

The Servicing of Global Insurance Programmes: can insurers overcome the challenge?

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Fellowship Dissertation

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Introduction

Global insurance programmes (hereafter “global programmes”) are a complex product. By design they are intended to both sit within, and sit above, multiple jurisdictions. Much has been written about global programmes for the purpose of marketing their advantages to buyers; be it the costs saved, the compliance and regulatory standards met or the improved claims service delivered. (AGCS, 2020)¹ (AIG, 2012)²

The literature surrounding global programmes as a product is understandably focused on the interactions between a ‘tripartite relationship’ of the insurance buyer (usually the head office of a multinational corporation), their insurance broker, and the insurance company. (Strategic Risk, 2011)³ However the success of global programmes requires a vast network of branches, subsidiaries and partners across multiple countries to implement any agreement made.

In researching this topic it is clear that very little analysis has been undertaken which specifically focuses on the challenges which arise for those parties who form the aforementioned network, whose responsibility it is to implement insurance coverage which has been agreed on their behalf with little to no input themselves. This paper will provide an analysis of this underexplored area and suggest solutions to the challenges which arise for specifically one of those parties – the insurance company. This is an area in which I have worked and have therefore encountered such challenges myself.

While specific detailed literature on this subject is limited, much has been written about global programmes generally and so this literature will be considered insofar as it furthers this paper’s analysis.

¹ Allianz Global Corporate & Specialty, ‘Allianz Multinational’, <https://www.agcs.allianz.com/services/allianz-multinational.html> [accessed 16 April 2020]

² AIG, ‘How to Build a Multinational Program’, <https://www.aig.com/content/dam/aig/america-canada/us/documents/brochure/aig-how-to-build-mn-prog-12-21-12-brochure.pdf> [accessed 16 April 2020] pages 4 and 5

³ Strategic Risk, ‘Global Programmes’, <https://www.strategic-risk-europe.com/download?ac=19856> [accessed 16 April 2020] page 8

The first part of this paper will define the relevant concepts and relationships. The second part will explore why these concepts and relationships give rise to challenges for the insurer. The third part will offer solutions as to how these challenges can be overcome.

Part 1: Global Programmes and the Servicing of Global Programmes

Global programmes seek to combine the benefits of possessing locally admitted insurance with the consistency of coverage which a global insurance policy provides. By grouping a multinational company's global exposure under one programme, the economies of scale and buying power of the multinational may allow the leveraging of lower premiums when compared to each subsidiary purchasing their own insurance locally. The advantages of global programmes have been further summarised by Chubb as such:

'A global insurance programme provides for compliance with complex regulatory and tax regimes, the ability to pay claims locally and efficiently; control over risk management practices; cost efficiency; consistency of coverage and claims service and enhanced customer outcomes.' (Chubb)⁴

However when surveyed, buyers hold the compliance advantages and consistency of coverage afforded by global programmes as the two most desired outcomes of the product. (Airmic)⁵ It is these two outcomes which shall be of particular importance in this paper because it is the parties who are not directly involved in negotiating a global programme who nonetheless serve a fundamental role in delivering these outcomes. Global programmes and the parties involved in their agreement and implementation will now be defined and explored.

Global programmes are delivered through the issuance of two types of policy. First the insurance company issues a master policy to the buyer or their broker. This master policy provides coverage on a worldwide basis for both the buyer's parent company and any overseas subsidiary companies. However to navigate around the issue of non-admitted insurance, the insurance company will instruct an overseas office present in the same

⁴ Chubb, 'Global Insurance Programmes', <https://www.chubb.com/za-en/assets/documents/global-programmes--what-every-corporate-risk-manager-insurance-buyer-needs-to-know.pdf> [accessed 16 April 2020]

⁵ Airmic, 'ACE Risk Management Survey: 90% say risk complexity increasing', <https://www.airmic.com/news-story/ace-risk-manager-survey-90-say-risk-complexity-increasing> [accessed 16 April 2020]

jurisdiction as the buyer's subsidiary to issue an admitted insurance policy to that subsidiary. These are called local policies. The master policy will then provide difference in conditions/difference in limits cover over any coverage afforded under the local policy. (Strnad, 2009)⁶

To distinguish between the parties who are in control of the programme and those who implement what has been agreed, the terms “producing” and “servicing” will be applied throughout this paper. However other such terms are frequently used, for example servicing business is often referred to as ‘reverse flow’ business. (London Market Group, 2018)⁷ It is the producing underwriter within the insurance company who instructs the servicing underwriter in one of its overseas offices to issue a local policy to the local subsidiary or their appointed servicing broker. It is possible for servicing parties to not be part of the same corporate structure as the producing parties (such as for third party fronting arrangements) but throughout this paper the assumption will be applied that both parties are part of the same corporate structure. Insurance companies which compete in offering global programmes as a product have established vast in-house overseas networks precisely to provide control over that product and to increase competitive advantage over those who do not. This has led to a small pool of insurers and brokers who can deliver global programmes. (FCA, 2019)⁸ Indeed as Dwyer observes: ‘The pool of carriers and brokers that can execute a multinational program well is relatively small... even the best methodologies and technologies can’t deliver without the foundation of ample talent, resources and financial strength.’ (Dwyer, 2019)⁹

The table below (Table 1) illustrates the relationships and chains of communication throughout a global programme. This shows a French multinational buyer, along with a broker and insurer who have operations in France (collectively the “producing parties”),

⁶ Martin Strnad, International In-house Counsel Journal, ‘International Insurance Programs – Legal Frictions and Solutions’, <https://www.iicjlaw.com/subscribersonly/09august/iicj5-internationalinsurance-martinstrnad-zurich-switzerland.pdf> [accessed 16 April 2020] page 1,265

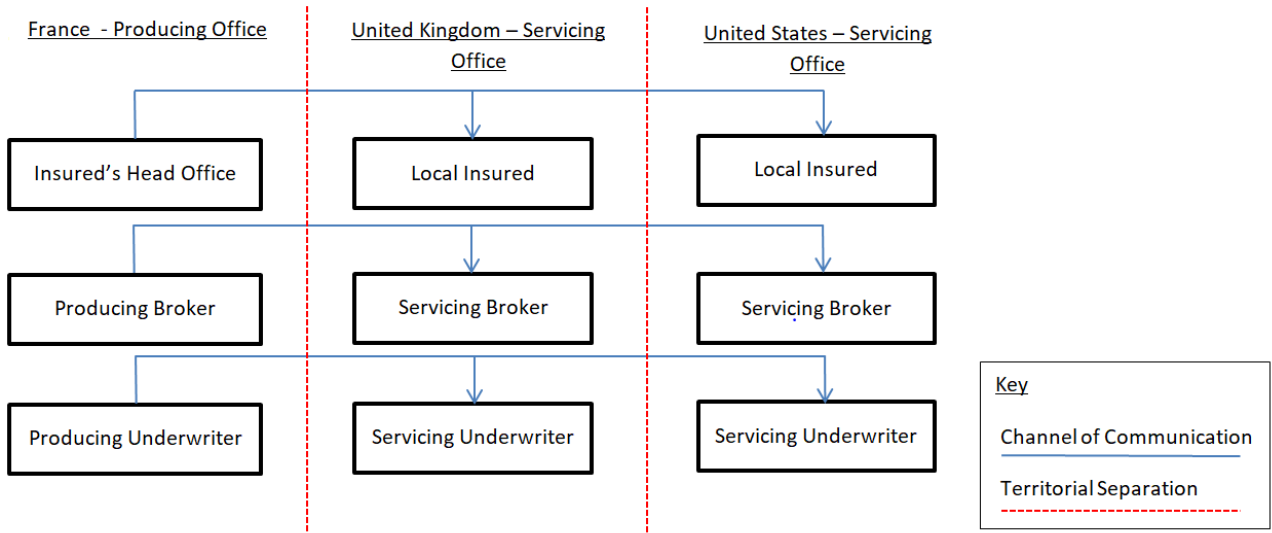
⁷ London Market Group, ‘Global Programme and Reverse Flow Business relating to Brokers and Company (Re)Insurers in the London Market’, <https://img.london/wp-content/uploads/2019/07/Global-Programme-and-Reverse-Flow-Business-Guidance-September-2018.pdf> [accessed 20 April 2020] page 1

⁸ Financial Conduct Authority, ‘Wholesale Insurance Broker Market Study’, <https://www.fca.org.uk/publication/market-studies/ms17-2-2.pdf> [accessed 05 June 2020] page 44

⁹ Katie Dwyer, Risk & Insurance, ‘4 Maddening Global Insurance Challenges and the Expert Solutions to Solve Them’, <https://riskandinsurance.com/expert-solutions-for-5-of-the-most-maddening-global-insurance-challenges/> [accessed 02 June 2020]

communicating with their overseas offices in the UK and the USA (collectively the “servicing parties”) to arrange the issuance of local policies. All parties will be fully licenced in their respective territories.

Table 1: The lines of communication within a global programme



It is common for the risk assumed by the local underwriters to be fully reinsured back to the producing underwriters, but this is not always the case. (PwC, 2019)¹⁰ While this is a simplistic example, global programmes have the potential to become both highly bespoke and immensely complex products, especially for the largest of multinational buyers. However due to the growing complexity and fragmentation of the regulatory landscape, even mid-market companies with smaller international exposures may require complex global programmes. (Collins, 2019)¹¹ Therefore the issues raised in this paper will only become more important as more companies seek insurance solutions for their increasingly internationalised risk profiles.

Fundamental to the proper implementation of a global programme is the effective replication of a valid contract of insurance within each territory in which the buyer operates. In doing so the objective of providing admitted insurance which stands up to the scrutiny of local regulators is fulfilled. Such a process however is built upon the fiction that each locally

¹⁰ PwC, ‘Proposed BEAT regulations address certain insurance issues’, <https://www.pwc.com/us/en/tax-services/publications/insights/assets/pwc-proposed-beat-regulations-address-certain-insurance-issues.pdf> [accessed 20 April 2020] page 1

¹¹ Stuart Collins, Commercial Risk, ‘Global Programmes Special Report 2019’, <http://edition.pagesuite-professional.co.uk/html5/reader/production/default.aspx?pubname=&edid=1973f287-c905-48c8-9bf7-2116d7c509c9>, [accessed 20 April 2020] page 15

admitted insurance policy has been individually negotiated between the servicing parties. As shall be discussed within this paper, the maintenance of this fiction is often the source of tension between the producing and servicing parties.

The intricacies of how to properly construct a global programme from the perspective of the producing parties has already been thoroughly explored (see Strnad¹², Roberto¹³ and Krishnan¹⁴) and so this paper will avoid re-exploring this topic. It will instead focus on the challenges faced by insurance companies in servicing a global programme which, as previously mentioned, has been underexplored. This will require particular focus on the role and challenges faced by the servicing underwriter.

Part 2: The Challenge of Servicing a Global Programme

A fundamental gap exists between the theory and practice of how a global programme is implemented. In theory, the producing underwriter negotiates the global coverage and the servicing underwriter merely replicates that coverage. However in practice what amounts to a process of clarification occurs internally between the producing and servicing underwriters of the insurance company. This involves the servicing underwriter clarifying what insurance coverage has been agreed on their behalf by the producing underwriter, and considering how best to implement it. This could also include clarifying the terms and conditions to apply or the policy form to use (be it standard or manuscript).

In light of these practicalities a question should be posed – why is this required at all? Surely what the producing underwriter agrees must be implemented without question, otherwise the primary purpose of organising the buyer’s insurance into a centralised global programme is lost? Such an opinion is understandable because that is how global programmes are marketed. (AGCS, 2020)¹⁵ However the insurance market globally is highly

¹² Martin Strnad, International In-house Counsel Journal, ‘International Insurance Programs – Legal Frictions and Solutions’, <https://www.iicjlaw.com/subscribersonly/09august/iicj5-internationalinsurance-martinstrnad-zurich-switzerland.pdf> [accessed 16 April 2020]

¹³ Joanna Roberto, Insurance Law, ‘The Rise of Global Insurance Policies’, <https://media.goldbergsegalla.com/uploads/jmr-forthedefense-may2016.pdf> [accessed 16 April 2020] page 21

¹⁴ Suresh Krishnan and James Potts, ‘Structuring Multinational Insurance Programmes: Challenges and Solutions for International Companies with US Exposures’, <https://d18b3k73pw7q78.cloudfront.net/app/uploads/2013/09/AM-Chubb-Insurance-Programmes-US-2013.pdf> [accessed 16 April 2020]

¹⁵ Allianz Global Corporate & Specialty, ‘Allianz Multinational’, <https://www.agcs.allianz.com/services/allianz-multinational.html> [accessed 16 April 2020]

fragmented, not just between nations but within the devolved institutions of those nations. (Canamero, 2014)¹⁶ (NIAC, 2011)¹⁷ The result is that, when the producing parties negotiate a global insurance programme which is informed by the laws, practices, customs and language of their own market, that agreement can become undone when it comes into contact with those same features of another market. (Skinner, 2008)¹⁸ (Fomchenko, 2006)¹⁹

The servicing underwriter must take the producing underwriter's instructions, which contain the skeleton coverage and pricing negotiated, and transform them into a fully compliant local policy. The role of a servicing underwriter must therefore be less focused on the strict implementation of any instructions received and instead focus on interpreting and adapting those instructions to fit the local market. This process does give rise to a fundamental challenge. If it is accepted that a servicing underwriter must interpret and adapt any instructions received from the producing underwriter, then it follows that the servicing underwriter's role is different from that propagated by insurers themselves (being that servicing underwriters merely implement the instructions received). By necessity, servicing underwriters need to amend the coverage agreed.

This necessity is borne out of the aforementioned fragmented nature of the regulatory landscape. Because the servicing underwriter is operating within a different jurisdiction, they must consider the interests of the local insurance company who employs them in addition to owing the local insured the duty of care mandated by local laws and by the local regulator. As was highlighted earlier, a key outcome of a global programme is its ability to maintain the fiction that each local transaction was negotiated between the servicing parties of that jurisdiction, and hence stand up to the scrutiny of local regulators. To act otherwise would be to remove the admitted insurance element of the programme and

¹⁶ Maria Canamero, Moody's Analytics, 'Regulatory Radar for Insurance: Emerging Regulations are Reshaping the Global Insurance Industry', <https://www.moodysanalytics.com/risk-perspectives-magazine/managing-insurance-risk/insurance-regulatory-spotlight/emerging-regulations-are-reshaping-the-global-insurance-industry> [accessed 12 June 2020]

¹⁷ National Association of Insurance Commissioners, 'State Insurance Regulation', https://www.naic.org/documents/topics_white_paper_hist_ins_reg.pdf [accessed 12 June 2020] page 1

¹⁸ Nathan Skinner, Strategic Risk, 'Are you breaking the law?', <https://www.strategic-risk-europe.com/are-you-breaking-the-law/1375136.article> [accessed 05 June 2020]

¹⁹ Steven Fomchenko and Peter Smithdale, 'International Property Coverage: thinking globally acting locally', <https://www.thefreelibrary.com/International+property+coverage%3A+thinking+globally+acting+locally.-a0141048569> [accessed 01 May 2020]

would jeopardise the key feature which differentiates a global programme from non-admitted solutions.

Therefore, it has been revealed that the practicalities of servicing a global programme give rise to a significant departure from the theory behind it. Servicing underwriters, due to the necessities of the markets and jurisdictions in which they operate, cannot simply implement the coverage agreed on their behalf by the producing underwriters. They must take into account the interests and requirements of the local insurer as well as those of the local insured, especially when the consideration of such interests is required by local laws and regulations. This is the fundamental challenge of servicing a global programme. As a result of this challenge, servicing underwriters often find themselves in a position of balancing the competing interests of multiple parties. Because this reality is not acknowledged by insurers, servicing underwriters have to overcome challenges on an *ad hoc* basis.

This paper will now propose solutions to resolve this fundamental challenge. To do this, and to better understand the competing interests which a servicing underwriter must balance, this paper will proceed with defining a new concept: that of a servicing underwriter's "mandate".

Part 3: Overcoming the Challenge

A servicing underwriter does not possess an underwriting authority in the traditional sense because they cannot make unilateral underwriting decisions. To allow such decisions would go against the purpose of a global programme. Despite this, the exposures which servicing underwriters bind the local insurer to can far exceed the underwriting authority of any individual within the local insurance company. This is because the local policy may also act as fronting documentation on behalf of an entire panel of co-insurers in the producing territory, thus the coverage afforded under it can accommodate vast exposures. This arrangement is also utilised where the local policy is fronting on behalf of a captive. (Wohrmann, 2018)²⁰ While the potentially large exposures are reinsured, the local policies are nonetheless valid and enforceable contracts as perceived by the local authorities.

²⁰ Paul Wohrmann, Global Programmes 2018, Captive Review, 'The Changing Insurance Market' via AIG UK, <https://www.aig.co.uk/content/dam/aig/emea/united-kingdom/documents/insights/ct-global-programmes.pdf> [accessed 05 June 2020] page 15

Therefore any mistake, miscommunication or misapprehension between the producing and servicing parties as to what the local policy should or should not cover may still be enforceable against the local insurer if implemented into the policy document. This is because insurance policies, like all contracts, are interpreted on an objective basis. (Clarke, 2014)²¹ This issue is especially acute considering how subjective the interpretation of insurance terminology can be, let alone insurance terminology utilised between different jurisdictions. (Fomchenko, 2006)²²

From these observations, it must follow therefore that the “mandate” a servicing underwriter has to bind the local insurer to potentially vast liabilities must be derived from a clear source with clear guidelines. This is not the case. There are multiple sources of authority from which a servicing underwriter derives their mandate to bind the local insurer; some express, some implied, and some out of necessity. This paper will now proceed by analysing these sources of authority and how useful they may be in terms of validating the servicing underwriter’s actions. To distinguish the authority of a servicing underwriter to bind the local insurer from that conferred upon a traditional underwriter, the term “mandate” will be applied henceforth in order to avoid any suggestion of equivalence between the two.

This paper proposes three sources from which a servicing underwriter’s mandate could be derived. These proposed sources are A) from the producing underwriter, B) from the local insurer and C) between the servicing parties.

Proposition A: The mandate is derived from the producing underwriter

The primary responsibility of a servicing underwriter is to issue a local policy in accordance with the instructions which they receive from the producing underwriter. Often these instructions are near replications of the master coverage. (Roberto, 2016)²³ It would seem appropriate therefore that a servicing underwriter should implement these instructions

²¹ Malcolm A Clarke, Routledge, ‘The Law of Liability Insurance’, section 6.2

²² Steven Fomchenko and Peter Smithdale, ‘International Property Coverage: thinking globally acting locally’, <https://www.thefreelibrary.com/International+property+coverage%3A+thinking+globally+acting+locally.-a0141048569> [accessed 01 May 2020]

²³ Joanna Roberto, Insurance Law, ‘The Rise of Global Insurance Policies’, <https://media.goldbergsegalla.com/uploads/jmr-forthedefense-may2016.pdf> [accessed 16 April 2020] page 23

because they represent the agreement made between the producing parties. Indeed, if one of the primary advantages of a global programme is the avoidance of the need for individually negotiated local policies, then it follows that servicing underwriters should not seek to amend or otherwise re-underwrite the terms negotiated and subsequently memorialised within the instructions received. Furthermore the existence of reinsurance behind the local policy suggests that the servicing underwriter need not be concerned with the consequences of implementing those instructions. Therefore the mandate of a servicing underwriter to bind the local insurer is conferred by the producing underwriter, with each individual instruction to be considered an individual mandate.

However this argument has some fundamental problems. To equate the mandate of a servicing underwriter within a global programme as tantamount to a “rubber stamp” is to misinterpret their role in addition to misunderstanding what the local policy’s function is in delivering the outcomes which a global programme seeks to deliver. A good local policy should not just implement the instructions of the producing underwriter, but should conform to the regulations and customs of its market. The alternative would be to issue local policies which may technically count as “admitted” policies but which would not stand up to scrutiny should their content be challenged. Therefore such local policies would act contrary to their intended function within the programme by increasing legal risk, since ambiguous contracts when subjected to the interpretation of the courts can result in unintended outcomes. (Clarke, 2014)²⁴ Furthermore local policies that seek to participate in local pools may also be challenged by the authorities that govern those pools should the rules of participation be contravened. Two examples can be offered to illustrate this fallacy:

1. A UK servicing underwriter, upon receipt of instructions from a French producing underwriter, issues a property damage policy implementing instructions requesting tenants and neighbours liability cover. This is duly documented in the policy schedule, even though such coverage on a property damage policy is only standard in Napoleonic Code jurisdictions. (Greenwald, 2019)²⁵ No accompanying clause is contained in the policy wording fully defining the scope of coverage. Hence

²⁴ Malcolm A Clarke, Routledge, ‘The Law of Liability Insurance’, section 6.7

²⁵ Judy Greenwald, Business Insurance, ‘Napoleonic code does not apply to Chubb coverage dispute: Court’, <https://www.businessinsurance.com/article/20190722/NEWS06/912329725/Napoleonic-code-does-not-apply-to-Chubb-coverage-dispute-Court> [accessed 19 June 2020]

ambiguity is created because the cover is neither market standard nor adequately defined.

2. A UK servicing underwriter, whose local insurer is a member of Pool Reinsurance Company Limited (Pool Re)²⁶ only covers the local insured's central London buildings against terrorism under the scheme as requested in the instructions received. This is in breach of Pool Re's adverse selection rules and therefore places at risk the viability of the coverage. (Willis Ltd, 2014)²⁷

Therefore, despite what may appear to be the *prima facie* case that the mandate of a servicing underwriter is to simply follow the instructions of a producing underwriter, this does not stand up to scrutiny. However there must be some truth to this proposition. If the producing parties were not fundamentally in control of the global programme, and the global insurance operation mandated the rejection of instructions over the implementation of those instructions, the desired outcome of a global programme where the local policies reflected the cover agreed by the producing parties would be defeated. The product would therefore be unsustainable and competitive advantage lost.

In summary, while the mandate of the servicing underwriter must involve following the producing underwriter's instructions this mandate cannot be considered to be derived wholly from those instructions where to follow them would create uncertainty and legal risk.

Proposition B: The mandate is derived from the local insurer

The opposite of proposition A, this proposition places the mandate of the servicing underwriter to bind the local insurer as arising from within the local insurer itself. Since local policies are issued by the locally licenced insurer it would seem correct for the servicing underwriter, in issuing that local policy, to be mandated to place the interests of the local insurer above that of the producing underwriter. Those interests would include compliance with local laws, regulations and customs.

²⁶ Pool Reinsurance Company Limited, <https://www.poolre.co.uk/> [accessed 01 May 2020]

²⁷ Willis Ltd, 'Terrorism Insurance – The Pool Re Adverse Selection Rule Explained', http://www.willis.com/Documents/Publications/Industries/Property_Investors/20140728_Terrorism_Adverse_Selection_JULY_2014_FINAL.pdf [accessed 01 May 2020]

Because the local insurer has a stake in ensuring its good reputation in the local market, to issue poor quality or even non-compliant local policies would damage its reputation and even its regulatory status. Poorly drafted policies containing unfamiliar and non-standard coverage may also lead to protracted and contested claims, and would therefore negate the efficiency in local claims handling which the local policy was intended to facilitate. (Hassett, 2014)²⁸ For example, a producing underwriter may instruct a UK servicing underwriter to issue an employers' liability policy on their behalf, knowing that it is a legal requirement in the UK. However, the instructions may request that a limit of indemnity of £5,000,000 in the annual aggregate be applied. There are two aspects of this to consider. First, the Employers' Liability (Compulsory Insurance) Regulations 1998²⁹ prevents aggregated limits of indemnity being applied on employers' liability policies. Second, the application of a £5,000,000 limit of indemnity is contrary to market practice, though not contrary to law. (Willis Ltd, 2011)³⁰ The dichotomy between the two warrants further consideration.

The servicing underwriter should reject the aggregation of the limit of indemnity on the basis that it conflicts with local laws. If the mandate of the servicing underwriter is to ensure that their local insurer's regulatory status and reputation is not damaged, on the basis that without that status the local insurer will be unable to issue local policies, then it follows that considerations of legality must take precedence over the producing underwriter's instructions. The issuance of "illegal admitted" policies is a self-defeating concept and contrary to the local policy's function as part of a global programme. While it is easy for local policies to be an afterthought, they represent a cornerstone of the insured's risk management strategy and should be perceived as a fundamental aspect of the insurer's product. As one publication states: 'Implementing best practices and a consistent loss prevention philosophy must take place within the context of local conditions and respect the requirements of local jurisdictions.' (Advisen, 2014)³¹ This therefore supports the

²⁸ Clive Hassett, Commercial Risk, 'Why local is best', <https://www.commercialriskonline.com/why-local-is-best-clive-hassett-ace/> [accessed 05 June 2020]

²⁹ Section 3 Employers' Liability (Compulsory Insurance) Regulations 1998, <http://www.legislation.gov.uk/ukxi/1998/2573/made> [accessed 02 June 2020]

³⁰ Willis Ltd, 'UK Employers' Liability' – A Guide, https://www.willis.com/Documents/Publications/Services/International/2011/UK_Intl_Alert_0911_v3.pdf [accessed 02 June 2020] page 2

³¹ Advisen, 'Managing a Globally Compliant Insurance Program', <https://www.advisenltd.com/wp-content/uploads/managing-globally-compliant-insurance-program-white-paper-2014-11-10.pdf> [accessed 05 June 2020] page 6

proposition that the servicing underwriter's mandate is to apply local considerations first, over the requirements of the producing parties.

However the same cannot be said for customs. Acting contrary to standard market practice is not the same as illegality because those local policies would still be perceived as valid by local regulators and enforceable in court. Furthermore the practical realities of servicing global programmes demand that servicing underwriters pursue the path of least resistance. If every instruction were to become a drawn out negotiation between producing and servicing underwriters then the legitimate expectations of the buyer, that the programme would be seamlessly implemented upon the finalisation of terms by the producing parties, would not be delivered. Therefore the argument that the mandate of the servicing underwriter can be drawn from the customs of the market in which they operate would seem inappropriate in this context.

Therefore the mandate of the servicing underwriter is to enforce the standards of the market insofar as they amount to legal standards, not customary standards. This conclusion remains consistent with the desired outcomes of a global programme and the function of a local policy within that programme.

Proposition C: The mandate is derived from ensuring the transaction between the servicing parties follows reasonable underwriting principles

Global programmes are built upon the fiction that each local policy is individually negotiated between the servicing parties. This means that, when perceived out of the context of the wider global programme, the local transaction should follow reasonable underwriting principles on the basis that local regulators would view the transaction from just a local perspective. The maintenance of this fiction is important because multiple taxation and regulatory issues would result should this fiction be compromised. However the current practice by the producing parties of considering the needs of the servicing parties 'almost as an afterthought' (Hall, 2001)³² threatens this fiction because it produces local transactions which do not adhere to reasonable underwriting principles. Therefore should it be the

³² Robert Hall, 'Fronting: Business Considerations, Regulatory Concerns, Legislative Reactions and Related Case Law', <https://debrahalljd.files.wordpress.com/2018/02/fronting-business-considerations-regulatory-concerns-legislative-reactions-and-related-caselaw.pdf> [accessed 05 June 2020] page 2

mandate of the servicing underwriter to ensure that the transaction follows reasonable underwriting principles in order to avoid the legal and regulatory risks which may result from deviating from those principles?

First however, it should be clarified what reasonable underwriting principles constitute. It should be noted that the concept of following reasonable underwriting principles as a proxy for ensuring regulatory compliance has already been suggested by Sharma, albeit specifically in the context of premium allocation. (Sharma, 2009)³³ In this same context Skinner equated reasonable underwriting principles with the terms which the local market would demand. (Skinner, 2008)³⁴ However such an approach would ignore the economies of scale which global programmes can leverage, and also does not consider the business decisions underwriters make in choosing to write desirable risks cheaply to win them from competitors. Therefore a servicing underwriter should not seek to re-underwrite the local risk. Instead their mandate should merely be to ensure that the local transaction does not constitute a gross deviation from reasonable underwriting principles. Such a standard should therefore only seek to target wholly unreasonable and unjustifiable local transactions.

There are two ways in which a servicing underwriter should be mandated to ensure the local transaction follows reasonable underwriting principles in order to avoid legal and regulatory risk: ensuring a sufficiency of capacity and a sufficiency of premium. Each shall be explored in turn.

Regulators are becoming increasingly concerned at the industry standard practice of issuing local policies carrying low limits of indemnity. From the insurer's perspective, this avoids accumulation issues should a large claim event trigger multiple local policies. (Strnad, 2009)³⁵ However the issuance of a local policy does not automatically eliminate all compliance considerations. As Strnad states, 'For most jurisdictions, the existence of a local

³³ Praveen Sharma, Strategic Risk, 'Taxing Issues', <https://www.strategic-risk-europe.com/taxing-issues/1380337.article> [accessed 05 June 2020]

³⁴ Nathan Skinner, Strategic Risk, 'Are you breaking the law?', <https://www.strategic-risk-europe.com/are-you-breaking-the-law/1375136.article> [accessed 05 June 2020]

³⁵ Martin Strnad, International In-house Counsel Journal, 'International Insurance Programs – Legal Frictions and Solutions', <https://www.iicjlaw.com/subscribersonly/09august/iicj5-internationalinsurance-martinstrnad-zurich-switzerland.pdf> [accessed 16/04/2020] page 1,265

policy does not in any way alter the fact that the producing country insurer is transacting insurance business directly in the [servicing] country if DIL or DIC insures a risk located in the [servicing] country.’ (Strnad, 2009)³⁶ Therefore, if the local policy limits are easily exhausted then reverting to the master cover does not negate the issue of non-admitted insurance. This means that the regular considerations on the payment of claims from non-admitted policies, such as the repatriation of the claims payment to the local entity, taxation issues, regulatory issues and loss adjusting issues would still apply. (Willis Ltd, 2011)³⁷ (Barton, 2018)³⁸ (Roberto, 2016)³⁹ (Advisen, 2014)⁴⁰ Indeed having to navigate around such issues may not even be anticipated by the insured, since their legitimate expectation would be that the issuance of a local policy would specifically protect against such problems.

Therefore such an approach should be avoided, especially in the circumstances where the local insured’s operation is very large. For example a large manufacturing operation may be provided with a local public and products liability policy carrying a £1,000,000 limit of indemnity, which would be inappropriately low for the local insured’s needs. While it is possible that a servicing broker may raise similar issues with the producing broker, it cannot be guaranteed that the producing broker would have even appointed a servicing broker. Therefore it should be the mandate of the servicing underwriter to challenge such an approach in a constructive way to make the local transaction follow reasonable underwriting principles. A simple solution would be to increase the capacity of the local policy, though not necessarily to the equivalent limit as the master policy, in order to mitigate against the aforementioned accumulation issues.

³⁶ Martin Strnad, International In-house Counsel Journal, ‘International Insurance Programs – Legal Frictions and Solutions’, <https://www.iicjlaw.com/subscribersonly/09august/iicj5-internationalinsurance-martinstrnad-zurich-switzerland.pdf> [accessed 16/04/2020] page 1,267

³⁷ Willis Ltd, ‘Non-Admitted Coverage and Premium Taxes: No Standard Solution’, https://www.willis.com/Documents/Publications/Services/International/2011/Intl_Alert-Non_Admitted_0611_v6.pdf [accessed 08 June 2020] page 3

³⁸ Carol Barton, Global Programmes 2018, Captive Review, ‘Global Programmes: Raising the Bar’ via AIG UK, <https://www.aig.co.uk/content/dam/aig/emea/united-kingdom/documents/insights/ct-global-programmes.pdf> [accessed 05 June 2020] page 16

³⁹ Joanna Roberto, Insurance Law, ‘The Rise of Global Insurance Policies’, <https://media.goldbergsegalla.com/uploads/jmr-forthedefense-may2016.pdf> [accessed 16 April 2020] page 22

⁴⁰ Advisen, ‘Managing a Globally Compliant Insurance Program’, <https://www.advisenltd.com/wp-content/uploads/managing-globally-compliant-insurance-program-white-paper-2014-11-10.pdf> [accessed 05 June 2020] page 5

Legal and regulatory issues may also arise if local policies carry insufficient premiums. This is because any tax levied upon that premium would be comparatively lower than if reasonable underwriting principles were followed and an appropriate premium charged on the local policy. As one publication states, 'Regulators may be alerted if a corporation is buying what could be perceived as an unrealistically low amount of cover for its local operations and paying a matching amount of insurance premium tax.' (Strategic Risk, 2011)⁴¹ Yet because the premium of a global programme is often allocated between territories in proportion to each territory's share of the economic measure (sums insured, turnover etc.) as standard practice, the situation can arise where local policies which consistently carry large claims only demand a low local premium in return. This may cause local regulators to argue that tax is being avoided, and no defence could be posited that the transaction is reasonable. Considering that the servicing underwriter will have the details of those claims reported against the local policy (though they may not have sight of any DIC/DIL claims made against the master policy), it would be practical for them to raise such issues with the producing underwriter and seek a proportionately larger allocation of the global premium, especially before renewal discussions between the producing parties begin. This is where servicing underwriters must be proactive in ensuring compliance. Since they possess the local expertise it would be incorrect to attempt to delegate all issues of compliance to the producing underwriter who cannot be expected to have sight over all aspects of the global programme. (Norris, 2019)⁴² Given that any breaches of local compliance issues would be held against the local insurer, this argument is consistent with the conclusions of Proposition B.

It can therefore be proposed that the mandate of a servicing underwriter, in co-ordination with the producing underwriter, should be to ensure that the local transaction follows reasonable underwriting principles. This would mitigate the legal and regulatory risks of issuing local policies carrying insufficient capacity and premiums. To go against this notion

⁴¹ Strategic Risk, 'Global programmes', <https://www.strategic-risk-europe.com/download?ac=19856> [accessed 05 June 2020] page 9

⁴² Ben Norris, Commercial Risk, 'Global Programmes Special Report 2019', <http://edition.pagesuite-professional.co.uk/html5/reader/production/default.aspx?pubname=&edid=1973f287-c905-48c8-9bf7-2116d7c509c9>, [accessed 20 April 2020] page 22

would put at risk the fiction which global programmes seek to uphold and would therefore threaten the viability of the product as a whole.

Conclusion

This paper has established that servicing underwriters, by necessity, serve a purpose greater than merely “rubber stamping” the insurance coverage agreed by the producing parties. This necessity is borne out of the need to give effect to the very outcomes which global programmes are designed to deliver. Therefore the perceived truism that the servicing underwriter merely implements the entire coverage as agreed by the producing parties has been revealed as false. Accepting and managing this state of affairs is the fundamental challenge of servicing a global programme.

To overcome this challenge, this paper has sought to rationalise the priorities and responsibilities of a servicing underwriter through proposing the concept of an underwriting mandate. This seeks to clearly delineate which interests of the various parties should take precedence when those interests are placed in opposition. The parties in question are the producing underwriter, the local insurance company and the local insured. This paper has explored the roles and responsibilities of a servicing underwriter *vis-à-vis* these parties and in doing so can propose a clear hierarchy of priorities which should form the servicing underwriter’s mandate. By following this mandate, the challenge of servicing a global programme can be overcome. Procedures could be established throughout the insurance company’s network to give effect to this mandate.

This paper can conclude the proposed mandate as such: a servicing underwriter should follow the instructions of the producing underwriter but only insofar as they do not create legal and regulatory risk. What constitutes legal and regulatory risk should be construed narrowly to give the greatest scope for the agreement made by the producing parties to be implemented. For example, servicing underwriters should not seek to enforce the customary standards of the local market because customary standards are not tantamount to legal standards. However, they should ensure that the transaction follows reasonable underwriting principles because to not follow them has been demonstrated as constituting a legal and regulatory risk. To act otherwise would threaten the capability of the insurer to

issue a local policy in the territory, and hence place at risk the insurer's ability to provide global programmes as a solution to the needs of multinational buyers.

This paper has sought to limit the scope of its analysis to that of the challenges faced by the insurance company. Considering the complexity involved in servicing global programmes, further analysis should be undertaken focusing on the challenges faced by the servicing broker and local insured. In doing so, this previously underexplored yet complex area of insurance can be given the degree of analysis which is warranted.

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