or members) or (ii) to the Central Assets of the Issuer;

“**Solvent**” means that the Issuer: (a) is able to pay its debts owed to its Senior Creditors and Pari Passu Creditors as they fall due; and (b) has Assets exceeding its Liabilities (other than Liabilities to persons who are not Senior Creditors);

“**sterling**” or “**pence**” or “**£**” means the lawful currency of the United Kingdom;

“**T1 Notes**” means the outstanding 7.421 per cent. Perpetual Subordinated Capital Securities issued by the Issuer on 21 June 2007;

“**T2 Notes**” means the outstanding 4.75 per cent. Fixed Rate Subordinated Notes due 2024 issued by the Issuer on 30 October 2014;

“**Tax Law Change**” means a change in or proposed change in, or amendment or proposed amendment to, the laws or regulations of the United Kingdom or any political subdivision or authority therein or thereof having the power to tax, including any treaty to which the United Kingdom is a party, or any change in the application of official or generally published interpretation of such laws, including a decision of any court or tribunal, or any interpretation or pronouncement by any relevant tax authority that provides for a position with respect to such laws or regulations that differs from the previously generally accepted position in relation to similar transactions or which differs from any specific written statements made by a tax authority regarding the anticipated tax treatment of the Notes or any payment made under these Conditions, which change or amendment becomes, or would become, effective on or after the Issue Date;

“**Taxes**” has the meaning given in Condition 8;

“**Tier 1 Capital**” has the meaning given by the Relevant Regulator from time to time in relation to the Issuer;

“**Tier 2 Capital**” has the meaning given by the Relevant Regulator from time to time in relation to the Issuer;

“**Trust Deed**” has the meaning given in the preamble to these Conditions;

“**Trustee**” has the meaning given in the preamble to these Conditions; and

“**UK Listing Authority**” means the FCA in its capacity as competent authority under the Financial Services and Markets Act 2000.

## **SUMMARY OF PROVISIONS RELATING TO THE NOTES WHILE IN GLOBAL FORM**

### **Initial Issue of Certificates**

The Global Certificate will be registered in the name of a nominee (the “**Registered Holder**”) for the Common Depositary for Euroclear and Clearstream, Luxembourg and may be delivered on or prior to the original issue date of the Notes.

Upon the registration of the Global Certificate in the name of any nominee for Euroclear and Clearstream, Luxembourg and delivery of the Global Certificate to the Common Depositary, Euroclear or Clearstream, Luxembourg will credit each subscriber with a nominal amount of Notes equal to the nominal amount thereof for which it has subscribed and paid.

### **Relationship of Accountholders with Clearing Systems**

Each of the persons shown in the records of Euroclear, Clearstream, Luxembourg or any other clearing system (an “**Alternative Clearing System**”) as the holder of a Note represented by a Global Certificate must look solely to Euroclear, Clearstream, Luxembourg or any such Alternative Clearing System (as the case may be) for his share of each payment made by the Issuer (as the case may be) to the Registered Holder and in relation to all other rights arising under the Global Certificate, subject to and in accordance with the respective rules and procedures of Euroclear, Clearstream, Luxembourg or such Alternative Clearing System (as the case may be). Such persons shall have no claim directly against the Issuer in respect of payments due on the Notes for so long as the Notes are represented by the Global Certificate and such obligations of the Issuer will be discharged by payment to the Registered Holder in respect of each amount so paid.

### **Transfer and Exchange**

No beneficial owner of an interest in a Global Certificate will be able to transfer such interest, except in accordance with the applicable procedures of Euroclear and Clearstream, Luxembourg, in each case to the extent applicable.

Interests in the Global Certificate will be exchangeable (free of charge), in whole but not in part, for definitive Certificates without interest coupons attached only upon the occurrence of an Exchange Event. For these purposes, **Exchange Event** means that (i) an Event of Default has occurred and is continuing or (ii) the Issuer has been notified that both Euroclear and Clearstream, Luxembourg have been closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or have announced an intention permanently to cease business or have in fact done so. The Issuer will promptly give notice to Noteholders in accordance with Condition 12 if an Exchange Event occurs. In the event of the occurrence of an Exchange Event, Euroclear and/or Clearstream, Luxembourg or any person acting on their behalf (acting on the instructions of any holder of an interest in such Global Certificate) may give notice to the Registrar requesting exchange. Any such exchange shall occur not later than 10 days after the date of receipt of the first relevant notice by the Registrar.

Any reference herein to Euroclear and/or Clearstream, Luxembourg shall, whenever the context so permits, be deemed to include a reference to any Alternative Clearing System.

### **Amendment to Conditions**

The Global Certificate contains provisions that apply to the Notes that it represents, some of which modify the effect of the Conditions set out in this Prospectus. The following is a summary of certain of those provisions:

### **Payments**

All payments in respect of Notes represented by a Global Certificate will be made to, or to the order of, the person whose name is entered on the Register at the close of business on the record date which shall be on the Clearing System Business Day immediately prior to the date for payment, where “**Clearing System Business Day**” means Monday to Friday inclusive except 25 December and 1 January.

### **Calculation of interest**

Notwithstanding the provisions of Condition 4.3, for so long as all of the Notes are represented by the Global Certificate, interest shall be calculated on the aggregate principal amount of the Notes represented by the Global Certificate (and not per £1,000 in principal amount), but otherwise shall be calculated in accordance with Condition 4.

### **Notices**

So long as all the Notes are represented by the Global Certificate and it is held on behalf of Euroclear, Clearstream, Luxembourg and/or an Alternative Clearing System, notices to Noteholders shall be given by delivery of the relevant notice to Euroclear, Clearstream, Luxembourg and/or the Alternative Clearing System (as the case may be) for communication by it to entitled accountholders in substitution for notification as required by the Conditions, provided that, so long as the Notes are admitted to the official list maintained by the Financial Conduct Authority in its capacity as the UK Listing Authority (the “UKLA”) and admitted to trading on the London Stock Exchange plc’s regulated market, all requirements of the UKLA have been complied with. Any such notice shall be deemed to have been given to the Noteholders on the day on which such notice is delivered to Euroclear, Clearstream, Luxembourg and/or the Alternative Clearing System (as the case may be) as aforesaid.

### **Meetings**

For the purposes of any meeting of Noteholders, the holder of the Notes represented by the Global Certificate shall be treated as being entitled to one vote in respect of each £1,000 in principal amount of the Notes.

### **Trustee’s Powers**

In considering the interests of Noteholders while the Global Certificate is held on behalf of, or registered in the name of any nominee for, a clearing system, the Trustee may have regard to any information provided to it by such clearing system or its operator as to the identity (either individually or by category) of its accountholders with entitlements to the Global Certificate and may consider such interests as if such accountholders were the holders of the Notes represented by the Global Certificate.

## **USE OF PROCEEDS**

The net proceeds of the issue of the Notes will be used to provide the Issuer with additional solvency capital to meet regulatory capital requirements and for general corporate purposes.

## THE SOCIETY OF LLOYD'S

### History

The Lloyd's market originated in a coffee house in the City of London in the late 17th century. For over 300 years, it has been a market place at which businesses underwrite insurance business for their own account.

In 1871, pursuant to Lloyd's Act 1871, the then existing association of underwriters was incorporated as the Society and Corporation of Lloyd's (the "**Society**"). The activities of the Society are accordingly governed by statute and, since 1982, have been managed by 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.

### Lloyd's market

#### General

References are made below to the Society's pro forma financial statements (the "**Pro Forma Financial Statements**" or "**PFFS**"). The Pro Forma Financial Statements provide financial information in relation to the Lloyd's market (also taking account of the Society's own assets). Investors should have regard to the Society's audited accounts for information on the Society's own financial position. The Pro Forma Financial Statements and the Society's 2014 and 2015 financial statements, the Pro Forma Financial Statements and the Society's financial statements for the six month period ending 30 June 2016 and the interim management statement of the Issuer's group for the nine months ended 30 September 2016 are available on [www.lloyds.com](http://www.lloyds.com) and incorporated by reference herein. See also "*Annual Accounting*" below.

The underwriting members of Lloyd's (referred to collectively as the "**Lloyd's market**") write business through syndicates and together form one of the world's largest specialist commercial insurers and reinsurers, reporting Gross Written Premiums of £26.7 billion in the financial year ending 31 December 2015 (based on the Society's Pro Forma Financial Statements for 2015) (the "**2015 PFFS**"). In the same year the capital, reserves and subordinated debt and securities supporting the Lloyd's market increased to £25.1 billion (based on the 2015 PFFS). This figure includes the net resources of the Society excluding liabilities for the following existing debt securities:

- The £500,000,000 7.421 per cent. Perpetual Subordinated Capital Securities with a first call date of 21 June 2017, of which £392,013,000 principal amount remains outstanding (the "**2007 Notes**"); and
- The £500,000,000 4.750 per cent. Subordinated Notes (the "**2014 Notes**").

Profit before tax reported for the Lloyd's market for the financial year ended 31 December 2015 was £2.1 billion (based on the 2015 PFFS).

Gross Written Premiums were £16.3 billion (based on the Society's Pro Forma Financial Statements for the six month period ended 30 June 2016) (the "**interim 2016 PFFS**"). In the same period, the capital reserves and subordinated debt and securities supporting the Lloyd's market (including the net resources of the Society excluding liabilities for the 2007 Notes and 2014 Notes) were £26.6 billion (based on the interim 2016 PFFS). Profit before tax reported for the Lloyd's market for the same period was £1.5 billion (based on the interim 2016 PFFS).

The Lloyd's market combined ratio as further described below under "*Profitability of different sectors*" worsened from 88.4% in 2014 to 90.0% in 2015, reflecting the continuing challenging conditions in the property and casualty insurance market and the ongoing pressure on premium rates. The combined ratio as at 30 June 2016 was 98.0% (based on the interim 2016 PFFS).

Standard and Poor's current insurer financial strength rating of the Lloyd's market is A+ (Strong) with a stable outlook. Fitch's current insurer financial strength rating of the Lloyd's market is AA- (Very Strong) with a stable outlook. A.M. Best's current insurer financial strength rating of the Lloyd's market is A

(Excellent) with a stable outlook. The Lloyd's market ratings apply to all policies issued at Lloyd's since 1993.

The Lloyd's market writes a broad portfolio of general insurance and reinsurance business and is authorised to underwrite business in over 80 jurisdictions, giving syndicates access to insurance markets all over the world. Lloyd's also benefits from its position at the heart of the London insurance market. The proximity of major broking houses to Lloyd's and the concentration of underwriting expertise ensures a strong business flow.

*Lloyd's market performance, 2011 to 30 June 2016*

	2011	2012	2013	2014	2015	H1 2016
Pre-tax result (£bn)	(0.5)	2.8	3.2	3.0	2.1	1.5
Combined ratio (%)	106.8	91.1	86.8	88.4	90.0	98.0
Investment return <sup>1</sup> (%)	1.9	2.6	1.6	2.0	0.7	1.8
Gross written premium (£bn)	23.3	25.2	25.6	25.3	26.7	16.3
Net resources (£bn)	19.1	20.2	21.1	23.4	25.1	26.6
Pre-tax Return on Capital <sup>2</sup> (%)	-2.8	14.8	16.2	14.1	9.1	11.7
Pre-tax Return on Capital 5 year average (%)					10.4	
Pre-tax Return on Capital 10 year average					14.9	

Source: Lloyd's pro forma financial statements

Note: 1) Actual return for the period; Return on syndicates' assets, members' funds at Lloyd's and central assets in aggregate; 2) Annualised basis

**Categories of business**

The business carried on by the Lloyd's market falls into a number of categories, as indicated in the table below. The table sets out the Gross Written Premiums (prior to the deduction of reinsurance premium and brokerage) by business class during the financial year ended 31 December 2015, based on the 2015 PFFS.

**Gross Written Premiums (£million)**

Category of Insurance	2015	2014
Reinsurance .....	8,593	8,488
Property .....	6,893	6,274
Casualty <sup>(1)</sup> .....	5,764	4,959
Marine .....	2,245	2,140
Energy .....	1,414	1,532
Motor .....	1,120	1,213
Aviation .....	587	581
Life .....	74	72
TOTAL .....	26,690	25,259

<sup>(1)</sup> This covers professional indemnity, directors' and officers' liability, medical malpractice, employers' liability/workers' compensation, accident and health and other general liability business.

### ***Geographical split***

The geographical split in terms of premium income by the Lloyd's market for the financial year ended 31 December 2015 was as follows:

#### **Premium income %**

<i>Region</i>	<i>2015</i>
United States & Canada .....	47%
United Kingdom .....	18%
Rest of Europe .....	14%
Central Asia and Asia Pacific.....	10%
Other Americas .....	7%
Rest of the World .....	4%

### ***Profitability of different sectors***

The 2015 PFFS reported profit before tax for the Lloyd's market of £2.1 billion and the table below illustrates the profitability of the main business sectors for the financial year ended 31 December 2015. The "combined ratio" is a measure of an insurer's profitability based on the ratio of net incurred claims plus net operating expenses to net earned premiums. A combined ratio of 100% is a break even result from underwriting activities (before taking into account investment income). A ratio of over 100% is an underwriting loss. The Lloyd's market overall combined ratio for 2015 calendar year was 90.0% (this includes central adjustments made in the 2015 PFFS for certain transactions between syndicates and the Society which are disclosed in the notes to the 2015 PFFS). As indicated by the table, the combined ratios for individual classes of business (which do not include central adjustments) show that all business sectors except Motor and Casualty were profitable in 2015. All other classes were profitable based on strong underlying performance and the comparatively low major catastrophe experience in 2015. During 2015 in aggregate, claims development in respect of reserves established at December 2014 has been better than projected, leading to a 7.9% improvement within the above-mentioned Lloyd's market overall combined ratio for 2015. Gross written premiums for the six months to June 2016 were £16.31 billion (June 2015: £15.51 billion) representing an increase of 5% year-on-year. After adjusting for the impact of foreign exchange rate movements the underlying increase in gross written premium was 0.6%. Rates have continued to decline, however these have been offset by increases in volume.

The investment environment and resulting returns in 2015 were dominated by events in the second half of the year with the economic slowdown in China and fall in oil prices. Risk assets generally suffered amidst the market turbulence but returns varied by asset type. In aggregate, for 2015 syndicate investment returns were 0.8%, returns on members' capital held centrally by the Society were 0.5% and the return on the Society's central assets was 1.5%. Over the nine months to 30 September 2016 the Society's investments returned £239 million, or 7.9%, a significant improvement on the same period in 2015.

### **Combined Ratio**

#### *Category of insurance*

	<b>2015</b>	<b>2014</b>
	<b>(%)</b>	<b>(%)</b>
Reinsurance .....	86.7	81.3
Property .....	90.1	87.4
Casualty .....	100.1	97.9
Marine .....	94.2	95.2
Energy .....	76.0	82.7
Motor .....	102.0	106.4
Aviation .....	95.7	102.1

### ***Comparative profitability***

The table below compares the combined ratios for the Lloyd's market in the 2015 and 2014 calendar years (derived from the 2015 and 2014 PFFS) against those of its primary competitor group.

	<b>Combined Ratio YE 2015 (%)</b>	<b>Combined Ratio YE 2014 (%)</b>
Lloyd's market .....	90	88
Primary competitor group .....	95	92

- (i) This competitor group is derived from the ratings agencies' own Lloyd's competitor groups and comprises of: Arch, AIG, ACE, Everest Re, Munich Re, Partner Re, Hannover Re, SCOR, Swiss Re, Mapfre and XL.
- (ii) The competitor group's results are derived from the weighted average published results of these companies for the period ending 31 December 2015.
- (iii) For the 6 months to June 2016 the Lloyd's market combined ratio of 98% exceeded that of the competitor group (95%) for the first time since 2011, due to an increase in attritional loss ratios, an increase in catastrophe losses (from an extremely low level in 2015) and a reduction in reserve releases (from an extremely high level in 2015).

### ***Lloyd's major losses: net ultimate claims, £ million***

The table below shows net ultimate claims for each of the years listed for the Lloyd's market. Net ultimate claims represent the total sum the entity expects to pay for a fully developed loss (i.e., paid losses plus outstanding reported losses and incurred but not reported losses) less the amounts it expects to recover from its reinsurers.

2000	284
2001	3,565
2002	329
2003	183
2004	1,672
2005	4,402
2006	60
2007	573
2008	1,933
2009	383
2010	2,364
2011	4,855
2012	1,875
2013	888
2014	671
2015	724

*Note: Indexed for inflation to 2015. Claims in a foreign currency translated at the exchange rates at the date of loss.*

### ***Lloyd's market profile***

The Lloyd's market wrote £26.7 billion Gross Written Premiums in 2015. This has increased over the years and compares with Gross Written Premiums of £16.4 billion in 2006.

### ***Membership profile***

Insurance is underwritten at Lloyd's by members of Lloyd's (comprising corporate members and individual members). No new individual members have been permitted to join Lloyd's since 2003.

Prior to 1994, all Lloyd's members were individuals. Corporate membership was introduced in 1994. The number of individual members has reduced steadily since this time whilst the number of corporate members has increased. 89% of capacity in 2015 is supported by corporate capital.

A significant proportion of the Lloyd's market corporate member capacity comes from the major global insurance centres of the UK, US, Japan and Bermuda. Insurance and reinsurance companies have operations at Lloyd's representing approximately 86% of the market's capacity.

## **Structure of Lloyd's market**

### ***Syndicates and members of Lloyd's***

Members underwrite insurance business through syndicates. A syndicate is managed by a managing agent (see "*Managing Agents*" below). A syndicate may have a number of members who may be individual and/or corporate members. A syndicate does not have any legal status and is not a partnership.

Between the early 1990's and mid 2000's, the number of active syndicates reduced but generally grew in size and increasingly transformed from single-line to multi-line businesses. Since 2004, participation by external, non-traditional capital providers has resulted in an increase in the number of syndicates. As at 30 June 2016, there were 84 syndicates and 15 Special Purpose Arrangements writing business at Lloyd's.

Where a corporate member participating in, and a managing agent of, a syndicate are owned by the same company or are part of the same corporate group, the corporate member is said to be "aligned". Some corporate members and individual members have no ownership links with managing agents and are therefore "unaligned".

Each syndicate is an annual venture through which members participate for a specific "year of account". However, the annual venture concept is more relevant for syndicates whose composition changes from year to year than it is for the syndicates which are aligned.

A member does not have joint liability with any other member of a syndicate for risks underwritten through that syndicate, but is severally liable in respect of the proportion of each risk underwritten on its behalf as a member of the syndicate. Members do not have liability for business underwritten by the same syndicate in previous years of account unless they were members in those years or unless they have reinsured the members of that syndicate for the previous years. It is usual for the liabilities of the members of a syndicate for a year of account to be reinsured in full with effect from the end of three years through reinsurance to close (see "*Reinsurance to Close*" below).

### ***Managing Agents***

As at 30 June 2016, there were 58 managing agents permitted to operate at Lloyd's and manage syndicates for the 2016 year of account. The role of the managing agent includes determination of the underwriting strategy of any syndicate it manages, the acceptance of underwriting risks on behalf of the syndicate, determination of the syndicate's reinsurance programme, management of the syndicate's investments and the determination of the premium for reinsurance to close (see "*Reinsurance to Close*" below). The business of each managing agent and of the syndicates which they manage is subject to oversight by the Society. In particular, all managing agents must seek the Society's agreement for the proposed business plan for each syndicate that the agent manages and the capital required to support that business plan (see "*Business Planning*"). Managing agents are regulated by the PRA and the FCA.

Members are required to enter into a managing agent's agreement with their managing agent, certain terms of which are prescribed by the Society. In the agreement the member gives the managing agent absolute discretion as to the risks which may be underwritten on behalf of the member and authority to conduct the business of the syndicate.

Under the managing agent's agreement, managing agents have the power to request that members of the syndicate make funds available, where necessary, to enable them to pay all claims and all necessary and

reasonable expenses and outgoings incurred or made in connection with the members' underwriting as members of the syndicates. These are known as cash calls.

Managing agents are also responsible for the maintenance of accounting records and statistical data for the syndicate and for preparing and obtaining the audit of syndicate accounts. Also, pursuant to the Society's accounting requirements, managing agents are required to prepare syndicate returns in respect of each syndicate they manage. The returns must be prepared quarterly and must include details of assets held in accordance with eligible asset rules and estimated future liabilities in accordance with valuation of liabilities rules set by the Society.

The Society requires annual actuarial sign-off of syndicate reserves for solvency purposes and this process is overseen by an actuary employed by the Society. Managing agents are responsible for assessing the estimated future liabilities (reserves) for the syndicate. The majority of managing agents have an actuarial department, headed by a chief actuary, and carry out claims reserving in-house. Despite this the majority of managing agents obtain their actuarial sign-off externally from an actuarial consultancy firm to provide additional assurance and independence on the appropriate levels of technical reserves.

In both cases, a formal certificate and report are required on an annual basis. These must be signed by a qualified actuary possessing a current practising certificate for this role issued by the Institute and Faculty of Actuaries (a "signing actuary"). The signing actuary must review the reserves (both gross and net of reinsurance) of each open year (including years that have been reinsured to close) and provide an opinion confirming that the reserves for each open year which form the technical provisions for solvency are at least equal to their best estimate of the amounts required.

*Top 10 managing agents by 2016 half-year premium and market share in Lloyd's*

Rank	Top 10 Managing Agents	2016 half-year GWP (£m)	Share of Lloyd's %
1	Catlin Underwriting Agencies Limited	1,284	8%
2	MS Amlin Underwriting Limited	1,153	7%
3	Beazley Furlonge Limited	887	5%
4	Hiscox Syndicates Limited	864	5%
5	Tokio Marine Kiln Syndicates Limited	811	5%
6	Liberty Managing Agency Limited	797	5%
7	QBE Underwriting Limited	772	5%
8	Brit Syndicates Limited	719	4%
9	Canopus Managing Agents Limited	621	4%
10	Asta Managing Agency Limited	604	4%
	Other	7,795	48%

*Lloyd's managing agents as a proportion of Lloyd's 2016 half-year total gross written premiums of £16,307 million excluding syndicates set up as Special Purpose Arrangements.*

### **Brokers, Underwriting & Claims**

Insurance business is generally brought to managing agents of syndicates through Lloyd's brokers – insurance broking firms registered by the Society, to broke their clients' insurance business at Lloyd's. In order to be registered as a Lloyd's broker, brokers need to meet certain entry criteria set by the Society. In particular, the Society requires all Lloyd's brokers to be authorised by the FCA or registered with a competent authority elsewhere in the EU. Non-EU based Lloyd's brokers will need to comply with equivalent standards. In addition, they also need to show that they have the ability to transact and process Lloyd's market business. As at 30 June 2016 there were 254 Lloyd's brokers. Managing agents may also accept business from brokers who are not registered Lloyd's brokers. The Society has prescribed requirements to ensure that managing agents apply the same prudential standards that are required of Lloyd's brokers to any non-Lloyd's brokers with whom they directly deal.

Risks placed at Lloyd's will be allocated, and all premiums and claims attributed, to the year of account corresponding to the calendar year in which the relevant insurance contract or binding authority incepts.

A risk is sometimes placed with a number of syndicates, with the managing agent of one syndicate acting as the lead underwriter and generally having responsibility for setting the premium rate, approving the policy wording and usually underwriting the largest "line" (percentage) of the risk. Generally, the lead underwriter will accept or reject a claim on behalf of its own syndicate. In the case of standard claims, the lead underwriter will also act on behalf of the following syndicates to accept or reject claims. In the case of complex claims, the underwriter for the lead syndicate, together with the underwriter for the second following syndicate, will act jointly on behalf of the following syndicates to accept or reject claims.

### ***Coverholders***

A coverholder is a business authorised by a managing agent to accept insurance risks on behalf of a syndicate. The managing agent enters into a contract known as a binding authority with a coverholder under which the Lloyd's managing agent delegates its authority to enter into contracts of insurance to be underwritten by the members of a syndicate. Coverholders are a key distribution channel, offering a local route to the Lloyd's market in many insurance markets around the world. As at 30 June 2016, there were 3,741 coverholders.

A service company operates like a coverholder but is a wholly owned subsidiary of a managing agent or its group. As at 30 June 2016, there were 376 service companies, the majority of which are based in the UK, the US and Singapore.

### ***Reinsurance to Close***

Normally each syndicate year of account is kept open for three years, at the end of which it is closed by reinsurance into the next year of account of the syndicate ("**Reinsurance to Close**" or "**RITC**"). This later year takes over all liabilities and related claims handling costs of the closing year of account in return for a premium. Occasionally, a year of account may be reinsured by a different syndicate. The premium for the reinsurance to close is determined by reference to the estimated outstanding liabilities (including claims incurred but not reported), net of estimated collectible reinsurance recoveries and also includes a provision for claims handling costs relating to the closed year of account and all previous years of account.

It may not be possible for a managing agent to close a year of account by RITC due to uncertainty as to the estimated underwriting liabilities and a consequent inability to fix an equitable premium for RITC or because there is no successor year of account to accept the RITC. In these circumstances, closure of the year of account may be delayed. In such circumstance, the Issuer increases its oversight of the managing agent of the syndicate and the managing agent continues to be required to comply with requirements for the preparation of syndicate accounts and returns. At 30 June 2016 there were only four syndicate years of account where no RITC premium could be determined.

### ***Annual Accounting***

The Aggregate Accounts (as defined below) are used in the preparation of the PFFS but are not incorporated by reference herein. They have been prepared in compliance with the Insurance Accounts Directive (Lloyd's Syndicate and Aggregate Accounts) Regulations 2008 ("**the Regulations**"), and in accordance with United Kingdom Accounting Standards, including Financial Reporting Standard 102, 'The Financial Reporting Standard applicable in the United Kingdom and the Republic of Ireland' ("**FRS 102**") and Financial Reporting Standard 103 'Insurance Contracts' ("**FRS 103**"). The Council is required to prepare Aggregate Accounts by totalling all of the syndicate annual accounts prepared under the Regulations. The adoption of annual accounting under UK Generally Accepted Accounting Practice ("**UK GAAP**") does not affect the allocation of profits / losses to members. Members continue to participate on syndicates by reference to years of account and results, assets and liabilities are assessed according to policies incepting in each syndicate year of account for that member's share of each syndicate year of account.

The PFFS have been prepared by aggregating audited financial information reported in syndicate annual accounts ("**Aggregate Accounts**"), members' Funds at Lloyd's ("**FAL**") and the financial statements of the

Society of Lloyd's. The PFFS have not been prepared in accordance with full UK GAAP consolidation principles and do not present a consolidated view of the results of the Lloyd's business taken as a single entity. However, the PFFS may 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.

The syndicates' financial information included in the PFFS has been prepared in accordance with the recognition and measurement requirements of UK GAAP by reference to the accounting policies which are deemed most appropriate by the managing agents. Where different accounting policies have been selected by managing agents in preparing syndicate annual accounts, no adjustments are made to align the bases of recognition and measurement in the PFFS. In addition, no adjustments are made to eliminate inter-syndicate transactions and balances except for those relating to inter-syndicate loans and Special Purpose Arrangements. Transactions between syndicates and the Issuer's group are eliminated in the PFFS.

The Issuer's 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 (various paintings, antiques and artefacts), which are measured at fair value. Loans and receivables and other financial liabilities are carried at amortised cost. The Issuer's group financial statements are presented in sterling and all values are rounded to the nearest thousand (£'000).

## **The Society, The Council and The Franchise Board**

### ***The Society***

The Society is a statutory corporation, not a company incorporated under the Companies Act 2006, and it does not have a registered office. Its head office is located at One Lime Street, London, EC3M 7HA, United Kingdom, telephone number: +44(0) 207 327 1000.

The Society's governing body is the Council, which was established by Lloyd's Act 1982. Under this Act, the Council has the power to manage and supervise the affairs of the Society, to regulate and direct the business of insurance at Lloyd's and to exercise all of the powers of the Society. The Council has power to make such byelaws as it thinks fit to further the objects of the Society.

The Society does not itself underwrite and is not authorised by the PRA to carry on insurance business, however, it is authorised to carry on the regulated activities of: (i) arranging deals in contracts of insurance written at Lloyd's; (ii) arranging deals in participation in Lloyd's syndicates; and (iii) any activities carried on in connection with, or for the purposes of, the activities in (i) and (ii). The external regulation of Lloyd's is described below (see "*External Regulation of the Lloyd's market*"). The principal activities of the Society include authorising and monitoring market participants (including members of Lloyd's and managing agents) and agreeing syndicate business plans, setting capital requirements and monitoring syndicate level systems and controls.

The Society does not have liability for the risks underwritten by its members, although it may at its discretion make its assets (in particular, the Central Fund) available to meet the underwriting liabilities of Lloyd's members where members are unable to meet these liabilities in full. See "*The third link: central resources*" for details of how the Central Fund is operated and applied.

The Society is funded by levying an annual subscription on members and imposing certain other charges on members. The funding arrangements for the Central Fund are discussed below (see "*Funding of the Central Fund*").

### ***The Council***

The members of the Council exercise many functions which are equivalent to those performed by directors of a Companies Act company.

The membership of the Council is divided between “working members”, “nominated members” and “external members”. The Council is required by Byelaw to have a maximum of 18 members with six members falling into each category. Members are generally appointed for three year terms up to a maximum of nine years.

Working members of the Council are persons who are: (a) working members of the Society; and (b) elected as Council members by the working members of the Society. The working members of the Society comprise those members who are or were, immediately before retirement, principally occupied with the conduct of business at Lloyd’s, by a Lloyd’s broker or underwriting agent.

External members of the Council are persons who are: (a) external members of the Society; and (b) elected as Council members by the external members of the Society. External members of the Society are all members of the Society who are not working members.

Nominated members are appointed by the Council.

All appointments to the Council are required to be notified to the PRA and the FCA.

The current Council members, each of whose service address is One Lime Street, London EC3M 7HA, United Kingdom, their functions within the Lloyd’s market and their principal outside activities of significance are as follows:

### ***Planned Council changes***

John Nelson will step down as chairman of Lloyd’s in 2017. The selection process for a new chairman is underway.

Two-thirds of the Council of Lloyd’s are elected from amongst the members of the Society. In accordance with that process the following changes are imminent (as noted above):

Andrew Brooks and Nameco (No 1249) Limited (represented by Jeffrey Barratt) have been elected as new working and external members of the Council respectively and will be starting their first three year term of office on 1 February 2017.

Catlin Syndicate Ltd (represented by Paul Jardine), an external member of the Council, will be stepping down from the Council on 31 January 2017 when its current term of office comes to an end having served 9 years on the Council (the maximum permitted by Lloyd’s rules). An election for the vacancy arising will be held in early 2017.

Lawrence Holder a working member of the Council will be stepping down from the Council on 31 January 2017. He is replaced by Andrew Brooks (above).

### ***Working members***

Simon Beale, Deputy Chairman of Lloyd’s, the Group Chief Underwriting Officer of MS Amlin plc, an Executive Director of the MS Amlin plc board and Non-Executive Director of MS Amlin Underwriting Limited.

Andrew Brooks is Chief Executive Officer of Ascot Underwriting Limited since 2008 and a member of the Board (with effect from 1 February 2017).

Dominic Christian, Executive Chairman of Aon Benfield International and the Chief Executive Officer of Aon UK Limited. He sits on Aon Group’s Executive Committee.

Karen Green, Chief Executive Officer of Aspen UK which includes Aspen Managing Agency Limited and performs a number of other roles within the Aspen Group.

Lawrence Holder, LMA Board member and former Managing Director of Cathedral Underwriting Limited (term ends on 31 January 2017).

Julian James, President Global Markets for Allied World Assurance Company and Chief Executive Officer of Allied World Managing Agency Ltd.

Neil Maidment, Chief Underwriting Officer of Beazley plc and Active Underwriter for its six Lloyd's syndicates, Director of Beazley Furlonge Ltd and Beazley plc.

#### ***External members***

Catlin Syndicate Limited, represented by Paul Jardine. Deputy Chairman of Lloyd's, Executive Vice President and Chief Experience Officer with responsibility for XL Group's Communication & Marketing function, Claims and Distribution Strategy and Deputy Chairman of Catlin Underwriting Agencies Limited, impending CEO subject to regulatory approval. He is also a director of Catlin Insurance Company (UK) Limited, XL Insurance Company SE and a large number of other XL Catlin group UK entities including various service companies. He is a Non-Executive Director of CX Reinsurance Limited (term ends on 31 January 2017).

Flectat Limited, represented by Michael Watson. Chairman of Sompo Canopus AG.

Hiscox Dedicated Corporate Member Limited, represented by Robert Childs. Non-Executive Chairman of Hiscox plc, Hiscox Syndicates Limited, Hiscox Insurance Co Limited, impending Chairman of Hiscox Bermuda Limited and a Director of Hiscox Dedicated Corporate Member Limited.

Nameco (No 1249) Limited, represented by Jeffery Barratt, Consultant at Norton Rose Fulbright LLP, Chairman of TheCityUK's Infrastructure and Energy Executive Board and the Council of the Cook Society. Non-Executive Director of the International Project Finance Association and sits on the London Council and the International Advisory Group of the CBI. He is the Deputy Chairman of the Cook Society. (with effect from 1 February 2017).

Nomina No 115 LLP, represented by Philip Swatman, Non-Executive Chairman of Cambria Automobiles plc and Wyvern Partners.

Novae Corporate Underwriting Limited, represented by Matthew Fosh. Chief Executive Officer of Novae Group plc

#### ***Nominated members***

John Nelson, Chairman of Lloyd's.

Inga Beale DBE, Chief Executive Officer of Lloyd's.

Andy Haste, Senior Independent Deputy Chairman of Lloyd's, Senior Independent Director of ITV plc, Chairman of Wonga Group.

Dr Fred Hu, Chairman of Primavera Capital Group. Non-Executive Director of Hang Seng Bank and the Hong Kong Stock Exchange. Member of the US Council on Foreign Relations' Global Board of Advisors.

Sir David Manning GCMG-KCVO, Director of Gatehouse Advisory Partners, Chair of 'IDEAS' at the London School of Economics, and of Macquarie's Infrastructure and Real Estate Advisory Board. He is on the panel of Senior Advisers at the Royal Institute of International Affairs, Chatham House.

#### ***Potential conflicts of interest between duties to the Issuer and private interests of Council members***

Members of the Council frequently have an involvement in the Lloyd's market and may also come from a particular constituency of the market. Provided that members of the Council do not allow an allegiance to any particular constituency of the market to override their duties to act in the best interests of the Society, they will not be precluded from discussing or voting on a matter simply because it affects the interests of the member's particular constituency. This is subject to compliance with the Society's governance arrangements and requirements on declarations of interest below.

The Society's governance arrangements for members of the Council include provisions on conflicts of interest and declarations of interests. Members of the Council are required to complete an annual declaration of interests. In addition, at any meeting of the Council when the Council is going to discuss a matter in which the member has an interest (whether or not disclosed in the annual declaration), the member must also make a declaration of interest prior to the discussion of that matter. The Chairman of the Council will then consider

whether the member should be precluded from being present during the relevant discussion. The same arrangements are in place for members of the Franchise Board.

Other than as disclosed above, there are no potential conflicts of interest between any duties of members of the Council and their private interests or other duties.

### ***The Franchise Board***

The Council established the Franchise Board in 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 Council has delegated certain of its powers to the Lloyd’s Franchise Board which must operate within the limitations set by the Council which include operating in accordance with the overriding principles (legal, regulatory and corporate governance), capital principles and operating principles (which include setting a market supervision framework in accordance with PRA and/or FCA requirements).

The Franchise Board is chaired by the Chairman of Lloyd’s and has three executive members: the Chief Executive Officer, Performance Management Director and Chief Financial Officer. It also has three non-executive directors connected with the Lloyd’s market and five independent non-executive directors.

The current members of the Franchise Board and their principal business activities are as follows:

John Nelson, Chairman of Lloyd’s.

#### *Independent Non-Executive Directors*

Sir Andrew Cahn KCMG, Non-Executive Director of Nomura International plc, General Dynamics (UK), Huawei Technologies (UK). Chair of WWF (UK) and on the International Board of WWF Trustee of the Gatsby Foundation, the Arvon Foundation and the Institute for Government.

Joy Griffiths, Global Managing Director, Decision Analytics and Chairman, Asia Pacific region, Experian.

Richard Keers, Director and Chief Financial Officer of Schroders plc.

Dr Martin Read CBE, Chairman of Laird plc, Chairman of the Low Carbon Contracts Company and the Electricity Settlements Company, the Independent Chairman of the Remuneration Consultants Group and the UK Government Senior Salaries Review Body.

#### *Market-Connected Non-Executive Directors*

Mark Cloutier Executive Chairman of the Brit Group and serves on the Board of Brit Limited.

Charles Franks, Group Chief Executive Officer of Tokio Marine Kiln Group, Tokio Marine Kiln Syndicates and Tokio Marine Kiln Insurance Limited.

Richard Pryce, Chief Executive Officer of QBE European Operations (with effect from 1 January 2017).

#### *Executive Directors*

Inga Beale DBE, Chief Executive Officer of Lloyd’s.

Jon Hancock, Performance Management Director of Lloyd’s.

John Parry, Chief Financial Officer of Lloyd’s.

### **Managing the Lloyd’s market**

Operating at Lloyd’s provides managing agents and members with immediate benefits including: the Lloyd’s brand, the Lloyd’s market ratings, the mutual security of the Central Fund and access to the Lloyd’s market licences to conduct business in various jurisdictions around the world.

Benefits to brokers and policyholders include:

- Underwriting expertise and product offering — The Lloyd’s market is a recognised centre of specialist underwriting, claims and analytics expertise. This expertise supports a wide range of specialist insurance and reinsurance products, often developed to meet complex and challenging insurance needs.
- Claims payment — Lloyd’s is proud of its reputation for paying claims in a timely and efficient manner.
- Security and ratings — The single market ratings – from Standard & Poor’s, Fitch and A.M. Best – reflect the fact that all contracts underwritten at Lloyd’s are backed by Lloyd’s ‘chain of security’. All policyholders benefit from the robust financial position of the market as a whole.

Benefits to syndicates and capital providers:

- Market access — Through Lloyd’s central licensing arrangements syndicates at Lloyd’s are able to access business from more than 200 countries and territories. The London underwriting room, in which transactions take place on a face to face basis, and Lloyd’s strategically located international hubs are all supported by a global network of representatives with extensive local knowledge.
- Capital advantages — Lloyd’s capital framework, under which insurance commitments are underpinned by a Central Fund, is efficient and flexible.
- Central processes — Lloyd’s market infrastructure supports its efficient operation. The Society provides central cash settlement and up to date information on regulatory and legal changes that could have an impact on underwriting decisions. It provides efficient tax and regulatory reporting to help the market meet its requirements and represents the market’s interests to regulators and governments.
- Market oversight — The Society aims to strike a proportionate balance between supporting a robust market oversight regime and supporting the entrepreneurial and innovative culture that has contributed to its growth and reputation for more than three centuries. It seeks not only to work with market participants wanting to develop new and innovative products but also to foster new thinking for the market as a whole – for example, through research into emerging risks and their potential mitigation.

These benefits are central to “Vision 2025” which sets out the strategic direction for Lloyd’s in the context of long term industry trends and the challenges which Lloyd’s faces in the current global economy. Lloyd’s strategic plan identifies the steps that are being taken to deliver Vision 2025 and identifies Lloyd’s eight major strategic priorities which are market oversight, global market access, ease of doing business, capital, innovation, talent, brand and global corporate social responsibility.

- **Market Oversight**  
The unique nature of Lloyd’s, as a market of independent businesses backed by a mutual Central Fund, requires the Society to play a supervisory role. This role covers performance management, capital setting and risk management. It is also critical that Lloyd’s market oversight is supportive of sustainable profitable growth and innovation, and is valued by all stakeholders. As industry conditions remain challenging, market oversight remains a priority for the Society and market participants alike. Ensuring that oversight is appropriately calibrated between protection and growth is an ongoing task, requiring dialogue between the Society, managing agents and regulators.
- **Global Market Access**  
Access to international insurance markets is one of Lloyd’s most important assets. A key strand of Vision 2025 is the protection and expansion of this access. Lloyd’s is pursuing new trading rights in developing markets which will be supported by effective operational infrastructure. This access will reflect ongoing and long-term shifts in the global economy and the dispersal of insurance capacity. In some territories, commercial or regulatory requirements may require Lloyd’s local presence. The

prioritisation of new trading rights and the form of access is agreed by the market and the Society working in partnership to consider opportunities on a territory by territory basis. This work takes into account forecast insurance market development, legislative developments, local placement trends and managing agent appetite. The aim is to create access in the short-term which leaves Lloyd's well positioned for opportunities over the medium to longer term.

- **Ease of Doing Business**

Addressing the operational challenges being faced by the London market is a high priority and the required change can only be delivered by the whole market working together. By working in partnership to build an industry-leading infrastructure and service proposition covering the London market, international operations and delegated authorities, Lloyd's aims to make the market more attractive to existing and new business in London and in local markets alike. The overall programme of work – the London TOM – along with Lloyd's-specific elements, aims to provide: a market with 21st century processes and infrastructure; improved access to, and from, global insurance markets; increased efficiency, reduced administrative burden and consequently reduced frictional costs; a suite of central services for non-competitive activities; and improved access to, and smarter use of, Lloyd's market data.

- **Capital**

Maintaining the attractiveness of Lloyd's to a range of capital providers will underpin the market's future success. Further increasing the diversity of the market's capital base, both by type and by geography, is an important objective. Lloyd's focus in recent years had been on meeting the requirements of Solvency II ahead of its implementation from 1 January 2016. Lloyd's has been successful in this task. The focus now is to consider Lloyd's future capital strategy within the Solvency II framework.

- **Innovation**

Lloyd's has a reputation for innovation and will build on this in the coming years. The aim of this priority is to enhance Lloyd's activity in respect of product innovation, thought leadership, and alternative capital and alternative products. The existing strengths and expertise of the market, combined with developments in analytics and technology, provide a strong basis from which to develop this capacity for innovation into a sustainable competitive advantage. The Society has a role in facilitating innovation and product development. This is delivered through pioneering thought leadership and support for market participants at the 'pre-competitive' stage of product development.

- **Talent**

Lloyd's has a reputation for a breadth and depth of expertise in specialist risk. This arises in part through the clustering benefits of the London insurance market. The whole market has an interest in ensuring that relevant skills, capabilities and knowledge are acquired and developed in order to reinforce this differentiator. London market participants are working to raise awareness of the sector with individuals who might not otherwise be attracted to insurance. This will become increasingly important as the 'baby boom' generation transitions into retirement. Lloyd's is committed to attracting, retaining and developing the best talent through a high performance culture, best practice and inspirational leadership. Diversity and inclusion is good for business and remains a priority. The Society and market work in partnership, through Inclusion@Lloyd's, to embrace and embed diversity by widening perspectives and sharing best practice.

- **Brand**

Lloyd's 329-year old brand is globally recognised and highly valued both within the insurance industry and broader society. The positive role Lloyd's plays in times of crisis is well documented and the current strength and buoyancy of the marketplace is held in high regard. Nonetheless, as globalisation gathers pace and competition intensifies, there is no time for complacency and the Society is continually working to protect and enhance the Lloyd's brand.

- **Global Corporate Social Responsibility**

As a major player in the global economy, it is important that Lloyd's acts responsibly. Lloyd's is already highly regarded for the corporate social responsibility activities undertaken in its local communities. As the market grows and diversifies, so do the levels of activity. This responsibility also applies to business practices. The Lloyd's market should aspire to the highest standards in business conduct and ensure its customers are fairly treated at all times. Lloyd's also wants to use its experience and expertise to help communities around the world build resilience against disasters, including the effects of climate change and extreme weather events.

## ***Performance Management***

### *Business Planning*

On an annual basis and for each time it wishes to change its plan, each managing agent is required to submit a business plan to the Society for each syndicate it manages. The agreement of the Society is required for each syndicate's business plan and for any changes to the plan.

In preparing a business plan the managing agent must have regard to the guidelines issued by the Society (the "**Franchise Guidelines**"). Franchise Guidelines were first issued by the Society in 2002 and are reviewed regularly. The Franchise Guidelines represent prudent parameters within which each syndicate should operate. They are based on sound underwriting and business practices and are aimed at assisting managing agents to optimise and, where necessary, improve the performance of the syndicates they manage. If a managing agent wishes to operate outside the Franchise Guidelines, it will generally require the agreement of the Society through the business plan process. Some of the key Franchise Guidelines are as follows:

- *Profitability by business line* – There should be a reasonable expectation of making a gross underwriting profit on each line of business every year. In practice, the cyclical nature of insurance means constant profit is not a realistic expectation every year but unless a line of business can be written profitably over the insurance cycle there can be few reasons for writing it;
- *Catastrophe Risk* – As part of business-planning and capital-setting, Lloyd's controls the level of catastrophe risk relative to capital. This applies to individual syndicates and Lloyd's as a whole.

At syndicate level, there are two main controls. The first is volatility of catastrophe risk (both gross and net of reinsurance) relative to earnings, for which a percentage of capital-plus-expected-profit is a proxy. As measured by the defined metrics, syndicates are generally not permitted to allow forecast catastrophe risk to exceed 80% of capital-plus-expected-profit on a gross basis, or 30% on a net basis. Exceptions are considered on an individual basis.

The second control is on forecast catastrophe risk at an exceedance probability of 0.5% (1-in-200 years) relative to both the catastrophe element of capital, and the Economic Capital Assessment overall. Syndicate modelling techniques are explicitly considered, especially where catastrophe risk is high relative to overall capital.

At the level of Lloyd's as a whole, there are defined appetites for catastrophe risk including the relationship of catastrophe losses at an exceedance probability of 0.4% (1-in-250 years) relative to available capital including mutual assets. Forecast versions of the catastrophe risk appetites are explicitly considered during the capital and planning process.

- *Gross line size* – The maximum gross line that a syndicate should have on an individual risk is 8% of Gross Written Premium. This is to ensure that syndicates use their capacity across a relatively large set of uncorrelated risks.

In addition to the Franchise Guidelines, the Society issues from time to time additional requirements and guidelines for underwriting, which may be notified to the market in market bulletins or emails to managing agents. The Franchise Guidelines and any additional requirements or guidelines are periodically consolidated in updated editions of 'Performance Management: Supplemental Requirements and Guidance'.

The Society reviews and agrees syndicate business plans. In addition to applying the Franchise Guidelines as a framework for this review, the Society also examines the syndicate's business strategy, the lines of business the syndicate intends to underwrite, the syndicate's reinsurance strategy and its forecast financial performance. Following discussions with the managing agent, the Society will, where appropriate, seek modifications to the business plan following which the plan can be agreed. The Society also reviews each managing agents' Own Risk and Solvency Assessment ("ORSA") annually. Managing agents are required to produce an ORSA report for each syndicate under management taking into consideration the risks to members' capital. Syndicate ORSAs must be an agent's own assessment of risk and capital, tailored to meet the wide variety of individual businesses across the market. For this reason, the Society does not prescribe the output required. It does however set minimum standards on the ORSA scope, policy, process, record and report to which all managing agents are expected to comply with to operate at Lloyd's (see "*Performance Monitoring*" below).

### *Performance Monitoring*

The Society requires a managing agent to report quarterly on the performance of each syndicate it manages. Through analysis and performance modelling the Society seeks to produce forecast results for each syndicate and each line of business. This produces a modelled development pattern against which the reported quarterly performance of each syndicate can be tracked.

The Society also tracks a variety of other performance measurements at syndicate and market level including the development of syndicate reserves for prior years of account, expenses, accuracy of each syndicate's results forecasting, investment performance and historic and current premium income levels.

The analysis of this information enables the Society to track actual syndicate performance against a number of benchmarks. The aim is to seek to identify underperforming syndicates and/or lines of business at an early stage to ensure appropriate action can be taken. Where appropriate the Society provides the results of its analysis on a particular syndicate to the managing agent of that syndicate.

In addition, managing agents' performance against a set of minimum standards is also reviewed. The original Lloyd's minimum standards were developed in 2005 and covered fundamental elements such as underwriting, governance and risk management (the "**Lloyd's Minimum Standards**"). Over time, additional minimum standards have been developed to support broader activity in other areas and multiple sources of requirements existed which managing agents needed to comply with. Accordingly, the Society published a new set of Minimum Standards on 1 July 2014 (the "**Minimum Standards**") which provide a clear and complete framework within which all managing agents are required to operate. The Minimum Standards align clearly with the requirements of Solvency II and cover the following areas –

- The underwriting management standards cover underwriting strategy, underwriting controls, delegated underwriting, pricing and rate monitoring, exposure management and assessment, reinsurance and data quality.
- The claims management standards cover claims philosophy, resources, skills management and controls, claims processes, documentation, claims reserving, management of external service providers and performance measurement.
- The governance standards cover systems of governance, internal controls, organisational structure, allocation and segregation of responsibilities, documentation of key policies, board effectiveness, collective suitability of the board, management of outsourcing arrangements and requirements relating to certain required functions (compliance, internal audit, risk management & actuarial).
- Risk management standards cover risk management systems, strategy and processes (identification, assessment, control and mitigation, monitoring and reporting) and requirements relating to the ORSA.
- The standards relating to internal models cover model design and implementation, model scope, model change, use and validation of the internal model.

- The investment management standards cover investment strategy and governance.
- The reserving standards cover board responsibility for setting reserves, the Statement of Actuarial Opinion, the actuarial function, board information and the reserving procedure.
- The regulatory standards cover relationships with regulators in the UK and overseas, conducting business in accordance with applicable UK and international regulatory requirements (including but not limited to applicable financial crime and international sanctions requirements).
- The standards for operating at Lloyd's cover operational requirements relating to IT and infrastructure, HR and finance and the protection of Lloyd's reputation and brand.
- The conduct standards cover how managing agents should assess, control and oversee conduct risk arising from their underwriting business at Lloyd's.

Where a managing agent of a syndicate is underperforming or does not meet any part of the Minimum Standards, the Society will provide the managing agent with information and guidance to enable it to raise its standard of performance. If a managing agent does not respond to this facilitative approach, the Society will consider what action may be appropriate to manage the risks posed by that syndicate to Lloyd's. This will usually involve the imposition of suitable conditions, including conditions on the amount, duration and risk profile of business that the syndicate can underwrite. Continued underperformance may result in withdrawal of the Society's agreement to the syndicate's business plan and/or withdrawal of the managing agent's permission to operate in Lloyd's.

#### *Risk Management*

The Franchise Board views the development of leading risk management practices as critical in maximising the performance of the market. The Society has a dedicated risk management function to identify and ensure that all the key risks affecting the Lloyd's market as a whole (and individual managing agents and the syndicates which they manage) are managed.

The Franchise Board defines its risk appetite (the risk it deems to be acceptable across the Lloyd's market as a whole and the Society) and has put in place risk appetite statements which provide details of the appropriate levels of risk. These statements are supported by a set of metrics for monitoring which are regularly reviewed and escalated where appropriate through the Society's governance structure. The metrics are set at levels at which they are intended to be triggered to ensure that sufficient remedial actions are put in place.

Effective risk management is fundamental to the operation of Lloyd's and a core responsibility of the Society. A risk management framework has been established that identifies the key risks that the Society and the Lloyd's market faces, and enables an assessment of these risks on a common basis. This framework is led by the Society's Risk Committee, chaired by an Independent Non-Executive Director from the Franchise Board which is responsible for overseeing the risks to the Society and providing assurance that the risks are managed in accordance with approved policies and risk appetites. The Risk Committee reports to the Franchise Board and Council to ensure appropriate oversight and challenge on key risk issues and to provide assurance that risk is being identified and managed effectively. The current principal risks identified by the Risk Committee and the Franchise Board are (i) market conditions, (ii) catastrophe exposure, (iii) delivery of Vision 2025 initiatives, (iv) supplier management, (v) tax, (vi) Solvency II compliance, (vii) deteriorating supervisory environment and (viii) the consequences of Brexit. Information about these risks is covered in "*Risk Factors*" above.

As part of the Society's framework, each managing agent is expected to have in place its own comprehensive risk management framework to manage the risks facing their businesses and must set its own risk appetite that is appropriate for its individual business model and strategy. The Society continuously reviews managing agents' capabilities and track records to ensure they meet the Minimum Standards set for operating within the Lloyd's market (details of these standards are outlined in the "*Performance Monitoring*" section above).

## **Catastrophe Risk and Exposure Management**

The Society uses a variety of methods to assess catastrophe risk within the Lloyd's market.

The primary method is to collect from syndicates probabilistic risk assessments, gross and net of reinsurance, for regions and perils which represent material natural catastrophe risk to the Society. These are aggregated into a 'whole market' exceedance-probability curve. The syndicate data is created by the managing agents using generally-accepted methods for representing natural catastrophe risk, often (though not always) including external vendor catastrophe models.

In addition to probabilistic modelling, the Society continues to collect loss estimates based on deterministic scenarios (Realistic Disaster Scenarios ("RDS")), plus aggregated exposure data for selected countries, on a biannual basis. The RDS are a collection of hypothetical scenarios based on plausible yet challenging assumptions representing a range of manmade and natural catastrophes. Managing agents are currently required to report loss estimates for scenarios which include: (i) a single Florida hurricane leading to insurance industry property losses of \$131 billion or \$134 billion depending on location, (ii) two major hurricane landfalls in one year hitting South Carolina (\$39 billion) and North East (\$81 billion), and (iii) Californian earthquakes leading to industry insured losses of \$78 billion or \$80 billion depending on location. Other compulsory scenarios include: Two bespoke syndicate scenarios, New Madrid earthquake, European Windstorm, Japanese Typhoon and Earthquake, Terrorism and UK flood. There are additional scenarios for marine, aviation, liability, satellites and political risks and these are reported subject to materiality criteria.

Atlantic hurricane represents Lloyd's most material natural catastrophe risk to both earnings and solvency. The Society remains of the view that Atlantic hurricane risks are non-stationary and therefore requires that the market take a forward view of risk to take this into account. In 2016 Lloyd's published a study in association with the Met Office ('The Risk of Global Weather Teleconnections') analysing the links between extreme weather events occurring in separate regions of the world that can take place over a range of timescales from days to years (known as teleconnections). The Met Office research found that the majority of perils are not significantly correlated and so an assumption of independence for capital-holding purposes is appropriate for the key risks the Lloyd's market currently insures.

North American earthquake represents Lloyd's next most material natural catastrophe risk. Latest seismic research by the US Geological Survey indicates that fault lines in north and south California may be interconnected. Lloyd's expects this finding to be incorporated into generally accepted views of North American earthquake risk during 2017, and will monitor syndicates with material exposures accordingly.

In addition to financial risk data, Lloyd's also has a suite of Minimum Standards for Exposure Management. Managing agents are required to self-assess compliance with the standards and this is reviewed periodically by skilled personnel within the Society. The standards include a requirement of data completeness, accuracy and appropriateness, communication of uncertainty, and identification and management of emerging risks.

### *Capital Requirements*

Each member, either corporate or individual, must provide capital to support its underwriting at Lloyd's. In accordance with the PRA regulatory capital regime, each managing agent produces its own capital assessment in respect of each managed syndicate stating how much capital it considers is needed to cover its underlying business risks with a 99.5% confidence level. In light of the Lloyd's market's mix of business, it is important that this assessment goes beyond the 12 month horizon required by Solvency II and covers the risk of such extreme losses until all liabilities are paid and extend to an ultimate basis. The Society carries out an annual review of syndicate capital and the PRA reviews a sample of syndicates in order to validate the effectiveness of the reviews carried out by the Society.

The Society reviews each syndicate's capital, using all the information submitted and held regarding the historical performance, business plans and risk appetite of that syndicate in assessing the adequacy of the capital level proposed. When agreed, each syndicate's capital assessment is then 'uplifted' by 35% to ensure extra capital is in place to support Lloyd's ratings and financial strength. This uplifted capital (known as the Economic Capital Assessment ("ECA")) for the syndicate is used to determine the funds at Lloyd's that the

syndicate's members must provide to support their underwriting. Members' funds at Lloyd's are held in trust by the Society, as readily realisable assets (such as cash, securities, letters of credit and bank and insurance company guarantees). If required, these assets can be used to meet any Lloyd's insurance liabilities of that member but not the liabilities of other members.

### **Lloyd's Solvency Capital Requirement and Solvency II**

The Society also prepares a capital assessment for the Lloyd's market overall, using the PRA's defined risk categories and 99.5% confidence level. This examines the risks that are not captured in each member's capital assessment including, for example, investment risk on assets held centrally or damage to the Lloyd's building itself. In addition the Society's capital considers the risk that members' FAL will be insufficient to meet the risks arising from members' underwriting activities.

In addition, the Society calculates and reports on the statutory solvency position of the Society to the PRA. As at 30 June 2016, the Society reported a surplus over central SCR of £1,772 million, and a surplus over MWSCR (as defined below) of £6,999 million. See "*Resources within the Lloyd's market and the Protection of Policyholders*" for further information on the Society's capital resources and structure.

### ***Other activities of the Society***

These include: obtaining and maintaining the Lloyd's members' authorisations to conduct business in other jurisdictions, identifying and taking action in respect of breaches of its requirements by market participants, operating a central settlements system for the market, and providing other services, such as treasury services, to market participants.

### ***Subsidiaries of the Society***

The Society has three principal subsidiaries: Additional Securities Limited, Centrewrite Limited ("**Centrewrite**"), and Lloyd's Insurance Company (China) Limited. The Society had a fourth principal subsidiary, Lioncover Insurance Company Limited ("**Lioncover**"), and an application for the voluntary strike off of Lioncover from the Companies Register was approved on 21 October 2014 by Companies House.

Additional Securities Limited is funded by members and provides deposits overseas on behalf of Lloyd's members in order to comply with local insurance regulations.

Centrewrite is an authorised UK insurance company. Centrewrite's principal business is to offer reinsurance protection to members of Lloyd's who participate in syndicates which are unable to close their accounts through RITC. Lioncover was formed in 1987 to reinsure the liabilities of members in certain syndicates (the "**PCW Syndicates**"). Following implementation of Reconstruction and Renewal (see "*Reconstruction and Renewal and Equitas*"), the liabilities of Lioncover and the pre-1992 liabilities of Centrewrite were reinsured into Equitas. The Society gave an indemnity bond to both Lioncover and Centrewrite against any shortfall of their assets or cashflow (including any shortfall arising from an insufficiency of recoveries from Equitas Reinsurance Limited under its reinsurance of the obligations of Centrewrite to Equitas Insurance Limited ("**EIL**"), a subsidiary of Equitas Holdings Limited). The Council determined that any losses resulting from such indemnities will be met by the Central Fund. Accordingly, if Equitas were unable to discharge in full the Lioncover and Centrewrite liabilities which it has reinsured, any resulting shortfall would be met out of the Central Fund under the terms of the indemnity bonds. However, the transfer of Equitas' reinsurance obligations to National Indemnity Company in 2006 makes the contingent liabilities under the Centrewrite bond which existed at that date and continues to exist considerably less likely to crystallise (see "*Reconstruction and Renewal and Equitas*" for further information on the retrocession of Equitas' reinsurance obligations).

In 2009 the Lioncover bond was released and replaced by a substitute Lioncover bond. Equitas Policyholders Trustee Limited received the benefit, on behalf of the former policyholders of the PCW Syndicates, of the Lloyd's undertakings set out in the substitute bond and under which Lloyd's would meet any shortfall in recoveries by such policyholders from EIL on the occurrence of an insolvency event relating to Equitas

Reinsurance Limited or EIL. This was undertaken as part of the transfer of Equitas-reinsured members' 1992 and prior non-life business to a specifically authorised new insurance company, EIL.

In March 2007 Lloyd's received regulatory approval for Lloyd's Reinsurance Company (China) Limited to commence underwriting reinsurance business. In May 2010, the China Insurance Regulatory Commission ("CIRC") extended Lloyd's Reinsurance Company (China) Limited's licence to include non-life direct insurance in the Shanghai region. In line with this expanded licence and in accordance with the regulations of CIRC, the company name changed from Lloyd's Reinsurance Company (China) Limited to Lloyd's Insurance Company (China) Limited ("LICCL") in October 2010. The extended licence became operational in September 2011. Reinsurance forms the majority of business written by LICCL but the extended licence allows the Lloyd's market greater access to Chinese business and is an important long term development for Lloyd's presence in China. LICCL was granted a Beijing branch licence in 2014 and the branch office became operational from March 2015.

Lloyd's syndicates participate in LICCL's business by means of retrocession agreements which allow a 100% risk transfer. LICCL's capital is provided centrally by Lloyd's. A risk-oriented solvency regime, China Risk Oriented Solvency System ("C-ROSS"), was introduced by the CIRC with effect from 1 January 2016. LICCL meets the C-ROSS solvency requirements as an on-shore company. A minimum solvency ratio of 200% will be required for LICCL to be considered commercially attractive as a reinsurer by cedants. In response to the C-ROSS requirements, in 2014 the Council resolved to use the New Central Fund to increase LICCL's capital from RMB 220 million to RMB 1 billion.

## **Resources within the Lloyd's market and the Protection of Policyholders**

### ***The "Chain of Security"***

The resources held within the Lloyd's market to support members' underwriting liabilities are derived from three separate sources which together make up what has been described in the Lloyd's market as the Lloyd's "chain of security" (although the term "security" is not used in a technical sense).

**Investors should note that assets that are described below as falling within the first and second links of the chain of security are held by or on behalf of members to support their own insurance liabilities only and would not therefore be directly available to meet the Society's obligations to repay the Notes (although such assets may become available to meet the Society's obligations to the extent they are transferred to the Society as a result of the Society making calls on members for contributions or imposing levies on members). Furthermore, assets falling within the third link of the chain of security (central resources) would, in accordance with the terms and conditions of the Notes, be used to discharge the claims of Senior Creditors (as defined in the terms and conditions of the Notes) of the Society in priority to claims of the holders of the Notes in the event of a winding-up of the Society.**

### ***The first link: syndicate level assets***

The first link in the chain of security is the members' Premiums Trust Funds ("PTF"), and other assets held in trust at syndicate level. To protect the interests of policyholders, all premiums and monies received or receivable in connection with the members' underwriting business are initially paid into the PTFs, managed by the managing agent of the syndicate concerned. Payments from these funds may only be made to meet permitted trust outgoings which include claims, reinsurance premiums and underwriting expenses, including funding overseas regulatory deposits. Investment of the assets of the syndicate level PTFs is at the discretion of managing agents. These funds are required to retain high levels of liquidity. Typically, the funds are invested in money-market and short to medium dated fixed-interest securities of high credit quality. Average portfolio durations are typically between one and three years. Volatility arising from yield movements is consequently low.

A member's PTF is held at two levels – syndicate level and personal reserve level. Assets held at syndicate level of the PTF form part of the first link of the chain of security whereas assets held at the personal reserve

level of the PTF fall within the second link. Premiums and other amounts received in respect of a member's insurance business are initially held in a member's PTF at syndicate level.

Outgoings are met from the syndicate level PTF applied at the direction of the managing agent. Profit is distributed from syndicate level to personal reserve level in the PTF. Amounts are distributed from personal reserve level of the PTF to a member only once the Society is satisfied that all of a member's outstanding underwriting liabilities have been met or adequately provided for. There are separate PTFs for life business and non-life general business. There is a further segregation in that a number of the PTFs are exclusively available to support certain overseas underwriting of members.

The Lloyd's Dollar Trust Funds (the "LDTF") receive premiums in respect of U.S. dollar denominated non-life business underwritten or incepting on or after 1 August 1995.

The other overseas PTFs are the Lloyd's Canadian Dollar Trust Fund (the "LCTF") in Canada, comprising members' underwriting receipts in respect of Canadian situs business and the Lloyd's Asia trust funds for general business written 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 cash call requests by managing agents to make such funds available. Cash calls are met by members from their own resources or, if necessary, from their FAL or, at the Council's discretion, the Central Fund.

PTFs 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 surplus lines business, US situs reinsurance as accredited reinsurers, and for Illinois and Kentucky business respectively). In addition, separate joint asset trust funds provide joint security for members' US situs surplus lines, US situs reinsurance and Kentucky business respectively.

These deposits would be available to meet judgment debts of a member in respect of business connected with the relevant overseas territory in the event that the relevant premiums trust fund of the member, even after replenishment from other links in the chain of security and other free assets of the member in question, was inadequate. Underwriters also maintain regulatory deposit trust funds in Australia and South Africa and various deposits in other countries. The total value of all the above funds was £51,585 million in aggregate, at 30 June 2016.

#### *The second link: members' funds at Lloyd's (FAL)*

The second link is members' FAL. 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 held under the terms of the premiums trust deed. These are each available to meet cash calls made on the member in respect of a syndicate. The assets in FAL must be at least equivalent to the aggregate of the member's net FAL requirement and certain liabilities in respect of its underwriting business. From 1 July 2007, capital deposits by aligned corporate members can be held in premium trust funds (see first link above). FAL will include assets lodged by members to cover deficits declared by syndicates. Where syndicates report such losses on open years that do not immediately trigger a cash call requirement at syndicate level, members are required to deposit additional assets centrally to cover these deficits, so that their FAL are sufficient to meet both open year losses and their ECA. Minimum capital ratios are set at 40% of overall premium limits. 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 FAL, which can be called upon to meet its underwriting liabilities. As at 30 June 2016, the total value of FAL held in trust by members amounted to £20,108 million in aggregate.

#### *The third link: central resources*

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 with the purpose of being available, at the discretion of the Council, 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 and for complying with the Society's regulatory capital requirements. 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. A member or former member of the Society does not have any right to the repayment of any contribution that member or former member has made other than in a winding up of the Society.

The New Central Fund is funded by annual contributions from members. These amounts are treated as equity in the Society's financial statements. The equity of the Central Fund as at 30 June 2016 was £1,838 million.

In addition to the Central Fund, the other equity of the Society, which totalled £25 million at 30 June 2016, is available to meet underwriting liabilities in the last resort, resulting in total equity of the Society at 30 June 2016, of £1,863 million.

The Society also has the right to make a call on members of up to 3% of members' premium limits ("**callable contributions**"). The callable contributions can be drawn from members' premiums trust funds without the members' consent.

In 2007 the Society issued the 2007 Notes and in 2014 the Society issued the 2014 Notes which, as at 30 June 2016, are included as a liability of £882 million within the Society's financial statements. Payments on the 2007 Notes and 2014 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.

The table below shows a breakdown of the central resources of the Society, excluding the callable layer.

	<b>30 June 2016</b> £m	31 December 2015 £m	31 December 2014 £m
Society Equity	<b>1,863</b>	1,763	1,693
2014 Notes	<b>494</b>	494	497
2007 Notes, with a first call date of 21 June 2017	<b>388</b>	388	388
<b>Central assets</b>	<b>2,745</b>	<b>2,645</b>	<b>2,578</b>

Interest payments on the Notes will be funded out of the Central Fund "working layer" which is capitalised as shown in the table below.

£ million	2013	2014	2015	H1 2016
Net Central Fund "working layer" assets (opening balance)	1,460	1,512	1,587	1,655
Cash contributions from members	106	102	107	100
Subordinated debt repurchase	(15)	(9)	0	0
Claims and provisions	(18)	(1)	0	0
Investment income	59	91	38	153
Coupon payments accrued	(56)	(49)	(54)	(27)
Other	(24)	(59)	(23)	(46)
Net Central Fund "working layer" assets (closing balance)	1,512	1,587	1,655	1,835
Corporation of Lloyd's & subsidiaries & reserves	123	103	105	25
Dated Sub debt and perpetual subordinated securities	721	885	882	882
<b>Central assets excluding sub-debt liabilities</b>	<b>2,356</b>	<b>2,575</b>	<b>2,642</b>	<b>2,742</b>

Callable layer	788	779	822	875
Central assets including callable layer	3,144	3,354	3,464	3,617
Other adjustments for solvency <sup>2</sup>	(19)	(117)	(135)	(131)
Central assets for solvency	3,125	3,237	3,329	3,486

Notes:

- 1) Repurchase of £180 million principal of sterling and euro 2004 subordinated notes in May 2013 (the “**Sterling 2004 Notes**” and the “**Euro 2004 Notes**” respectively); Repurchase of £149 million principal of the Sterling 2004 Notes in October 2014; Issue of the 2014 Notes in 2014; Redemption of £178 million principal (at December 2013 rates of exchange) of Euro 2004 notes in November 2014; Redemption of £5 million principal of the Sterling 2004 Notes in November 2015;
- 2) 2013-2015 adjustment on a Solvency I basis.

### **Application of central assets**

The New Central Fund is held and owned by the Society and, at the discretion of the Council, can be applied to discharge any liabilities of Lloyd’s members that they are unable to meet in full and also for such other purposes as may appear to the Council to further any of the objects of the Society. The New Central Fund may be used to meet directly 1992 or prior year non-life insurance business claims of members only if the members of Lloyd’s resolve in a general meeting to make the New Central Fund available for this purpose. The Central Fund may however be applied to meet liabilities to which members of Lloyd’s or the Society could be exposed in the event of a failure of Equitas (see “*Reconstruction and Renewal and Equitas*”).

When a corporate member is unable to meet its liabilities, the Society would, under normal circumstances, give an annual undertaking to that member by which the Society agrees to use the New Central Fund to meet cash calls made on the member. The undertaking would have a duration of 12 months and would be subject to a financial limit. The undertaking is limited to monies or other assets from time to time forming part of the New Central Fund. For corporate members in provisional liquidation, the Society will also provide 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. A supporting undertaking is legally enforceable. Whilst the Society is solvent, the likelihood of the supporting undertaking being called in is extremely remote.

When assessing the need for further annual undertakings, the Society reviews the most recent audited solvency returns prepared by managing agents of syndicates on which the corporate member participates.

These returns will be supported by an actuarial opinion on the adequacy of the syndicate reserves. This enables the Society to form a view on both the level of future cash calls that may be made on the relevant member during the next 12 month period and to assess the total level of the member’s underwriting liabilities.

As noted above, the Central Fund equity as at 30 June 2016 was £1,838 million. This is stated after making provision for all undertakings given by the Council up to that date. The aggregate outstanding amounts of all undertakings given by the Council were £6 million.

The requirement to give undertakings reflects the likelihood that cash calls on insolvent corporate members will need to be funded by the Central Fund over the following 12 months in order to ensure that the insurance liabilities (including policyholder claims) of insolvent corporate members may be paid in full as and when they are due.

### **Regulatory solvency**

The Society and the Lloyd’s market are regulated by the PRA in accordance with the requirements of the Solvency II regime, which was implemented on 1 January 2016, as ‘the association of underwriters known as Lloyd’s’.

Lloyd’s must calculate and cover two SCRs, given the unique structure of Lloyd’s: the Lloyd’s market wide SCR and the central SCR. Under the Solvency II regime, it must then ensure that each SCR is covered by

eligible capital at all times. In respect of the Notes, also see “*Risk Factors - Interest payments under the Notes may be deferred at the option of the Issuer and must be deferred under certain circumstances*”.

The Lloyd’s market wide SCR (“**MWSCR**”) is calculated to cover all of the risks of ‘the association of underwriters known as Lloyd’s’, i.e. those arising on syndicate activity, members’ capital provided at Lloyd’s and the Society taken together, at a 99.5% confidence level over a one year time horizon as provided for in Solvency II legislation. All of the capital of the component parts of the market taken together are available to meet the MWSCR.

The Lloyd’s central SCR (“**central SCR**”) is calculated in respect of only the risks facing the Society and the Central Fund at the same confidence level and time horizon used to calculate the MWSCR. The material risk is that members do not have sufficient funds to meet their underwriting losses even having complied with Lloyd’s rigorous capital setting rules. In such an event assets from the Central Fund can, at the discretion of the Council, be made available to ensure that policyholders’ claims are met. Only eligible capital held by the Society may be used to cover the central SCR.

The MWSCR and central SCR are both calculated in accordance with the Lloyd’s full Internal Model which was approved for this purpose by the PRA in December 2015.

Coverage of the MWSCR and Central SCR is an ongoing and continuous requirement. In accordance with the Pillar 3 Solvency II requirements, Lloyd’s reports the results of its solvency test – i.e. the amount of the MWSCR, eligible assets to cover it and the solvency ratio – on a quarterly basis to the PRA. This information shall also be reported publicly in the Solvency & Financial Condition Report, as at 31 December 2016, in May 2017. The results of the coverage of the central SCR are reported privately to the PRA quarterly, and ad hoc after any material event.

Lloyd’s solvency ratios in respect of the MWSCR and central SCR as calculated for the first time in Solvency II ‘Day 1’ reporting to the PRA (i.e. as at 1 January 2016) and at 30 June 2016 are set out below:

<b>MWSCR</b>	30 June 2016	1 January 2016
SCR £million	15,057	14,150
Eligible assets to meet the SCR £million	22,056	20,662
Solvency coverage ratio	146%	146%

<b>Central SCR</b>	30 June 2016	1 January 2016
SCR £million	1,543	1,450
Eligible assets to meet the SCR £million	3,315	3,162
Solvency coverage ratio	215%	218%

#### **Market wide SCR (MWSCR)**

- The MWSCR for 2016 at 1 January 2016 was £14.2 billion.
- The dominant risk lies in insurance claims, whether writing loss-making new business, natural catastrophe claims or increases to existing claims reserves.
- The highest ever annual loss reported by Lloyd’s was in 2001 (£3.1 billion) with a combined ratio of 140% and a positive investment contribution of over £1 billion. In today’s market size terms, that loss would be equivalent to £7.1 billion versus an MWSCR surplus of £6.5 billion (as at 1 January 2016) and £7.0 billion (as at 30 June 2016).

## Central SCR

- The central SCR for 2016 at 1 January 2016 was £1.5 billion.
- The risk to central assets derives from the following sources:
  - Member losses (due to writing insurance business through Lloyd’s syndicates and other causes of syndicate loss).
  - Investment losses on central assets.
  - Operational losses to the Society (such as losses ensuing from a data theft).
  - Pension fund losses.
- The latter risks are significant in their own right, but for the extreme scenarios that the central SCR considers, it is members’ insurance claims that present the dominant risk to central assets.
- The central SCR has been compared to previous experience, updated to today’s capital setting regime and the 2016 market’s size. This “back-testing” provides comfort that previous losses are much lower than the current central SCR.
- No credit has been taken in the model when calculating the MWSCR or Central SCR for members injecting new capital as losses emerge or following events that exhaust their capital or for members holding actual capital in excess of the minimum required. In practice, recapitalisation to trade forward at Lloyd’s has been observed for many different reasons. When considering the scale of industry-wide losses that would trigger the MWSCR for Lloyd’s, the expectation would be for this to be market-changing and further drive capital providers to “reload” and inject new money. Also, in the event of severe losses, members would be required to come into line (replenish their capital to levels required for their ECA) and would not be able to withdraw surplus capital. However, as members are not legally obliged to recapitalise and, in principle, may withdraw surplus capital, this basis is considered appropriate for assessing the Central SCR. Member recapitalisation is explicitly considered as part of the central economic capital requirement contained in the ORSA.

### MWSCR: Diversified risks

The table below shows the contribution of each risk to the MWSCR as at 1 January 2016 after allowing for positive diversification adjustments.

<b>MWSCR One year basis Diversified risks £m</b>	<b>2016 SCR</b>
Reserving risk	3,117
All other (attritional) premium risk	4,975
Catastrophe risk	3,574
Additional Central Fund risk	326
Market risk	675
Reinsurance credit risk	666
Operational risk	264
Pension risk	22
<b>MWSCR before adjustments</b>	<b>13,619</b>
FX adjustment for movement in H2 2015	545
<b>MWSCR*</b>	<b>14,150</b>

\* Rounded to nearest £50million

### Central SCR: Standalone risks

The table below shows that by far the largest risk to the central assets is presented by syndicate losses, which can potentially exhaust member capital, with the resulting member deficits having to be covered by the Central Fund.

<b>Central SCR One year basis Standalone risks £m</b>	<b>2016 SCR</b>
All syndicate losses: member deficits	<b>1,422</b>
Operational risk to central assets	<b>378</b>
Investment risk	
Central Fund assets	<b>242</b>
Other Society assets	<b>60</b>
Pension liabilities and assets	<b>324</b>
Diversification	<b>-968</b>
<b>Total before adjustments</b>	<b>1,458</b>
Adjustment for USD movement June to Dec '15	<b>58</b>
Central Fund contributions less debt interest	<b>-50</b>
<b>Central SCR*</b>	<b>1,450</b>

\* Rounded to nearest £50m

Capital tiering and Lloyd's solvency margin as at 30 June 2016:

	Tier 1	Tier 2	Tier 3	Total
	£m	£m	£m	£m
Syndicate assets	2,647			2,647
Funds at Lloyd's (FAL):				
- Cash, bonds, equities etc (Tier 1)	9,841			9,841
- Ancillary own funds (LOCs, Bank Guarantees, FAL provided by Covenant & Charge etc) <sup>1</sup>		9,446		9,446
Society assets:				
- Subordinated debt (valued at fair value) <sup>2</sup>	399	525		924
- Deferred tax			46	46
- Balance of net assets	1,640			1,640
Total own funds <b>available</b> to meet the SCR	14,527	9,971	46	24,544
Lloyd's MWSCR				15,057
Total own funds <b>eligible</b> to meet the SCR (Tier 2 and 3 assets can only cover up to 50% of SCR)	14,527	7,529	-	22,056
'Excess' own funds not eligible to meet SCR	-	2,442	46	2,488
Lloyd's solvency ratio (based on MWSCR)				146.5%

Notes:

1. FAL provided by ancillary own funds is treated as Tier 2 capital.

2. The 2007 perpetual securities are treated as Tier 1 and the 2014 dated debt as Tier 2.

While Letters of Credit (“LoCs”) issued to the Society qualify as Tier 2 capital, they are assets callable on demand. When called, the proceeds, namely cash, would qualify as Tier 1 capital. Under these circumstances, the additional £2,442 million of Tier 2 currently ineligible to meet the SCR (since they exceed the 50% tiering limit for Tier 2 and Tier 3 Capital set by Solvency II) would then become fully eligible.

In addition, the Society applies robust controls in respect of member level solvency. 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 (i.e., solvency reserves or ‘technical provisions for solvency’) must be made in accordance with the Society’s valuation of liabilities rules and are subject to a statement of actuarial opinion (the “SAO”). The SAO must confirm that the technical provisions for solvency are not less than the actuary’s best estimate of future liabilities. In the event that it is not possible for the managing agent to secure an unqualified actuarial opinion for any reason, the solvency reserves would be determined by the Lloyd’s Actuary, who would provide a report to the PRA. In addition, any syndicate which is not able to secure an unqualified actuarial opinion will normally be subject to a monitoring review by the Society. There were no qualified actuarial opinions at 31 December 2015.

Insurance provides protection against uncertain future events. The inherent uncertainty in insurance is reflected in financial statements principally in respect of the solvency reserves established for future events and the eventual outcome of claims that have occurred but have not yet been settled. Accordingly, although the directors of each syndicate’s managing agent consider that the estimate of solvency reserves is fairly stated on the basis of the information currently available to them and the solvency reserves are subject to actuarial opinion that the reserves are at least equal to the actuary’s best estimate of the amounts required, the ultimate liability will vary as a result of subsequent information or events, which may result in significant adjustments to the amounts provided.

The Council has given undertakings, with financial limits, to certain corporate members to use the New Central Fund to discharge the liability of corporate 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 members to continue to be paid in full upon their insolvency. Such 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 which should be accounted for, even if not renewed, as if they were enforceable contractual obligations. Unutilised undertakings as at 31 December 2015 were £6 million; the undertakings have been replaced by further annual undertakings given on 21 March 2016 that total £6 million.

In light of Lloyd’s mix of business, it is important that members hold capital beyond the 12 month horizon required by Solvency II and must cover the risk of such extreme losses until all liabilities are paid and extend to an ultimate basis. The Society reviews each syndicate’s SCR to assess the adequacy of the proposed capital level. When agreed, each SCR is then ‘uplifted’ to ensure there is sufficient capital to support Lloyd’s ratings and financial strength. The uplift applied for 2016 is 35%. This uplifted SCR is known as the syndicate’s ECA and drives members’ capital levels across all of the syndicates in which they participate in proportion to their share of those syndicates. The Society will take action where a member has insufficient assets to meet its ECA, which will include requiring the member to cease underwriting unless new funds are provided. Each member, whether corporate or individual, must provide sufficient capital to support their underwriting at Lloyd’s. Managing agents are required to assess the SCR for each syndicate that they manage. Each member’s capital is held in trust by the Society for the benefit of policyholders but is not available for the liabilities of other members.

Lloyd’s solvency coverage (eligible Own Funds/ SCR) risk appetites are:

- MWSCR: The Society aims to hold capital sufficient to provide financial security to policyholders and capital efficiency to investors (or ‘members’). Members are required to put up funds to meet their

ECA, which is set as their SCR (on an ultimate view of risk) plus an uplift of 35%. Lloyd's does not require excess capital to be held above this level and considers that the risk appetite of 125% of SCR gives an appropriate buffer following diversification benefits. In the event that the capital put up by a member falls below their ECA through losses incurred or an increase in their risk profile, additional funds must be deposited. If members do not recapitalise, their authority to continue to trade is restricted to the level of their available capital or ultimately fully withdrawn and they cease trading. Such action would then reduce their risk and the aggregate MWSCR.

- Central SCR: All policies written at Lloyd's are supported by central assets, which underpin the financial strength ratings of the Lloyd's market and its international licence network. Accordingly, the risk appetite for 200% Central SCR coverage reflects the prudent approach to maintaining adequate central assets to meet a 1-in-200 year event and be in position to continue to write new business.

#### *Lloyd's solvency coverage sensitivities*

Lloyd's SCR could be affected by a range of risks. The table below shows the extent to which Lloyd's MWSCR and Central SCR coverage ratios as at 30 June 2016 would be affected by certain stresses.

		Central SCR coverage	MWSCR coverage
<b>Baseline</b>	<b>Coverage</b>	<b>215%</b>	<b>146%</b>
	Risk Appetite for solvency coverage	200%	125%
<b>Equity stress: Equity &amp; growth asset values fall by 25%</b>	<b>Coverage estimate</b>	<b>199%</b>	<b>139%</b>
	Change	-16%	-7%
	Reduction in eligible assets above SCR	-£248m	-£1,165m
<b>Credit spread stress: Investment grade credit spreads widen by 100 basis points</b>	<b>Coverage estimate</b>	<b>213%</b>	<b>142%</b>
	Change	-2%	-4%
	Reduction in eligible assets above SCR	-£27m	-£698m
<b>Combination of equity &amp; credit stress</b>	<b>Coverage estimate</b>	<b>197%</b>	<b>134%</b>
	Change	-18%	-12%
	Reduction in eligible assets above SCR	-£275m	-£1,863m
<b>Risk free rate stress: Government bond yields rise by 50 basis points</b>	<b>Coverage estimate</b>	<b>213%</b>	<b>143%</b>
	Change	-2%	-3%
	Reduction in eligible assets above SCR	-£24m	-£576m
<b>Reserve stress: Reserves deteriorate by 20% for all syndicates on Casualty lines in recent years of account</b>	<b>Coverage estimate</b>	<b>215%<sup>1</sup></b>	<b>137%</b>
	Change	0%	-9%
	Reduction in eligible assets above SCR	-	-£1,500m
<b>Catastrophe stress: 30 year return period from natural catastrophes world-wide</b>	<b>Coverage estimate</b>	<b>215%<sup>2</sup></b>	<b>123%</b>
	Change	0%	-23%
	Reduction in eligible	-	-£3,500m

Notes: Coverages are based on estimates of the stress impact on basic own funds, the SCR is assumed not to change as a result of the stress. Stresses are applied on an instantaneous basis.

<sup>1</sup> Impact on central assets (and so central SCR coverage) is not affected as these claims are spread across the market and are adequately covered by member-level funds.

<sup>2</sup> Impact on central assets (and so central SCR coverage) will be dependent on whether claims are spread across the market or concentrated in particular syndicates. The impact of significant claims on central assets would be zero unless the Issuer, at its discretion, made its assets (in particular the Central Fund) available to meet the underwriting liabilities of any Lloyd's member unable to meet their liabilities in full.

### **Aggregate Resources supporting the Lloyd's market**

The table below shows the total resources within the Lloyd's market.

£m	30-Jun-16	31-Dec-15	31-Dec-14
Syndicate level assets	51,585	46,191	45,156
FAL	20,108	17,840	15,704
<b>Central assets</b>			
Net Central Fund assets	1,838	1,658	1,590
Subordinated loan notes	494	494	497
Subordinated perpetual securities	388	388	388
Other net assets of the Society	25	105	103
Total resources of the Society	2,745	2,645	2,578
<b>Total</b>	74,438	66,676	63,438
Net Syndicate Technical Provisions	(47,821)	(41,578)	(40,025)
<b>Total</b>	26,617	25,098	23,413

Note: Prepared under UK GAAP

### **Funding of the Central Fund**

The New Central Fund is funded by an annual contribution from members which is required by the New Central Fund Byelaw.

The Society also has the right to make a call on members for callable contributions of up to 3% of members' capacity. The callable contributions can be drawn directly from members' premiums trust funds without seeking the consent of members.

The Society must announce the level of New Central Fund contributions (including callable contributions) for the forthcoming calendar year by 30 September in the year preceding that calendar year. Payment of any of these contributions by members of Lloyd's is a condition of their continuing to underwrite at Lloyd's.

The Society is empowered under the New Central Fund Byelaw to impose on members such further special contributions as the Council may by special resolution prescribe if it appears requisite or expedient to do so provided that the Society obtains the consent of members.

For the 2017 year of account, the required annual contribution has been set at 0.35% of members' Gross Written Premium for that year (new corporate members in 2015, 2016 or 2017 underwriting in 2017 on new syndicates are required to pay increased contributions of 1.4% of Gross Written Premiums for each of their first three years of operation at Lloyd's). The Society recognised £100 million in respect of contributions in 2016.

In addition to member contributions, the Society also has the power to borrow money for the purposes of funding the New Central Fund.

Lloyd's continuously reviews the capitalisation of the market and the balance of member capital (held severally) and central capital (held mutually). The Society aims to secure a capital framework in which the benefits of mutuality demonstrably outweigh the costs and which cannot be readily duplicated outside Lloyd's. In particular, the Society reviews the size of the Central Fund and the different elements which finance central assets.

### ***Investment of assets in the Central Fund***

The assets available for investment within the Central Fund totalled £2,642 million at 30 June 2016. A significant element of the Central Fund assets is invested in cash and fixed interest securities of high credit quality (62%) with the balance held in more volatile asset classes. As at 30 June 2016 exposures include global equities, high yield bonds, commodity-based investments, senior secured loans and hedge funds. The full disposition as at 30 June 2016 is shown below.

	<b>Value £m</b>	<b>% Central Fund assets</b>
Deposits	<b>44</b>	2%
Government bonds	<b>616</b>	23%
Investment grade corporate bonds	<b>1,002</b>	37%
Equities <sup>1</sup>	<b>557</b>	21%
Hedge funds	<b>148</b>	6%
Emerging market & high yield bonds	<b>136</b>	5%
Commodities	<b>45</b>	2%
Senior secured loans	<b>94</b>	4%
<b>Total</b>	<b>2,642</b>	100%

<sup>1</sup> Equities includes developed and emerging equities

Central assets form part of the overall investment fund for the Lloyd's market where the aggregate of syndicate level assets, members' FAL and central assets totalled £62,529 million. The aggregate of equities held within Lloyd's market investments is £3,373 million at 30 June 2016, or less than 5% of the total assets.

The Central Fund is generally utilised only if relevant syndicate and members' assets prove insufficient to meet claims and, therefore, the likelihood of significant cash out flows from the Central Fund is deemed to be low. Consequently, the Central Fund has a longer investment horizon than many other investment assets at Lloyd's.

The investment strategy of the Central Fund is to maximise investment returns, net of relevant liabilities, whilst operating within a defined risk budget and ensuring appropriate liquidity. Investment strategy is overseen by the Lloyd's Investment Committee. The risk budget is reviewed regularly. Value at Risk ("VAR") methodology is used to measure portfolio risk.

Financial liabilities of the Central Fund include obligations to redeem outstanding capital market debt. The effect of capital market movements on the present value of these liabilities is taken into account when calculating net investment risk. Consequently, the risk budget relates to changes in the net value of the Central Fund, after taking account of movements in liability values.

### ***Financial Services Compensation Scheme***

In October 2003 the FSA extended the application of the Financial Services Compensation Scheme (the "FSCS") to Lloyd's with effect from 1 January 2004. The FSCS provides compensation for consumers where a financial services firm fails. It covers the banking, investment and insurance sectors. In the insurance context, it provides protection to policyholders of UK insurance firms if their insurer cannot meet the claims arising from policies they have issued. The extension of the FSCS to Lloyd's policyholders provides them

with further protection in addition to that provided by the Lloyd's chain of security. This extension of the FSCS to Lloyd's does not provide protection to members of Lloyd's in the event of the failure of the Society.

Since being subject to the FSCS no levies have been charged to the Lloyd's market by the FSA or FCA in respect of the FSCS. The Council reviews annually whether or not to use central assets to contribute towards FSCS charges and, if so, at what level. The Council has agreed, as in previous years, that for 2017 it will meet the first £10 million of any such charges.

## **External Regulation of the Lloyd's market**

### ***General***

The Society is subject to the UK regulatory framework established under the Financial Services and Markets Act (the "FSMA"). Prior to 1 April 2013 the Society was regulated by the Financial Services Authority (the "FSA") and from 1 April 2013 the Society has been regulated by both the PRA (as regards prudential and organisational requirements) and the FCA (as regards conduct of business requirements).

The PRA is a subsidiary of the Bank of England, and is responsible for the micro-prudential regulation of insurance companies, banks and certain large investment firms. The PRA's primary purpose and objective is to promote financial stability. It also has a specific "insurance objective" of contributing to the securing of an appropriate degree of protection for those who are or may become policyholders of PRA-authorized insurers.

The FCA regulates the conduct of every authorised firm. Its "operational objectives" are to protect and enhance confidence in the UK financial system by protecting consumers, enhancing the integrity of financial markets and promoting effective competition in the interests of consumers. The FCA also has a "strategic objective" of ensuring that relevant markets function well.

This section describes the current regulatory framework administered by the PRA and the FCA.

### ***PRA/FCA Regulation: overview***

Since FSMA came into force in 2001, the FSA and, from 1 April 2013, the PRA and the FCA have regulated the Society. Members of Lloyd's are not required to be authorised by the PRA or the FCA to carry on insurance business, and accordingly, neither the PRA nor the FCA regulate them directly, although they have the power under FSMA to bring members within their jurisdiction by making a direction requiring that they be authorised (either generally or for specific purposes). Managing agents are regulated by both the PRA and the FCA and members' agents and Lloyd's brokers are regulated by the FCA alone.

### ***PRA/FCA Regulation: the Society***

The Society is regulated as an authorised person pursuant to article 14 of the Financial Services Act 2012 (Transitional Provisions) (Permission and Approval) Order 2013. This gives the Society permission to carry on the regulated activities of: (i) arranging deals in contracts of insurance written at Lloyd's; (ii) arranging deals in participation in Lloyd's syndicates; and (iii) any activities carried on in connection with, or for the purposes of, the activities specified in (i) and (ii) above. For regulatory purposes, the Society's role is to provide the market infrastructure which enables participants in the Lloyd's market to engage in insurance business; it does not arrange any contracts of insurance or participation in Lloyd's syndicates.

The Society nevertheless requires permission from the PRA for the activities referred to above because "arranging" has a broad meaning for UK regulatory purposes.

For the purpose of article 14, "arranging deals" is defined by FSMA as making or offering or agreeing to make: (a) arrangements with a view to another person buying, selling, subscribing for or underwriting a particular investment; or (b) arrangements with a view to a person who participates in the arrangements for buying, selling, subscribing for or underwriting investments.

Each regulator is required under FSMA to keep itself informed of: (a) the way in which the Council supervises and regulates the Lloyd's market; and (b) the way in which regulated activities are carried on in the market.

Either regulator has power under FSMA to direct the Society to exercise one or more of its powers (this may be with a view to achieving a specified objective). Generally, they must consult publicly before making a direction of this kind, but need not do so if it considers that the delay involved would be prejudicial to the interests of consumers. This power could be used by the PRA or the FCA to direct the way in which members of Lloyd's are regulated by the Council.

The Society is required by the PRA to meet various prudential requirements including the following:

- (i) that it manages its affairs with due regard to the interests of policyholders;
- (ii) that it ensures that the Lloyd's market is soundly and prudently managed; and
- (iii) that it ensures that its assets and its members' assets are adequate to meet the liabilities assumed by members in their insurance business at Lloyd's (and for this purpose, to maintain a risk based capital system).

The Society, as is the case of other insurers subject to the Solvency II regime, must comply with the supervisory reporting and disclosure requirements as specified under Pillar 3 of that regime. Specifically the Society must submit to the PRA annual and quarterly data on its financial situation and solvency and on the whole of the insurance business carried on by members (see "*Regulatory solvency*"). This includes the annual Solvency and Financial Condition Report which is a publicly available submission and which is subject in part to audit in line with the PRA's requirements in this respect.

The Society is also required by PRA rules (among other things) to make quarterly reports to the PRA on the Central Fund and its application.

#### ***PRA/FCA regulation: managing agents***

Managing agents are required to be authorised by the PRA and the FCA for the key activities which include managing the underwriting capacity of a Lloyd's syndicate and the buying and selling of general insurance as agent. As authorised persons under FSMA, they are subject to relevant requirements of the PRA and FCA Handbook of Rules and Guidance including applicable conduct of business rules, and they must at all times meet the PRA and FCA's threshold conditions that apply to them, which require (among other things) authorised persons to be fit and proper. Managing agents must also comply with the PRA and FCA's high level Principles for Businesses (which include (among other things) requirements that an authorised firm conduct its business with integrity and with due skill, care and diligence).

#### ***Overseas Regulators***

The Lloyd's market is authorised to underwrite insurance business in over 80 jurisdictions worldwide and, as a result of those authorisations, the Lloyd's market is subject to a range of overseas regulatory requirements. The Society maintains relationships with the overseas regulators in each of the jurisdictions where the Lloyd's market is licensed and also has systems and controls in place to ensure that all international regulatory requirements are met on behalf of the Lloyd's market. These requirements include providing overseas regulators with regulatory returns and audits and maintaining local financial deposits and trust funds requirements. The Society also closely monitors the overseas regulatory environment to ensure that it can effectively manage the impact of any changes in regulatory requirements overseas.

#### ***Solvency II***

The Solvency II Directive, which came into effect from 1 January 2016, replaced the previous EU regulatory framework for the prudential supervision of insurance and reinsurance companies and introduced more consistent risk sensitive standards to insurers' capital requirements.

Solvency II adopts a three pillar approach to prudential regulation:

- (i) Pillar 1 covers technical provisions, the SCR and Minimum Capital Requirement ("**MCR**"), rules on market consistent valuation, investment of assets and the use of internal models to calculate the SCR;

- (ii) Pillar 2 covers risk management, governance requirements, supervisory review and the ORSA of an insurer; and
- (iii) Pillar 3 covers public and supervisory reporting and disclosure.

A key aspect of Solvency II is the focus on a supervisory review at the level of the individual legal entity. Insurance companies are now encouraged to improve their risk management processes and are allowed to make use of internal economic capital models to calculate capital requirements, subject to regulatory approval. In addition, Solvency II requires firms to develop and embed an effective risk management system as a fundamental part of running the firm.

Solvency II requires firms to disclose a considerably greater level of qualitative and quantitative information than under the previous regime (Solvency I), both to their own supervisor through Regular Supervisory Reporting (“RSR”) and to the market through the publication of a Solvency and Financial Condition Report (“SFCR”). This is intended to increase transparency, allowing easier comparison across the industry and enabling supervisors to identify sooner if firms are heading for financial difficulty. In turn, increased transparency is intended to drive market discipline, arising from the reaction of ratings agencies and the capital markets to firms’ performance. See also “Regulatory solvency” above.

### **Reconstruction and Renewal and Equitas**

A flood of asbestosis and other long-tail claims in the early 1990’s meant that certain syndicates were exposed to large losses. The problems caused by such claims (and others) were addressed by the 1996 Lloyd’s Reconstruction and Renewal plan. As part of the plan, Equitas Reinsurance Limited, an independent special purpose reinsurer, was established to reinsure without limitation in time or amount all of the general business liabilities of open syndicates for the 1992 and prior years of account (including all business reinsured to close into those years of account). The reinsured amount totalled approximately £14.7 billion. In return for this reinsurance, all members were required to pay a premium to Equitas calculated in accordance with their estimated liabilities. In addition to the premiums received from members for the reinsurance provided, Equitas was funded by taking an assignment of the rights of syndicates to the proceeds from reinsurance contracts that they had taken out for their protection in respect of their 1992 and prior business. Equitas retroceded all of its reinsurance obligations to its subsidiary Equitas Limited (“EL”).

#### *Retrocession of Equitas Limited’s reinsurance obligations to National Indemnity Company (NICO)*

In 2006 EL entered into a retrocession and run-off contract with NICO, becoming effective on 27 March 2007, by which NICO provided to EL retrocession cover up to a limit of \$14.4 billion less adjustments for claims payments between 1 April 2006 and 27 March 2007. The premium for that retrocession was all of EL’s existing assets less £172 million plus a contribution of £72 million from Lloyd’s. This first phase of the transaction provided substantial additional retrocession cover for Equitas and for the Society’s subsidiaries, Lioncover and Centrewrite.

The second phase of the transaction involved the transfer of Equitas-reinsured members’ 1992 and prior non-life business to a specially authorised new insurance company, EIL. This transfer of business was sanctioned by the High Court under Part VII of the Financial Services and Markets Act 2000 on 25 June 2009 and the transfer became effective on 30 June 2009. As part of the second phase, a further contribution of £18m was made by the Society and EL also exercised an option to purchase \$1.3 billion of additional reinsurance from NICO at a cost of £40 million which resulted in policyholders benefitting from a total of \$7 billion reinsurance cover from NICO over and above EL’s net undiscounted claims reserves as at 31 March 2006.

The transfer also relieved the members and former members concerned from the transferred liabilities under English law and the law of every other state within the European Economic Area. Recognition of the Part VII has not been sought in the US.

### *Remaining Contingent Liabilities*

Following the completion of the second phase, the Society continues to have contingent liabilities arising from entering into undertakings for the benefit of certain policyholders of EIL (former policyholders of the PCW Syndicates or of members who at the relevant time still have the benefit of hardship or other agreements with the Society), under which the Society would meet any shortfall in recoveries by such policyholders from EIL on the occurrence of an insolvency event relating to Equitas Reinsurance Limited or EIL.

Following implementation of Reconstruction and Renewal, the liabilities of Lioncover and the pre-1992 liabilities of Centrewrite were also reinsured into Equitas (see “*Subsidiaries of the Society*”). The Society gave an indemnity bond to both Lioncover and Centrewrite against any shortfall of their assets. The Council determined that any losses resulting from such indemnities will be met by the Central Fund. Accordingly, if Equitas were unable to discharge in full the Lioncover and Centrewrite liabilities which it has reinsured, any resulting shortfall would be met out of the Central Fund under the terms of these indemnity bonds.

In 2009 the Lioncover bond was released and replaced by a substitute Lioncover bond. Equitas Policyholders Trustee Limited received the benefit, on behalf of the former policyholders of the PCW Syndicates, of the Lloyd’s undertakings set out in the substitute bond and under which Lloyd’s would meet any shortfall in recoveries by such policyholders from EIL on the occurrence of an insolvency event relating to Equitas Reinsurance Limited or EIL. This was undertaken as part of the 2009 transfer referred to above.

The Lloyd’s market has established two Joint Asset Trust Funds (“**JATFs**”) in the United States to support surplus lines policies and to support reinsurance policies. The Lloyd’s market is required to maintain at least \$100 million in the reinsurance JATF and at least \$100 million in the surplus lines JATF. As at 30 June 2016, the value of the reinsurance JATF and the surplus lines JATF were each approximately \$100 million. The Society is responsible for the investment management of the assets in the JATFs and adopts a low risk management policy with a view to minimising the risk of the value of each of the JATFs falling below their respective minimum amounts.

In the event that Equitas were unable to make payments in full on a claim by a US surplus lines or reinsurance policy allocated to a 1992 or a prior year of account, payment of any shortfall could be realised from the respective JATF. If the balance in such JATF were as a result to fall below their respective minimum amounts the Lloyd’s market would be required to replenish the funds in such JATF if it wished to continue to write such lines of business in the US. In such circumstances the Central Fund may be applied for this purpose.

The financial strength ratings of the Lloyd’s market assigned by Standard & Poor’s, Fitch Ratings and A.M. Best (see “*Lloyd’s market – General*”) take account of both phases described above and also the exposure of the Society and the Lloyd’s market to the failure of Equitas.

### **Reorganisation and Winding Up Directive**

The European Council Directive on the reorganisation and winding-up of insurance undertakings (2001/17/EC) (the “**Directive**”) was implemented in the UK in relation to the insurance company market in 2003 and in relation to the Lloyd’s market in 2005, by means of the Insurers (Reorganisation and Winding Up) (Lloyd’s) Regulations 2005.

The objective of the Directive is to establish co-ordinated rules for reorganisation and winding-up of insurance undertakings throughout the EU. The basic framework of the Directive is that only an insurer’s home Member State is entitled to take a decision in relation to the reorganisation or winding-up of the insurer. This decision must be recognised and given effect in all other Member States. The law of the home Member State will (subject to certain exceptions) govern the insolvency procedure. The Directive is therefore primarily concerned with mutual recognition of insolvency measures and conflict of laws.

In the case of Lloyd’s, the insurance undertaking to which the Directive applies is “the association of underwriters known as Lloyd’s”. The Directive therefore applies to the persons who carry on insurance business as members of Lloyd’s, taken collectively.

Members of Lloyd's can be subject to insolvency processes individually (the particular procedures which apply will depend on the precise legal status of the member). The Society is capable of being wound up by the court but cannot be the subject of an administration order.

Because the Directive engages at the "association" level it and the implementing regulations become relevant only when there is a risk of possible or actual breach of the Lloyd's regulatory solvency test, in relation to the liabilities and assets of all of the members taken together. In such an event the following steps under the Insurers (Reorganisation and Winding Up) (Lloyd's) Regulations 2005 are envisaged:

- The Society or the PRA may apply to the court to make a "Lloyd's market reorganisation order" which would involve the appointment of a "reorganisation controller". The making of that order would not constitute winding-up proceedings. The objectives of the order would be:
  - to preserve or restore the financial situation of, or market confidence in, the association of underwriters known as Lloyd's in order to facilitate the carrying on of insurance market activities by members of Lloyd's;
  - to assist in achieving an outcome that was in the interests of creditors of members, and insurance creditors in particular;
- a moratorium would be put in place for all entities in the market to allow the reorganisation to take place. However, it would not prevent payments of insurance liabilities by solvent members where appropriate;
- the reorganisation controller's role would be to prepare a market reorganisation plan for achieving the objectives of the order. The reorganisation controller would assess the level of difficulty and advise the court whether in the case of particular members there was likely to be a failure to satisfy that member's insurance creditors by applying the usual market arrangements (including the New Central Fund). He/she would need to have regard to the existence of viable parts of the market and the desirability of avoiding a situation where solvent members were unable to carry on business as usual;
- the reorganisation controller would seek to ensure that solvent members could continue normal trading and remove them from the scope of the moratorium as soon as possible; and
- normal insolvency procedures would apply to insolvent members. Whether or not the Central Fund is applied to meet the liabilities (in whole or in part) of such members is a matter for the Council. If insufficient assets were available the particular insolvent member would be treated individually as an insurance undertaking for the purpose of the requirements of the Directive.

The Central Fund is not an asset of the members who together constitute the undertaking to which the Directive applies, but rather of the Society itself. Under the implementing regulations once a Lloyd's market reorganisation order has been made then unless otherwise agreed in writing (as to any class of payments) between the Society, the PRA and the reorganisation controller, the Society would have to notify the reorganisation controller of any payments proposed to be made out of the Central Fund, and the reorganisation controller could object to particular payments. The Society would then be unable to make those payments without the permission of the court. The purpose of this provision is to ensure that the Society retains sufficient funds to maintain the infrastructure necessary to achieve the purposes of the reorganisation order, including the due payment of insurance claims.

In the event that a Lloyd's market reorganisation order was made the holders of the Notes would be affected by the moratorium. Given the subordinated nature of the Notes it is unlikely that the reorganisation controller would permit repayment of the Notes unless he was satisfied that prior senior creditor claims could be paid in full and that the Society retained sufficient funds to enable it to continue to perform functions essential for the fulfilment of the objectives of the order.

In the event of a winding-up of the Society the assets would be distributed in the following order of priority:

- (i) Preferential creditors (employees, etc).
- (ii) Senior creditors, i.e.
  - All creditors of the Society (including costs and expenses of winding-up) other than creditors ranking *pari passu* with or junior to the Notes.
  - Payments in respect of other legal obligations of the Society including the Hardship scheme and payments under the substitute Lioncover bond and the Centrewrite bond.
  - Payments under Central Fund Undertakings.
  - Discretionary applications out of New Central Fund to meet insurance liabilities of members unable to meet such liabilities other than an Excluded Payment.<sup>1</sup>
- (iii) Holders of the Notes (once issued) and the 2014 Notes.
- (iv) Repayment of Members' Loans (other than any Members' Loans which rank *pari passu* with the 2007 Notes).
- (v) Holders of the 2007 Notes.
- (vi) Return of surplus to members.

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<sup>1</sup> Excluded Payments are not permitted to be made under the terms of the New Central Fund.

## GLOSSARY OF TERMS

Set out below is a guide to Lloyd's-related terms which are used in this Prospectus. These are not precise definitions but are included to provide assistance to readers as to the general meaning of terms most commonly used in the Lloyd's market.

**callable layer** means 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** means 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** has the meaning given in Condition 18.

**Central Fund** has the meaning given in Condition 18.

**closed year** means a year of account to which no further adjustments are to be made and final accounts can be prepared. This can be done only after providing for all outstanding claims by way of reinsurance to close. At Lloyd's a year of account cannot be closed earlier than the third year of account.

**combined ratio** means 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 of over 100% is a loss.

**corporate member** means a company incorporated with limited liability, a limited liability partnership or a Scottish limited partnership, admitted to membership of the Society.

**Council** has the meaning given to "Council of Lloyd's" in Condition 18.

**Economic Capital Assessment (ECA)** means the funds required from members. The Society reviews each syndicate's SCR on an ultimate view of risk to assess the adequacy of the proposed capital level. When agreed, each SCR is then uplifted, by 35% for 2017, to ensure there is sufficient capital to support Lloyd's ratings and financial strength. This uplifted SCR forms the syndicate's Economic Capital Assessment and is then allocated to members based on their share of each syndicate they support to derive the members' Economic Capital Assessment.

**Equitas** means Equitas Limited and, where the context so requires, any subsidiary or holding company of Equitas Limited, or any other subsidiary of such holding company.

**Franchise Board** means the board established by the Council with responsibility for creating and maintaining a commercial environment at Lloyd's in which the long-term return to all capital providers is maximised. This includes setting the Risk Management Framework and profitability targets for the market.

**funds at Lloyd's (FAL)** means funds lodged and held in trust at Lloyd's as security for the policyholders and to support a member's overall underwriting activities. The minimum amount is determined by reference to a member's capacity, in accordance with ratios laid down by the Council.

**Gross Written Premiums (GWP)** means written insurance premiums, gross of reinsurance and acquisition costs.

**individual member** means a member of Lloyd's who is an individual.

**Managing agent** means an underwriting agent responsible for managing a syndicate, or multiple syndicates.

**Member** means a person admitted to membership of the Society.

**Members' Loans** means loans made by members to the Society pursuant to Syndicate Loan Requirements made by the Council on 2 March 2005 and are also known as 'syndicate loans'.

**New Central Fund** has the meaning given in Condition 18.

**Old Central Fund** means the fund constituted and governed by the Central Fund Byelaw (No.4 of 1986) made by the Council as amended from time to time.

**open year** means a year of account of a syndicate which has not been closed by reinsurance to close (which will usually occur at the end of the third year). A year of account can be left open beyond the third year if the extent of the liabilities cannot be accurately quantified or where there is no successor year of account to accept the RITC.

**premiums trust funds (PTF)** means trust funds into which all premiums received by a managing agent on behalf of a member must be placed and out of which reinsurance premiums, claims and syndicate expenses are met.

**Realistic Disaster Scenarios (RDSs)** means a series of scenarios, both natural and man-made, which are used to model the market's exposure to a variety of different catastrophes and to enable better risk management practices within Lloyd's.

**Reinsurance to close (RITC)** means 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.

**Society** means the Society and Corporation incorporated by Lloyd's Act 1871 by the name of Lloyd's.

**Special Purpose Arrangements (SPA)** means a syndicate that writes a single reinsurance contract of another "host" syndicate.

**syndicate** means a member, or group of members, underwriting insurance business at Lloyd's through the agency of a managing agent.

**year of account** means 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.

## ALTERNATIVE PERFORMANCE MEASURES

The following metrics, which are consistently used to analyse financial performance of the Lloyd's market, are considered to be Alternative Performance Measures (APMs) as defined in the European Securities and Markets Authority Guidelines on Alternative Performance Measures.

Metric	Definition	Reason for use
Combined ratio	Combined ratio is a measure of the profitability of an insurer's underwriting activity. It is the ratio of Net operating expenses plus Claims incurred net of reinsurance to Earned premiums net of reinsurance.	Combined ratio is used to measure the profitability of the underwriting activity across the Lloyd's market. It also serves as a comparator of the Lloyd's market's underwriting profitability to its peers.
Return on capital	Return on capital is a measure of overall profitability (pre-tax). It is the ratio of Result for the year before tax to the average of opening and closing total Capital and reserves.	Return on capital ratio is used to measure the overall profitability and value-creating potential of the Lloyd's market.
Investment return	Investment return is a measure of performance of an insurer's investing activity. It is the ratio of Total investment return to the average of opening and closing Financial investments and Cash at bank and in hand.	Investment return ratio is used to measure the performance of the portfolio of investments and cash balances held across the Lloyd's market.

## TAXATION

### General

The comments below are of a general nature and are not intended to be exhaustive. They assume that there will be no substitution of the Issuer and do not address the consequences of any such substitution (notwithstanding that such substitution may be permitted by the Conditions). Any Noteholders who are in doubt as to their own tax position should consult their professional advisers.

### United Kingdom Taxation

*The following is a summary of the Issuer's understanding of current United Kingdom law and published HM Revenue and Customs' practice relating only to the United Kingdom withholding tax treatment of payments of interest (as that term is understood for United Kingdom tax purposes) in respect of Notes and to the United Kingdom stamp tax treatment of the issue and transfer of the Notes. It does not deal with any other United Kingdom taxation implications of acquiring, holding or disposing of Notes. The United Kingdom tax treatment of prospective Noteholders depends on their individual circumstances and may be subject to change in the future. Prospective Noteholders who may be subject to tax in a jurisdiction other than the United Kingdom or who may be unsure as to their tax position should seek their own professional advice.*

#### ***Withholding tax treatment of payments of interest on the Notes***

Payments of interest on the Notes may be made without deduction of or withholding on account of United Kingdom income tax provided that the Notes carry a right to interest and the Notes are and continue to be listed on a "recognised stock exchange" within the meaning of section 1005 of the Income Tax Act 2007. The London Stock Exchange is a recognised stock exchange. Securities will be treated as listed on the London Stock Exchange if they are included in the Official List (within the meaning of and in accordance with the provisions of Part 6 of the Financial Services and Markets Act 2000) and admitted to trading on the London Stock Exchange. Provided, therefore, that the Notes carry a right to interest and are and remain so listed on a "recognised stock exchange", interest on the Notes will be payable without deduction of or withholding on account of United Kingdom income tax.

Payments of interest on Notes may also be made without deduction of or withholding on account of United Kingdom income tax if the Notes are "regulatory capital securities" for the purposes of the Taxation of Regulatory Capital Securities Regulations 2013 (the "**TCS Regulation**"). The Notes will constitute "regulatory capital securities" for the purposes of the TCS Regulations if the Notes qualify, or have qualified, as an item listed in point (a)(iii) or (b) of Article 72 of Commission Delegated Regulation (EU) 2015/35 (as amended from time to time) (the "**CDR**") which is a Tier 2 item under Article 72 or 79 of the CDR. This is subject to there being no arrangements the main purpose, or one of the main purposes, of which is to obtain a tax advantage (as defined in section 1139 of the Corporation Tax Act 2010) for any person as a result of the application of the TCS Regulations in respect of the Notes (the "**Anti-Avoidance Condition**").

In other cases, an amount must generally be withheld from payments of interest on the Notes that has a United Kingdom source on account of United Kingdom income tax at the basic rate (currently 20%), subject to any other available exemptions and reliefs. However, where an applicable double tax treaty provides for a lower rate of withholding tax (or for no tax to be withheld) in relation to a Noteholder, HMRC can issue a notice to the Issuer to pay interest to the Noteholder without deduction of tax (or for interest to be paid with tax deducted at the rate provided for in the relevant double tax treaty).

#### ***Stamp duty and stamp duty reserve tax on issue and transfer of the Notes***

The transfer of Notes that are "regulatory capital securities" for the purposes of the TCS Regulations as set out above and which satisfy the Anti-Avoidance Condition is exempt from United Kingdom stamp duty and stamp duty reserve tax.

### **The proposed financial transactions tax (FTT)**

On 14 February 2013, the European Commission published a proposal (the “**Commission’s Proposal**”) for a Directive for a common FTT in Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia (the “**participating Member States**”). However, Estonia has since stated that it will not participate.

The Commission’s Proposal has very broad scope and could, if introduced, apply to certain dealings in the Notes (including secondary market transactions) in certain circumstances. Primary market transactions referred to in Article 5(c) of Regulation (EC) No 1287/2006 are expected to be exempt.

Under the Commission’s Proposal the FTT could apply in certain circumstances to persons both within and outside of the participating Member States. Generally, it would apply to certain dealings in the Notes where at least one party is a financial institution, and at least one party is established in a participating Member State. A financial institution may be, or be deemed to be, "established" in a participating Member State in a broad range of circumstances, including (a) by transacting with a person established in a participating Member State or (b) where the financial instrument which is subject to the dealings is issued in a participating Member State.

However, the FTT proposal remains subject to negotiation between participating Member States. It may therefore be altered prior to any implementation, the timing of which remains unclear. Additional EU Member States may decide to participate.

Prospective holders of the Notes are advised to seek their own professional advice in relation to the FTT.

## SUBSCRIPTION AND SALE

Citigroup Global Markets Limited, Lloyds Bank plc and The Royal Bank of Scotland plc (trading as NatWest Markets) (together, the “**Joint Lead Managers**”) have, pursuant to a Subscription Agreement dated 3 February 2017, jointly and severally agreed with the Issuer, subject to the satisfaction of certain conditions, to subscribe (or procure the subscription) for the Notes at 99.944 per cent. of their principal amount. The Issuer has agreed to reimburse the Joint Lead Managers for certain of their expenses in connection with the issue of the Notes. The Subscription Agreement entitles the Joint Lead Managers to terminate it in certain circumstances prior to payment being made to the Issuer. The initial yield of the Notes for the period to (but excluding) the First Call Date is 4.882 per cent. on an annual basis. The yield is calculated as at the Issue Date on the basis of the issue price of the Notes. It is not an indication of future yield.

### **United States**

The Notes have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in certain transactions exempt from the registration requirements of the Securities Act. Terms used in this paragraph have the meanings given to them by Regulation S under the Securities Act.

Each Joint Lead Manager has represented and agreed that, except as permitted by the Subscription Agreement, it has not offered, sold or delivered and will not offer, sell or deliver the Notes, (i) as part of their distribution at any time or (ii) otherwise until 40 days after the later of the commencement of the offering and the Closing Date (as defined in the Subscription Agreement) within the United States or to, or for the account or benefit of, U.S. persons, and it will have sent to each dealer to which it sells the Notes during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Notes within the United States or to, or for the account or benefit of, U.S. persons.

In addition, until 40 days after the commencement of the offering, an offer or sale of the Notes within the United States by a dealer that is not participating in the offering may violate the registration requirements of the Securities Act.

### **United Kingdom**

Each Joint Lead Manager has represented and agreed that:

- (a) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) received by it in connection with the issue or sale of the Notes in circumstances in which Section 21(1) of the FSMA would not, if the Issuer was not an authorised person, apply to the Issuer; and
- (b) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Notes in, from or otherwise involving the United Kingdom.

### **General**

None of the Issuer or any Joint Lead Manager has made any representation that any action will be taken in any jurisdiction by the Joint Lead Managers, the Issuer that would permit a public offering of the Notes, or possession or distribution of this Prospectus (in preliminary, proof or final form) or any other offering or publicity material relating to the Notes (including roadshow materials and investor presentations), in any country or jurisdiction where action for that purpose is required. Each Joint Lead Manager has agreed that it will not, directly or indirectly, offer or sell any Notes or have in its possession, distribute or publish offering circular, prospectus, form of application, advertisement or other document or information in any country or jurisdiction except under circumstances that will, to the best of its knowledge and belief, result in compliance with any applicable laws and regulations and all offers and sales of Notes by it will be made on the same terms. No Joint Lead Manager has been authorised to make any representation or use any information in

connection with the issue, subscription and sale of the Notes other than as contained in this Prospectus or any amendment or supplement to it.

## GENERAL INFORMATION

1. The listing of the Notes on the Official List will be expressed as a percentage of their nominal amount (exclusive of accrued interest). It is expected that listing of the Notes on the Official List and admission of the Notes to trading on the Market will be granted on or around 7 February 2017, subject only to the issue of the Global Certificate. Prior to official listing and admission to trading, however, dealings will be permitted by the London Stock Exchange in accordance with its rules. Transactions will normally be effected for delivery on the third working day after the day of the transaction. The total expenses related to the admission to trading are estimated to be £4,200.
2. The Issuer has obtained all necessary consents, approvals and authorisations in connection with the issue and performance of the Notes. The issue of the Notes was authorised pursuant to a resolution of the Council of Lloyd's dated 7 December 2016 and a resolution of the Committee of the Council of the Society passed on 24 January 2017.
3. There has been no significant change in the financial or trading position of the Issuer and its consolidated subsidiaries taken as a whole (the “**Group**”) since 30 June 2016. There has been no material adverse change in the financial position or prospects of the Group since 31 December 2015.
4. The Issuer is not or has not been involved in any governmental, legal or arbitration proceedings (including any proceedings which are pending or threatened of which the Issuer is aware) during the 12 months preceding the date of this Prospectus which may have, or have in such period had, a significant effect on the financial position or profitability of the Issuer.
5. The Notes have been accepted for clearance through the Euroclear and Clearstream, Luxembourg systems (which are the entities in charge of keeping the records). The Common Code is 155808926 and the International Securities Identification Number (ISIN) is XS1558089261.

The address of Euroclear is 1 Boulevard du Roi Albert II, B-1210 Brussels, Belgium and the address of Clearstream, Luxembourg is 42 Avenue JF Kennedy, L-1855 Luxembourg.

6. The financial statements of the Group for the years ended 31 December 2014 and 31 December 2015 have been audited by PricewaterhouseCoopers LLP, Chartered Accountants (members of the Institute of Chartered Accountants in England and Wales) and Registered Auditors (authorised and regulated by the FCA for designated investment business), in each case in accordance with Auditing Standards issued by the Auditing Practices Board, and have been reported upon without qualification. The business address of PricewaterhouseCoopers LLP is 1 Embankment Place, London WC2N 6RH.
7. Copies of the following documents will be available, during usual business hours on any weekday (public holidays excepted), for inspection at the office of the Principal Paying Agent from the date of this Prospectus:
  - (a) the Lloyd's Acts and Byelaws;
  - (b) the documents incorporated by reference in this Prospectus;
  - (c) the Trust Deed;
  - (d) the Agency Agreement; and
  - (e) a copy of this Prospectus together with any supplement to this Prospectus or further Prospectus.

This Prospectus will be published on the website of the Regulatory News Service operated by the London Stock Exchange at [www.londonstockexchange.com/exchange/news/market-news/market-news-home.html](http://www.londonstockexchange.com/exchange/news/market-news/market-news-home.html).

8. The Joint Lead Managers and their affiliates have engaged, and may in the future engage, in investment banking and/or commercial banking transactions with, and may perform services to the Issuer and/or its affiliates in the ordinary course of business.

**REGISTERED OFFICE OF THE ISSUER**

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**The Royal Bank of  
Scotland plc (trading as NatWest**

**Markets)**  
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*To the Joint Lead Managers and the Trustee*

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