Specimen coursework assignment and answer

960 Advanced underwriting

The specimen coursework assignment and answer provides a guide as to the style and format of coursework questions. These examples indicate the depth and breadth of answers sought by CII markers.

The answer given is not intended to be the definitive answer. Well-reasoned alternative answers can also gain marks.

Before commencing work on your coursework assignment, you need to familiarise yourself with the following documents:

- *Coursework assessment guidelines and instructions*
- *How to approach coursework assignments*
- *Explaining your results notification*

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Coursework submission rules and important notes

Before you start your assignment, it is essential that you familiarise yourself with the *Coursework assessment guidelines and instructions* available on RevisionMate.

This includes the following information:

- These questions must not be provided to, or discussed with, any other person regardless of whether they are another candidate or not. If you are found to have breached this rule, disciplinary action may be taken against you.
- Important rules relating to referencing all sources including the study text, regulations and citing statute and case law.
- Penalties for contravention of the rules relating to plagiarism and collaboration.
- Coursework marking criteria applied by markers to submitted answers.
- Deadlines for submission of coursework answers.
- There are 80 marks available per coursework assignment. You must obtain a minimum of 40 marks (50%) per coursework assignment to achieve a pass.
- Your answer must be submitted on the correct answer template in Arial font, size 11.
- Your answer must include a brief context, at the start of your answer, and should be referred to throughout your answer.
- Each assignment submission should be a maximum of 3,200 words.
- Do not include your name or CII PIN anywhere in your answer.

Top tips for answering coursework assignments

- Read the *Specimen coursework assignment and answer* for this unit, available on RevisionMate.
- Read the assignments carefully and ensure you answer all parts of the assignments.
- You are encouraged to choose a context that is based on a real organisation or a division of an organisation.
- For assignments relating to regulation and law, knowledge of the UK regulatory framework is appropriate. However, marks can be awarded for non-UK examples if they are more relevant to your context.
- There is no minimum word requirement, but an answer with fewer than 2,800 words may be insufficiently comprehensive.

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Assignment

Provide a brief context for an insurer or a reinsurer, or a division of either, with which you are familiar.

For **this** insurer or reinsurer, or division of either:

- Explain **one** significant insurance product that is negatively affecting the profitability.
- Analyse, based on your explanation, how the underwriting acceptance criteria influences the profitability of this product.
- Make recommendations, based on your analysis, to improve the profitability of this product.

Note:

You are recommended to discuss your own organisation, or one that is familiar to you.
Your answer is confidential to the CII and will not be shared. For this specimen answer, which is widely publicised, a fictitious company has been chosen so as not to highlight any particular company.

To be completed before submission:

Word count:	3,181

Start typing your answer here:

Brief context:

ABC Group (ABC) is one of the largest insurers in the world, a multinational general insurance company headquartered in London, but providing insurance to over 100 countries. The company provides both personal and commercial insurance and a range of classes of business under each of these sectors.

The Lloyd's Glossary provides the following definition for a class of business:

'A description of a type of insurance or reinsurance business based on the risks being covered. The Lloyd's market underwrites eight main classes of insurance and reinsurance business: reinsurance, property, casualty, marine, energy, motor, aviation and life. Each of these main classes consist of a number of sub-classes'[1]

This assignment will be focused on the Liability class of business (often also referred to as casualty). All the products within this class of business are built around providing cover for claims made against an insured by third parties, but this assignment will specifically focus on

[1] https://www.lloyds.com/common/help/glossary?page=4

professional indemnity insurance, a sub-class of Liability, designed to ‘protect an individual or business against claims made by clients for loss or damage due to negligent advice or services.’[2]

The UK Professional Indemnity division for ABC has a gross written premium of £85 million, consisting of income from both the London City and regional accounts. This income is derived from various forms of distribution, mainly being binders, a wide broker network and online systems.

Explanation of one significant insurance product that is negatively affecting the profitability of a class of business

It has already been determined that all the products offered by the Professional Indemnity (PI) division are aimed at offering cover for claims against professionals for any loss caused to third parties as a result of their negligent advice or omission.

ABC splits the PI offering into four main categories: accountants, engineers, property professions and miscellaneous (including technology and media). Of these four categories, accountants PI is the main product offering, and ABC are considered one of the leading insurers in the market and approved by both the Institute of Chartered Accountants in England and Wales (ICAEW) and the Association of Chartered Certified Accountants (ACCA). Both set minimum standards for PI cover for their members. For instance, The ICAEW requires a minimum limit of PI:

‘Two and a half times the gross fee income of the firm for its last financial year, subject to: a minimum of £100,000; and maximum of £1.5 million.’[3]

The ACCA also has similar minimums reflective of various bands of fee income. ABC aims to offer accountants the minimum limits required by their regulatory bodies and ensure that the PI product offered is compliant with all minimum requirements in terms of the cover offered.

Although this product is generally profitable, there is an area of concern which appears to be negatively affecting the account. Policies offered to accountants who are currently, or who have historically, given tax mitigation advice to their clients are suffering from an influx of notifications and paid claims. When an accountant has offered this service, they have advised or introduced their clients to invest money into schemes which have the main objective of avoiding payment of tax to the Government.

[2] https://www.know-insurance.co.uk/business/what-professional-indemnity-insurance

[3] https://www.hammondpi.com/pi-for-your-profession/professional-indemnity-insurance-for-accountants

In 2014 the Government introduced accelerated payment notices (APNs), which required the recipient to pay the relevant tax back to the government within 90 days. The HMRC began to heavily investigate the use of tax mitigation schemes and where these were deemed to be set up or entered for the purpose of avoiding tax, an APN would be issued.

> *'The taxman's crackdown on avoidance schemes led to the HMRC Counter Avoidance Directorate collecting £886m from people who had tried to avoid tax by signing up to schemes'*[4]

As a result of this sudden crack down on tax schemes, those who had invested and were facing paying the notices turned to their accountants for compensation stating that they were negligently advised to enter such schemes. As a result, several notifications have fallen under the PI policies. The accountants themselves will often also face direct fines from the Government themselves, although this would not be covered under the PI policy.[5]

In 2011 there were only three notifications to ABC falling under this category. The above actions of the HMRC, led to a sharp increase in notifications falling under this category.
For the year 2014 when the HMRC really focused their attention on this area, there was a total of 47 claims made during this accident year. The total incurred costs of such claims currently sits at just over £13.5 million (the total between 2005-2017) and just over £6 million has been paid out.[6] This demonstrates that there is a problem of several notifications as a result of this type of claim being under the lime light which has led to vast amount of legal costs being paid out, so even where there may not be a resultant claim paid against the Insured, the cost of defending such actions is affecting the industry immensely.

This is a generic problem across the PI market, but each Insurer has been affected differently and responded in different ways. ABC remains in the market offering of PI for accountants so inevitably has some of these risks within the account, which has led to large claims and several notifications. However, with careful amendments to underwriting strategy, ABC is aiming to reduce exposure within this area and manage the remaining risk.

Underwriting acceptance criteria for this Product

To ensure that ABC are not too heavily exposed from claims arising from tax mitigation, certain underwriting criteria have been set for the PI product offered to accountants undertaking such work.

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[4] *HMRC takes £400m extra income tax after crackdown on avoidance,* The Telegraph, Olivia Rudgard, 21 December 2016

[5] *Government to target accountants and advisers who help clients avoid paying tax in latest crackdown,* The Independent, Andy McSmith 16th April 2016

[6] Actuarial/claims figures as at April 2017.

New proposal forms have been introduced with additional questionnaires for those accountants performing such work. From the additional questionnaire underwriters can establish the extent to which the risk is exposed to tax mitigation claims.

Set criteria has been established and written into guidelines as to which risks should be declined on this basis.

For instance, where the accountant was promoting schemes themselves or designing such schemes and directly entering their clients, this would be an automatic declinature.
If, however, they were only introducing the client to other promoters of the scheme, this provides another step in the chain putting them further away from claims and therefore may be considered.

Where the accountant has only undertaken introduction, further questions will be asked as to the number of schemes that they introduced, the number of clients, the monetary value the clients invested and what schemes were they involved with.

ABC has set criteria according to the number of schemes that are acceptable and the maximum number of clients and values placed into schemes because if several clients are placed into the scheme this could potentially amount in block notifications. If the overall amount is too high or a single amount invested from any one client too high, then this would fall outside ABC ‘s appetite.

As underwriters, we would also be looking at the contracts in place between the accountant their client and the promoter. Questions should be considered such as whether there is third party advice (i.e. that of the promoter is specifically excluded within the contracts between the accountant and their clients), is there a separate contract in place between the promoter and the client and does the accountant specifically limit their liability? All of these measures would make an accountant undertaking such work more attractive. Specific guidelines have also been issued by the ICAEW[7] to help accountants draw up terms of engagement for contracts between themselves, promoters and clients. Where accountants have followed such advice, this will also be looked upon favourably by ABC.

These steps would form part of the Insured’s risk management. The additional questionnaire will ask further risk management questions which the underwriters of ABC will then analyse and assign points to for each positive step taken, according to the underwriting guidelines set. Where the points allocated fall below a threshold, the risk should then be declined.
Only those over the threshold become writable and the rate will be dependent on where they fit within the scale.

[7] https://www.icaew.com/en/technical/practice-resources/practice-helpsheets/engagement-letters

Another step taken within the underwriting criteria is to ensure that certain endorsements are added where the product is offered to accountants with tax mitigation exposure. A specific excess endorsement is added so that any work in respect of tax mitigation is subjected to a higher excess and this is also in respect of each and every claimant (as opposed to claim which is usual within PI).

Previous claims would also be considered by underwriters and whether any have amounted from this type of work historically. Where there have been several notifications or claims of this type paid, the risk will be less attractive.

Where a risk falls just outside the guidelines, for instance the amount invested into schemes or the number of schemes introduced falls just above the threshold, an underwriter can choose to refer the risk for discussion among a peer group, including a portfolio manager. This may be particularly important on renewal cases which were previously acceptable under historic guidelines but as a result of amendments made in response to the HMRC actions could potentially be a declinature.

How the underwriting acceptance criteria influences the profitability of this insurance product

The main aim of the revised underwriting acceptance criteria is to ensure that those risks which have historically exposed ABC to tax mitigation claims are no longer within the account, and that an acceptable level of exposure is present.

ABC would be unable to withdraw from this sector completely as they are seen as a lead insurer for accountants and have to maintain this reputation. Instead it has been important to use the expertise required to apply suitable restrictions within the underwriting guidelines which allow us to still accept risks where we are unlikely to have such severe claims and as a result protect the profitability of the account. With carefully selected underwriting, rather than complete withdrawal, we are able to maintain several clients and satisfy brokers needs in placing some difficult risks. In turn brokers should reward us by also keeping the standard, vanilla risks with us also, helping us to maintain profitability across the account.

In requesting an additional proposal form, ABC aims to understand the risk and its exposure:

> *'The insurer will need to understand the extent of the advice that has been provided by the accountant – particularly at the introduction stage. Did the accountant sit in on the meetings between the client and the scheme promoter/provider?'*[8]

[8] https://www.bluefinprofessions.co.uk/accountants-adding-up-the-risk/peeling-film-tax-avoidance-claims/
Peeling the Film of tax avoidance claims- Virginia Hickley, Mills and Reeve, Martin Thomas, Epic

The underwriting criteria set requires clients who have offered tax scheme advice to complete the questionnaire and answer further questions such as the above, so that we can establish the extent to which the insured were involved in offering tax mitigation advice.

This helps protect the profitability of the account because if the underwriter establishes that the accountant was heavily involved by directly promoting the scheme or attending meetings with the clients to the promoters, or that they have not protected themselves with the relevant terms of engagement, they should be more cautious in considering the risk. Where it appears that the accountant is too heavily involved, in order to protect the profitability of the account, such risk should be declined. If they are written there is a high chance that a claim will be directed at them and is likely to be successful.

In asking further questions about the values and number of the clients, and setting restrictions on what is acceptable, ABC can also control the level of claims that could arise. For instance, the criteria sets limits on the maximum amounts invested per client and overall. This ensures that should a claim be made under the policy it can only reach a certain level and not go beyond this.

The premiums are carefully conducted to take into account the levels of exposure so where there are higher amounts invested and a larger number of schemes or clients, the premium will be significantly increased. In doing so ABC can protect the profitability of the account by gaining more premium, the loss ratios will be improved, particularly if we are able to keep hold of the business for several years and only encounter few claims within those years. With the restrictions in place as above, which aim to reduce the amount of claims exposure, this will also positively affect the loss ratios.

Another measure that was taken in the underwriting criteria was the increased excess in respect of this work and to make the excess each and every claimant. This was a crucial move in protecting the account due to the nature of such claims making them susceptible to block notifications. For example, if a scheme comes under scrutiny from the HMRC, all the clients that the insured introduced to the scheme would be able to take action against the Insured. If the excess was each and every claim, a block notification would be made to meaning that only one excess is applicable for multiple clients as they all fall under the same claim. Making the excess each and every client ensures that every client that is part of the action would have to pay a separate excess, thus protecting ABC as the exposure will only be above that excess for each client. In making the excess higher any claims falling below this will be met by the insured so ABC are therefore protected up to a set level.

This is one of the reasons why the underwriting criteria caps the value that any one client can invest. In setting the limit on this and increasing the excess to above this amount, if a client tries to claim back the amount they have invested in the schemes as a loss due to negligent advice, this should fall within the excess that the Insured is required to pay out.

Any penalties enforced on the clients by the HMRC will also be proportionate to the amount invested ABC are also protecting the level of exposure from penalties that clients could claim back from the Insured.

All these methods to lower the level of exposure will also decrease the amount of claims payable or the value of the claims. In doing so this will protect the profitability of the account.

The key to protecting the profitability of the account is in understanding the risk that is being placed before the underwriters and where claims are likely to arise from and limiting the exposure to such claims. In asking the further questions in the additional questionnaire ABC can fully understand the risk and decline anywhere they see the exposure to be too great and the risk not worth taking. Those which are accepted can be done so with caution, with the relevant terms such as an increased each and every claimant excess applied and a higher premium applied.

Recommendations to improve the profitability of the product

As stated above, the key to protecting any account is to understand the risks that are within it. My first recommendation would be to work together with the HMRC, the ICAEW and the ACCA to understand where the claims are likely to come from and recognise the potential for claims to arise before they get out of hand and affect the account adversely.

Seminars and regular bulletins provided by these groups should be regularly monitored.
I would suggest that ABC appoint a senior underwriter for each profession that it writes so that they have a specialist in each area that can monitor developments. An underwriter with the responsibility of accountants can keep abreast of the developments occurring and feed back to the team to establish the best way to manage new exposures etc.

It is also essential that underwriters look beyond the underwriting guidelines:

> *'While underwriting management must endeavour to provide as many relevant guidelines as possible to cover issues that may arise in new business presentations, proposals or at renewal, underwriters must take care to assess all information available to them'*[9]

In researching the company, undertaking a financial check of the company and looking at their own website, the underwriter can establish the financial security of the company and their ability to pay the premium and higher excess if applicable. The website may give further details as to the historic business undertaken and any tax scheme work that may not have been declared on the proposal form.

[9] Advanced Underwriting 960, Nov 2015, Dr Laura Cochran

Client visits should be compulsory and built into the acceptance criteria for risks above a certain level for instance, if the fee income from the accountant is above £2.5 million.
This will help an underwriter to establish how the accountant manages their business and any risks associated with it. Any concerns arising from the additional tax questionnaire can be addressed directly by the insured.

ABC should consider the way in which a risk programme is structed and build this into its guidelines. For instance, where there is above a certain level of exposure to tax mitigation claims, ABC could consider co-insuring to spread the risk (a co-insurer provides partial coverage along with other co-insurers)[10], or write on an excess layer as opposed to the primary (attach to the risk above a certain level of exposure, for instance after a £5 million primary). In doing so they should be able to write risks with a higher level of exposure, but still limit the exposure to the company itself. The cut off points for number of schemes and amounts invested could then be raised, but only where considered on a co-insurance or excess basis.

Unfortunately, there is very little that can be done to the terms and conditions of the policy due to the fact that we need it to remain compliant with the accountant regulators minimum requirements in order for it to be a recommended, participating Insurer for accountants.
It would also make us far less competitive if we were to add further onerous terms. However, if the regulators would ever allow for it as a means to make it easier for their members to get insurance, it would be ideal to make the excess in respect of each and every claimant inclusive of defence costs. This would mean that the costs of defending against the claims could also be attributed to the excess paid by the Insured. As discussed above, there was an influx of claims notifications and although many did not result in claims paid, the biggest losses on the account have come from defending the actions. As the requirements of the ICAEW and ACCA currently stand, the excess needs to be exclusive of defence costs so these cannot fall within any payments made by the Insured themselves. However, the regulators have bent the rules for FCA regulated activities that accountants are undertaking, and allow for an inclusive excess here.[11] Perhaps the Insurance industry should be doing more to campaign for this to also be applicable to tax scheme activities. We should be working together with the Institutes to find solutions to make more accountants writable risks rather than them entering into the assigned risk pool where they are unable to get cover.

[10] http://www.investopedia.com/terms/c/coinsurer.asp

[11] Institute of Chartered Accountants in England and Wales, Institute of Chartered Accountants of Scotland Institute of Chartered Accountants in Ireland, Minimum Approved Wording, May 2017 sec C3.2

Reference List:

Course books

- Advanced Underwriting 960, Nov 2015, Dr Laura Cochran
- Underwriting Practice M80/P80, 2016, Phillip Priddle, ACII and Mark Wallace BA, FIA

Websites

- https://www.lloyds.com/common/help/glossary?page=4
- https://www.know-insurance.co.uk/business/what-professional-indemnity-insurance
- https://www.hammondpi.com/pi-for-your-profession/professional-indemnity-insurance-for-accountants
- https://www.icaew.com/en/technical/practice-resources/practice-helpsheets/engagement-letters
- https://www.bluefinprofessions.co.uk/accountants-adding-up-the-risk/peeling-film-tax-avoidance-claims/
- http://www.investopedia.com/terms/c/coinsurer.asp

Articles

- *HMRC takes £400m extra income tax after crackdown on avoidance,* The Telegraph, Olivia Rudgard, 21 December 2016
- *Government to target accountants and advisers who help clients avoid paying tax in latest crackdown,* The Independent, Andy McSmith 16th April 2016
- Peeling the Film of tax avoidance claims- Virginia Hickley, Mills and Reeve, Martin Thomas, Epic

Documents

- Institute of Chartered Accountants in England and Wales, Institute of Chartered Accountants of Scotland, Institute of Chartered Accountants in Ireland, Minimum Approved Wording, May 2017 sec C3.2
- Internal Actuarial/claims figures report as at April 2017.

Glossary of key words

Analyse

Find the relevant facts and examine these in depth. Examine the relationship between various facts and make conclusions or recommendations.

Construct

To build or make something; construct a table.

Describe

Give an account in words (someone or something) including all relevant characteristics, qualities or events.

Devise

To plan or create a method, procedure or system.

Discuss

To consider something in detail; examining the different ideas and opinions about something, for example to weigh up alternative views.

Explain

To make something clear and easy to understand with reasoning and/or justification.

Identify

Recognise and name.

Justify

Support an argument or conclusion. Prove or show grounds for a decision.

Outline

Give a general description briefly showing the essential features.

Recommend with reasons

Provide reasons in favour.

State

Express main points in brief, clear form.