

Lloyd's Members Agency Services Limited

Our ref: LMAS/CFT/JAM/«MEMBER_CODE»

5 February 2009

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«COUNTRY»

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MEMORANDUM

SYNDICATE 566 2000 YEAR OF ACCOUNT

I enclose, for your information, a copy of a letter I have received from QBE Underwriting Limited, (QBE) the managing agent of Syndicate 566 advising of a proposal to close the above year of account at 31 December 2008.

You will note for the reasons stated that QBE is suggesting a RITC into their wholly aligned Syndicate 2999 could prove to be a realistic proposition and is likely to produce a release of 5.4% of capacity in respect of the 2000 year of account. I enclose a schedule detailing your involvement in the above run-off year and the effect this potential release could have upon you. Names will be aware from our previous newsletters of the syndicate's involvement in the World Trade Center loss of 11 September 2001 upon which QBE have quoted in some detail.

Although, as QBE states the proposal is non-negotiable, it is not without merit particularly when bearing in mind the previous attempt to secure closure which would have resulted in further costs to Names.

The members agency community considers this a realistic proposition and one we are all minded to support. If, however, you have any questions to raise, or objections to the proposal, please advise me as quickly as possible, bearing in mind the tight reporting schedule and the fact that we have to advise QBE of our Names support by no later than **Monday 23 February 2009**.

«LetterName»

Encs.



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Ref: V:\Operations\KB\Letters\2009\03-02-09 Ltr to Capital Providers re 566 2000 Open Year.doc

3rd February 2009

Paul Box
Lloyd's Market Services
Floor 2, Fidentia House
Walter Burke Way
Chatham Maritime
Kent
ME4 4RN

Dear Paul

SYNDICATE 566 2000 OPEN YEAR

I am writing to update you on Syndicate 566's 2000 open year performance and RITC proposal.

2008 Year End Solvency Result

Syndicate 566's 2000 and prior open years produced a solvency surplus of 11.4% of capacity during the 2008 calendar year. This equates to a cumulative open year surplus to date of 10.7% (excluding Names' non-standard personal expenses). It is not our intention to distribute any solvency surplus during 2009.

RITC Proposal

The sole barrier to the closure of the 2000 year to date has been the well publicised uncertainties surrounding the aviation World Trade Centre (WTC) losses of 11th September 2001. You will recall that, at the end of 2006, we proposed closing the year into QBE's wholly aligned corporate syndicate, Syndicate 2999, at a loss to Names of 15% of capacity. Following consultation, the decision was then taken to leave the year open until sufficient certainty was achieved to affect a reinsurance to close (RITC) that was satisfactory to all capital providers. This was estimated to be no earlier than the end of 2010.

Whilst material uncertainties remain, particularly with regards the potential for subrogation by property insurers against aviation insurers, there have been sufficient positive developments to warrant a review of the RITC options. Those developments include:

- The majority of claimants who didn't sign up to the US Government's Victim Compensation Fund (VCF) have now had their claims settled broadly within expectation
- Continued market consensus that the four event scenario is the most applicable
- Stability in the non-WTC reserves
- New market entrants offering third party RITC

As a consequence we approached and entered into discussions with an external RITC provider in the summer of 2008. Those discussions were concluded in January 2009, however due to the materiality of the prevailing uncertainties and the penal cost of capital required, they were unable to provide a quote which was either satisfactory in quantum or achieved finality.

It was appropriate, however, to revisit the potential for an internal RITC into our wholly aligned Syndicate 2999. That exercise has now been concluded and I am pleased to propose the closure of Syndicate 566's 2000 open year into Syndicate 2999 at a final cumulative profit to Names of 5.4% of capacity (excluding Names' non-standard personal expenses).



RITC Rationale

The attached Appendix I summarises the key RITC statistics (as at QBE year end ROE of US\$1.46). As highlighted, the 2000 and prior years produced a 2008 calendar year surplus of £16.8m or 11.4% of capacity. This equates to a cumulative result to date of £15.8m or 10.7% of capacity and reflects:

- A pure solvency result with no risk premium;
- Total claims reserves of £134.2m gross, £55.5m net; including
- WTC aviation reserves maintained on a pure four event basis totalling £88.6m (US\$129.4m) gross, £22.2m (US\$32.4m) net (after accounting for inwards and outwards reinstatement premium);
- Surpluses arising from continued improvements in the non-WTC accounts;
- Reinsurance bad debt reserves of £5.7m;

In arriving at the proposed RITC, consideration has been given to both the potential upside and downside of the main issues:

- With regard to WTC, the Syndicate continues to maintain reserves on a pure four event policy limit basis, consistent with most of the direct airline market. Improvement on this position could be achieved if airline liability limits are not exhausted, however this is not considered likely. Whilst the consensus is that four events will prevail, there remains the potential for three events, which on a pure inwards and outwards basis, would be a net negative impact to the Syndicate of £18.0m (US\$26.3m) or 11.8% of capacity.

In reality however, if the market were to settle on a three event basis, the Syndicate's position would be significantly worse, as many clients have an "each and every aircraft" option for collection purposes and hence inwards claims would be considerably higher.

- With regard to the non-WTC accounts, the surpluses experienced to date reflect the conclusion in 2008 of an actuarial review of reserves and are therefore not expected to continue going forward. Claim reserves are now broadly in line with external actuarial estimates however, it should be noted that there remain some long tail exposures, particularly in the marine liability account.
- With regard to reserves for reinsurance bad debt, the solvency result at 31st December 2008 includes a provision of £5.7m, based on standard S&P default rates. This equates to 7.2% of total recoveries assumed of £78.6m. The majority (£61.0m) of these recoveries are in respect of WTC, which have a higher potential for dispute and/or default.

In light of the above uncertainties, the RITC proposal includes a risk premium of £7.9m, equating to 16.9% of total net reserves or 5.4% of capacity, broken down as follows:

	Risk Premium £000's	Rationale
WTC 3 event	4,499	25% of £18m minimum potential downside
WTC Bad debt	2,168	10% of recoveries due, less existing provision
Non-WTC deterioration	1,231	5% of total non-WTC net reserves
Total	7,898	

QBE Corporate Limited provides 60.5% of capital to the 2000 open year, hence the third party capital share of the risk premium equates to £3.1m.



Summary

This proposal has been reviewed and approved by QBE European Operations' General Business Committee, a delegated sub-committee of QBE Underwriting Ltd [QUL] and remains subject to formal ratification by QUL at its next scheduled meeting on 10th February 2009. It should be noted that, subject to any amendments arising from that meeting, this proposal is non-negotiable. In the event that sufficient approval is not secured from third party capital providers, the year will continue to remain open and no solvency surplus will be distributed.

We would be happy to meet with members agents to discuss further, however in order to comply with the year end reporting timetable, if you are in favour of the proposal to close the open year, I would appreciate your written affirmation on behalf of your Names by no later than Monday 23rd February 2009.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Robert Nias', with a large, sweeping flourish above the name.

Robert Nias
Franchise and Reporting Director

cc: Steven McCann, Lloyd's Open Year Management



QBE UNDERWRITING LIMITED

Appendix I

SYNDICATE 566 2000 & PRIOR YEARS

RITC ANALYSIS AS AT 31st DECEMBER 2008

US\$ ROE
1.460394

1 Syndicate Capacity (£000's) 147,571

2 Solvency Result	£000's	% of Cap
Cumulative to 31/12/07	-927	-0.6%
Calendar year 2008	16,763	11.4%
Total	15,836	10.7%

3 Reserve Analysis (excluding bad debt and claims handling provisions)

3a Total Reserves		O/S + IBNR Claims £000's	Reinst. Premiums £000's	RITC Total £000's
WTC Avn 4 Event	Gross	88,604	9,545	79,059
	R/I	60,980	4,095	56,885
	Net	27,624	5,450	22,174
Other	Gross	45,550	4,135	41,415
	R/I	17,665	878	16,787
	Net	27,885	3,257	24,628
Total	Gross	134,154	13,680	120,474
	R/I	78,645	4,973	73,672
	Net	55,509	8,707	46,802

3b WTC Avn 4 event vs 3 event		O/S + IBNR Claims £000's	Reinst. Premiums £000's	RITC Total £000's	O/S + IBNR Claims US\$000's	Reinst. Premiums US\$000's	RITC Total US\$000's
Pure 4 Events	Gross	88,604	9,545	79,059	129,397	13,939	115,457
	R/I	60,980	4,095	56,885	89,055	5,980	83,075
	Net	27,624	5,450	22,174	40,342	7,959	32,383
Pure 3 Events	Gross	77,882	9,269	68,613	113,739	13,537	100,202
	R/I	32,729	4,286	28,443	47,797	6,259	41,538
	Net	45,154	4,984	40,170	65,942	7,278	58,664
Variance	Gross	-10,722	-276	-10,446	-15,658	-402	-15,255
	R/I	-28,251	191	-28,442	-41,258	279	-41,537
	Net	17,530	-466	17,996	25,600	-681	26,281

5 Bad debt Provision (£000's) 5,697

6 Risk Premium Calculation		£000's	% of Net RITC	% of Cap	Rationale
WTC	3 event	4,499	9.6%	3.0%	25% of £18m minimum potential downside 10% of total recoveries due, less existing provision
	Bad debt	2,168	4.6%	1.5%	
Non-WTC	Reserves	1,231	2.6%	0.8%	5% of non-WTC reserves
Total		7,898	16.9%	5.4%	

7 Final Result 7,938 5.4%