

Underwriting practice

At the end of this unit, candidates should be able to demonstrate an understanding of the:

- business, regulatory and legal environment of underwriting;
- main influences on underwriting strategy;
- principles and practices of risk pricing.

Assumed knowledge

It is assumed that the candidate already has knowledge of the fundamental principles of insurance as covered in IF1, Insurance, legal and regulatory, or equivalent exams.

Summary of learning outcomes

1. Understand key aspects of the regulatory and legal environment of underwriting;
2. Know the main influences on underwriting;
3. Understand underwriting policy and practice;
4. Understand the main statistical techniques of measuring risks and relationships and their application to insurance;
5. Understand the role and significance of reinsurance;
6. Understand the principles and practices of risk pricing.

Notes:

- **The syllabus is examined on the basis of English Law and practice unless otherwise stated.**
- **The April session will test the legal position as of 31 August of the preceding year.**
- **The October session will test the legal position as of 28 February of the same year.**

1. Understand key aspects of the regulatory and legal environment of underwriting

- 1.1 The implications of FSA authorisation of the underwriting function;
- 1.2 The relationship between underwriting and capital and solvency requirements;
- 1.3 Implications of writing international business;
- 1.4 Implications of granting delegated authority;
- 1.5 Initiatives to gain greater contract certainty.

2. Know the main influences on underwriting

- 2.1 **The corporate underwriting strategy**
 - 2.1.1 The different types of underwriting strategy;
- 2.2 **Influences on the underwriting strategy**
 - 2.2.1 The competition for capital investment and return on capital;
 - 2.2.2 The tension between growth in market share and profit;
 - 2.2.3 The operation of the traditional underwriting cycle;
 - 2.2.4 The impact of legislation and litigation – terrorism, mesothelioma, contaminated land, the Motor Insurers Bureau;
 - 2.2.5 The impact of major events and trends – weather, terrorism, pandemics and emerging risks;
 - 2.2.6 The marketing strategy – use of branding, distribution channels and commissions.

3. Understand underwriting policy and practice

- 3.1 The importance of moral and physical hazards in setting an underwriting policy;
- 3.2 Typical criteria for policy cover, terms, conditions and restrictions;
- 3.3 Liaison between underwriting and claims functions, especially reserving;
- 3.4 Establishing risk classification and categorisation;
- 3.5 Establishing underwriting and risk improvement criteria;
- 3.6 Considering exposure to single risks and events – balancing the account;
- 3.7 Use of binding authorities and line slips;
- 3.8 Counter-fraud initiatives.

4. Understand the main statistical techniques of measuring risks and relationships and their application to insurance

- 4.1 **Principles**
 - 4.1.1 Measures of central tendency;
 - 4.1.2 The basic principles of probability;
 - 4.1.3 The law of large numbers and sample sizes;
 - 4.1.4 The relationship between frequency and severity;
 - 4.1.5 The meaning of correlation and regression.
- 4.2 **Application to insurance**
 - 4.2.1 Application of the above techniques to claims data;
 - 4.2.2 The ability to manage and analyse very large samples of homogeneous risks and its impact on the pricing of personal and motor risk portfolios;
 - 4.2.3 The use of current statistical knowledge to predict future performance;
 - 4.2.4 The difficulty of anticipating less-frequent and complex events.

5. Understand the role and significance of reinsurance

- 5.1 **The main types of reinsurance;**
- 5.2 **The main approaches to reinsurance programmes;**
- 5.3 **The aggregation of events and risks and the use of catastrophe modelling;**
- 5.4 **The typical reinsurance pricing cycle and its impact on the underwriting acceptance policy and pricing of risks;**
- 5.5 **The reinsurer's requirement for quality information, and the cost implications of better quality data.**

6. Understand the principles and practices of risk pricing

- 6.1 The three main elements of the premium;
- 6.2 The burning cost basis and the alternative prospective risk analysis method of risk assessment;
- 6.3 Claims data – interpretation and its use in setting prices;
- 6.4 The significance of the IBNR (incurred but not reported claims);
- 6.5 Competitor analysis – its use and significance;
- 6.6 Other risk data – for example, river flood maps;
- 6.7 The importance of the underwriting function liaising with the claims function with regard to trends in reporting and reserving;
- 6.8 The role and significance of the actuary in risk pricing.

Reading list

The following list provides details of various publications which may assist with your studies. Periodicals and publications will be of value in ensuring candidates keep up to date with developments and in providing a wider coverage of syllabus topics. Any reference materials cited are authoritative, detailed works which should be used selectively as and when required.

Note: The examination will test the syllabus alone. The reading list is provided for guidance only and is not in itself the subject of the examination.

CII/Personal Finance Society members can borrow most of these additional study materials from CII Knowledge Services and may be able to purchase some at a special discount. For further information on lending and discounts go to www.cii.co.uk/knowledge.

Underwriting practice. London: Chartered Insurance Institute. Coursebook P80.

The prudential regulation of insurance companies. Tony Wiltshire. London: CII Knowledge Services. Updated as necessary. Available online at www.cii.co.uk/knowledge/factfiles (CII/PFS members only).

Recent developments in general insurance underwriting. Gavin Dollings. London: CII Knowledge Services. Updated as necessary. Available online at www.cii.co.uk/knowledge/factfiles (CII/PFS members only).

Periodicals

The Journal. London: Chartered Insurance Institute. Six issues a year. Also available online (CII/Personal Finance Society members only) at www.cii.co.uk/knowledge.

Post Magazine. London. Incisive Financial Publishing.

Technical Focus. Underwriting Faculty. London: CII Knowledge Services. Six issues a year. Available online at www.cii.co.uk/knowledge/underwriting (CII/Personal Finance Society members only).

Reference materials

Dictionary of Insurance. C Bennett. 2nd ed. London: Pearson Education, 2004. Also available online at www.cii.co.uk/knowledge/doi (CII/Personal Finance Society members only).

Examination guides

Guides are produced for each sitting of written answer examinations. These include the exam questions, examiners' comments on candidates' performance and key points for inclusion in answers. You are strongly advised to study guides for the last two sittings. Please visit www.cii.co.uk to buy online or contact CII Customer Service for further information on 020 8989 8464. Older examination guides are available (for members only) at www.cii.co.uk/knowledge/examguides.

Exam technique/study skills

There are many modestly priced guides available in bookshops. You should choose one which suits your requirements. You will also find advice at www.cii.co.uk/knowledge/careersupport (CII/Personal Finance Society members only).

For a more interactive approach, you should consider: Winning the brain game. London: CII, 2006. CD-ROM.