

LANCASHIRE INSURANCE COMPANY (UK) LIMITED
(the "Company")

BOARD OF DIRECTORS
TERMS OF REFERENCE

Purpose

Without prejudice to the exercise of the general powers of the Board of directors in accordance with the company's articles of association, any resolutions of the Company or under the general law, the Board's purpose shall be to undertake the following duties and obligations at the indicated intervals to ensure the effective oversight of the operation of the Company:

Duties and responsibilities

Management Organisation

1. The Board should consider annually the organization of the Company's management. In particular, the responsibilities for apportionment and oversight, finance, compliance, risk management and human resources, should be allocated to the executive directors of the Board or the then current allocation of responsibilities be confirmed.
2. The Board shall record annually the extent of any delegation of its powers to individual directors or to senior managers within the Company.
3. The Board shall record annually the extent and effectiveness of the key control documentation produced or adopted by the Company.
4. The Board shall record annually the extent and effectiveness of the Company's enterprise risk management framework ('ERM') and ORSA in particular in relation to the validation and evaluation of its internal model to assist the Board in making material business decisions. This shall include an annual review of the effectiveness of the Company's policies in relation to risk management, internal control, internal audit and outsourcing.
5. The Board shall annually consider and review the current committee structure, if any. In particular, the Board should consider the terms of reference of any committees of the Board, their composition, and reporting obligations to the Board. The Board shall cause a record to be kept of any such delegation, terms of reference and reporting requirements.
6. The Board shall consider and adopt annually a high level strategy plan and budget ("business plan") for the Company. The business plan should include,

amongst other things, premium projections, reinsurance spend, claims development, product lines, assumptions made affecting the projected performance of the Company and the sensitivity of performance to changes in key assumptions, in the context of the Company's risk tolerances, limits and appetites.

7. The Board on an annual basis shall satisfy itself that an appropriate process exists for the remuneration of those staff whose services are provided to the Company.

Enterprise Risk Management

1. In light of the Company's business plan, the Board shall review the controls that are in place in relation to identified risks. The directors who have been given responsibility in relation to underwriting, compliance, claims, reinsurance and financial matters shall be responsible for ensuring the controls are implemented and for reporting to the Board on a periodic basis regarding any significant issues that arise.
2. Quarterly, the Board shall receive a report from the Chief Risk Officer which will facilitate them in their evaluation of the overall effectiveness Company's ERM framework and ORSA, including the Company's risk appetite, risk tolerances and risk management strategy and the use of the Company's internal model. The report will identify where improvements can be made to the risk management function and in addition update the Board on developments in respect of areas of improvement previously identified.
3. The director with responsibility for human resources, shall be responsible for monitoring the arrangement for the provision of staff to the Company. That director shall also monitor staff levels and consider alternatives if key individuals should leave the group.

Financial Results

1. Quarterly, review the financial results of the Company and the Group for the prior reporting period;

Reinsurance

1. Quarterly, review reinsurance of the Company's risks, including (i) outstanding exposure to third-party reinsurers, and (ii) ratings of and material credit events occurring with respect to its third-party reinsurers;

Audit

1. Annually, and, if, deemed appropriate, following the advice of the Audit Committee (a) recommend the appointment or reappointment of the Auditors, after considering the firm's independence, performance, quality of work, and

cost, (b) approve in advance any request by management for a formal second opinion because of a disagreement with the Auditors regarding financial statement presentation or disclosure, (c) obtain from the Auditors, as promptly as practical after the conclusion of each Audit:

- i. a report detailing the scope of the work performed; and
- ii. a “Management Letter” outlining the Auditors’ findings and recommendations with respect to the Company’s internal controls and accounting procedures, including recommendations with respect to operational improvements;

(d) obtain from management a copy of its response to the Auditors’ Management Letter; and (e) review with the Auditors and management the items described above.

Group Risk

1. Obtain and review reports of audits of the Company conducted.
2. Regular review of financial reports on other Group companies.
3. Monitor at each meeting the free assets available to the company or the solvency margin required of the Company in connection with an assessment of whether to call on the Company’s parent to provide additional capital.
4. Prepare a summary report on the Company’s activities in the quarter that will be available to other group companies to make such companies aware of the Company’s obligations and performance.

Compliance Risk

1. The Board shall appoint or confirm the appointment of the Company’s compliance officer.
2. The compliance officer shall report at each Board meeting on compliance issues.

Legal Risk

1. Legal Counsel to the Company shall be responsible for monitoring developments in the insurance and legal world that may affect the Company. For example, counsel shall report to the Board any significant cases affecting the interpretation or validity of products offered by the Company.
2. Counsel shall also be responsible for ensuring with underwriters that policy wordings are suitably drafted and reviewed in the light of legal developments.

3. No new product may be offered by the Company before sign off by the Counsel to the Company.

Management Information

1. The Board shall consider their management information requirements each year and the Finance Director shall be responsible for ensuring the management information, in accordance with those requirements, is submitted at each quarterly board meeting.
2. Without prejudice to the above, the management information shall include:
 - Quarterly profit and loss data.
 - Comparison of outcome to budgeted expectation and explanations of variances.
 - Valuation of assets and projections in various scenarios to stress test the adequacy of the Company's reserves.
 - The performance of reinsurance coverage.
 - Number of claims in last period.
 - Number of complaints and how dealt with in the last period.
 - Credit reports on insureds, highlighting in particular any downgrades.

Membership

The Board meeting is chaired by the Non-Executive Chairman of the Company. For a Board meeting to be quorate at least two directors need to be present. The directors shall be appointed upon recommendation of the Board and upon consideration of the skills that they possess and subject to the approval of the relevant regulatory authorities.

Attendees

The Chairman may at his or her discretion invite other individuals who are neither directors nor officers of the Company to attend all or part of any Board meeting.

Meetings

In the absence of the Chairman of the Board, the directors present at a quorate meeting shall appoint one of their number to be the Chairman pro tem.

The Chairman shall be entitled to chair all regular sessions of the Board meeting and agree the agenda structure, order and items.

Secretary

The Board will appoint a Company Secretary who will be an appropriately constituted officer of the Company who shall minute the action points arising and the names of those present and in attendance. In the event that the Company Secretary is absent then the directors present shall appoint either one of their number or any other individual to act as minutes secretary.

Schedule of Matters Reserved for decision by the Board of Directors

An effective Board controls the business but delegates day to day responsibility to the executive management. That said, there are a number of matters which are required to be, or in the interests of the Company, should only be decided by the Board of Directors as a whole. It is important that the Board makes it clear what these matters reserved for decision by the Board are.

Delegation

Certain matters may be delegated to or be subject of recommendation from the:-

1. Audit Committee;
3. Remuneration Committee;
4. Executive Committee; or
5. A Committee constituted by another company within the Lancashire group.

At the discretion of the Chairman these Committees may be required to provide regular written or oral reports to the Board at all its regular meetings in relation to their activities.

Items marked * are not considered suitable for delegation to a Committee of the Board.

1	Strategy and Management
1.1	Responsibility for the oversight of the management of the Company.
1.2	Approval of the Company's annual operating and capital expenditure budgets and any material changes to them.
1.3	Approval of the Company's investment strategy.
1.4	Review of performance in the light of the Company's strategy, objectives, business plans and budgets and ensuring that any necessary corrective action is taken.
1.5	Extension of the Company's activities into new business or geographic areas for consideration or commitments or other value not exceeding US\$10 million.
1.6	Any change in the Company's registered office domicile or status.*
1.7	Review of the compensation framework that may be applied to the Company's employees in whole or in part.
2	Structure and capital
2.1	Any changes to the Company's capital

	structure.
2.2	Material changes to the Company's management and control structure.
2.3	Approval of the dividend policy.*
3	Financial Reporting and controls
3.1	Review of management accounts
	Reports from the Company's Compliance Officer.*
3.2	Approval of the annual report and accounts.*
3.3	Discussion of any possible qualification to the accounts.*
3.4	Approval for any dividend of the Company.*
3.5	Approval of any significant changes in accounting policies or practices.*
4	ERM and Internal Controls
4.1	Maintaining oversight of the quality, effectiveness, resources and utility of the Company's arrangements concerning ERM.
4.2	Ensuring maintenance of a sound system of internal controls.
5	Contracts and transactions
5.1	Capital projects, not explicitly approved within the Group Annual Budget which relate solely or materially to the operation of the Company and below a value of US\$10 million.
5.2	Approval of contracts (other than insurance and reinsurance contracts entered into in the ordinary course of the Company's insurance and reinsurance business) involving expenditure in excess of \$200,000 per annum, but below a value of US\$10 million.
5.3	Consideration of any transaction, proposal or investment which is specifically referred to the Board by a Director.
6	Board membership and other appointments
6.1	Changes to the structure, size and composition of the Board.*
6.2	Ensuring adequate succession planning, training, development and appraisal for the board and senior management.*

6.3	Appointment to the Board.*
6.4	Selection of the Chairman of the Board and the Chief Executive Officer.*
6.5	Membership and chairmanship of board committees.*
6.6	Continuation in office of any director at any time, including the suspension or termination of service of an executive director as an employee of the Company, subject to the law and the conditions of the service contract.*
6.7	Appointment or removal of the Company Secretary.*
6.8	Appointment or removal of any individual carrying out an FSA regulated controlled function on behalf of the Company.*
6.9	Appointment, reappointment or removal of the external auditor to the Company following the recommendation of the Audit Committee.*
7	Delegation of Authority
7.1	The division of responsibilities between the executive directors and non-executive directors.*
7.2	Approval of terms of reference of board committees.*
7.3	Receiving reports from board committees on their activities.*
8.	Policies
8.1	Review of the Company's corporate governance arrangements.
8.2	Determining the independence of Directors.*
8.3	Considering the balance of interests between shareholders, employees, customers and the community.*
8.4	The approval of policies, procedures and processes for the Company.
9	Other
9.1	Any actual or likely litigation where the exposure of the Company exceeds US\$100,000.
9.2	Any material fine (in excess of US\$100,000), prosecution, disciplinary action or censure proposed to be taken or imposed against the Company or any

	subsidiary by any government or regulatory body, or any material regulatory breaches.
9.2	This schedule of matters reserved for board decisions.

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APPENDIX TO THE BOARD OF DIRECTORS'
TERMS OF REFERENCE
IN RELATION TO RISK MANAGEMENT

Matters for the Board to consider in relation to the execution of its risk management responsibilities are:-

- i. that a clearly defined risk management function has been implemented, that the risk strategy documents the risk management function's objectives and key principles and that it is consistent with the Company's overall business strategy;
- ii. that the Company's risk tolerance limits have been properly documented and the assignment of responsibilities for risk management have been properly documented;
- iii. that the risk management function has adopted written policies that effectively define and categorise the material risks to which the Company is exposed and the approved risk tolerance limits for each type of material risk;
- iv. that reporting procedures and processes which ensure that information on the material risks faced by the Company and the effectiveness of the risk management function are established and actively monitored and analysed. That, as appropriate, modifications to the function are made;
- v. that the executive decision making of the Company is informed by the information reports provided by the risk management function; and
- vi. that the Company shall undertake stress and scenario analysis as appropriate in relation to all relevant risks faced by it carried out by its risk management function.