P66 – Delegated authority

Diploma in Insurance

October 2017 Examination Guide

SPECIAL NOTICE

Candidates entered for the April 2018 examination should study this Examination Guide carefully in order to prepare themselves for the examination.

Practise in answering the questions is highly desirable and should be considered a critical part of a properly planned programme of examination preparation.

P66 – Delegated authority

Contents

Published February 2018

Telephone: 020 8989 8464
Fax: 020 8530 3052
Email: customer.serv@cii.co.uk

IMPORTANT GUIDANCE FOR CANDIDATES

Introduction

The purpose of this Examination Guide is to help you understand how examiners seek to assess the knowledge and skill of candidates. You can then use this understanding to help you demonstrate to the examiners that you meet the required levels of knowledge and skill to merit a pass in this unit.

Before the examination

Study the syllabus carefully

This is available online at www.cii.co.uk or from Customer Service. All the questions in the examination are based directly on the syllabus. *You will be tested on the syllabus alone*, so it is vital that you are familiar with it.

There are books specifically produced to support your studies that provide coverage of all the syllabus areas; however you should be prepared to read around the subject. This is important, particularly if you feel that further information is required to fully understand a topic or an alternative viewpoint is sought. The reading list which can be found with the syllabus provides valuable suggestions.

Read widely

It is vital that your knowledge is widened beyond the scope of one book. *It is quite unrealistic to expect that the study of a single study text will be sufficient to meet all your requirements.* While books specifically produced to support your studies will provide coverage of all the syllabus areas, you should be prepared to read around the subject. This is important, particularly if you feel that further information is required to fully understand a topic or an alternative viewpoint is sought. The reading list which can be found with the syllabus provides valuable suggestions.

Make full use of the Examination Guide

This Examination Guide contains a full examination paper and model answers. The model answers show the types of responses the examiners are looking for and which would achieve maximum marks. However, you should note that there are alternative answers to some question parts which would also gain high marks. For the sake of clarity and brevity not all of these alternative answers are shown.

This guide and previous Examination Guides can be treated as 'mock' examination papers. Attempting them under examination conditions as far as possible, and then comparing your answers to the model ones, should be seen as an essential part of your exam preparation. The examiner's comments on candidates' actual performance in each question provide further valuable guidance. You can purchase copies of the most recent Examination Guides online at www.cii.co.uk. CII members can download free copies of older Examination Guides online at www.cii.co.uk/knowledge.

Know the structure of the examination
Assessment is by means of a three hour paper.

Part 1 consists of 14 compulsory questions, worth a total of 140 marks.

Part 2 consists of 2 questions selected from 3, worth a total of 60 marks.

Each question part will clearly show the maximum marks which can be earned.

Read the current Diploma in Insurance Information for Candidates
Details of administrative arrangements and the regulations which form the basis of your examination entry are to be found in the current Diploma in Insurance Information for Candidates brochure, which is *essential reading* for all candidates. It is available online at www.cii.co.uk or from Customer Service.

In the examination

The following will help:

Spend your time in accordance with the allocation of marks

- The marks allocated to each question part are shown on the paper.
- If a question has just two marks allocated, there are likely to be only one or two points for which the examiner is looking, so a long answer is a waste of time.
- Conversely, if a question has 12 marks allocated, a couple of lines will not be an adequate answer.
- Do not spend excessive time on any one question; if the time allocation for that question has been used up, leave some space, go on to the next question and return to the incomplete question after you have completed the rest of the paper, if you have time.

Take great care to answer the question that has been set

- Many candidates leave the examination room confident that they have written a 'good' paper, only to be surprised when they receive a disappointing result. Often, the explanation for this lies in a failure to fully understand the question that has been asked before putting pen to paper.
- Highlighting key words and phrases is a technique many candidates find useful.
- The model answers provided in this Examination Guide would gain full marks. Alternative answers that cover the same points and therefore answer the question that has been asked would also gain full marks.

Tackling questions

Tackle the questions in whatever order feels most comfortable. Generally, it is better to leave any questions which you find challenging until you have attempted the questions you are confident about. Candidates' should avoid mixing question parts, (for example, 1(a)(i) and (ii) followed by 2(b)(ii) followed by 1(e)(i)) as this often leads to candidates unintentionally failing to fully complete the examination paper. This can make the difference between achieving a pass or a narrow fail.

It is vital to label all parts of your answer correctly as many questions have multiple parts to them (for example, question 1(a) may have parts (i), (ii) and (iii)). Failure to fully distinguish between the separate question parts may mean that full credit cannot be given. It is also important to note that a full answer must be given to each question part and candidates should not include notes such as 'refer to answer given in 1(b)(i)'.

Answer format

Unless the question requires you to produce an answer in a particular format, such as a letter or a report, you should use 'bullet points' or short paragraphs. The model answers indicate what is acceptable for the different types of question.

Where you are asked to perform a calculation it is important to show **all** the steps in your answer. The majority of the marks will be allocated for demonstrating the correct method of calculation.

Provided handwriting is legible, candidates will **not** lose marks if it is 'untidy'. Similarly, marks are not lost due to poor spelling or grammar.

Calculators

If you bring a calculator into the examination room, it must be a silent, battery or solar-powered, non-programmable calculator. The use of electronic equipment capable of being programmed to hold alphabetical or numerical data and/or formulae is prohibited. You may use a financial or scientific calculator, provided it meets these requirements. The majority of the marks will be allocated for demonstrating the correct method of calculation.

EXAMINER COMMENTS

Question 1
For part (a), most candidates could identify four types of delegated authority, although some confused types with the amount of authority (e.g. limited or full). In addition, five types were required but many candidates explained the different types after they had identified them, and no additional marks were available for doing this. Candidates are reminded to look at the question and the verb and ensure they don't waste time producing answers that cannot gain any marks. Part (b) was answered well, with many candidates achieving the full five marks.

Question 2
For part (a), many candidates correctly described the Lloyd's ATLAS system, however, only the stronger ones focused on the purpose of ATLAS. It is essential to read the question carefully to provide a focused answer that related specifically to the question. Part (b) was generally well answered with candidates providing their answers in list or bullet point format.

Question 3
In part (a), few candidates were able to clearly explain why a standard binding authority contract has a different format to an open market contract. Many who did went into detail, listing the different parts at length which was required in part (b). Part (b) was well answered with the majority of candidates gaining all three marks.

Question 4
For part (a), many candidates correctly defined the term run-off period, but few were able to explain what dictates its length. Most candidates provided good answers to part (b) although few achieved full marks.

Question 5
Although generally well answered, some candidates did not read the question carefully and so based their answer on complaints handling in general rather than claims related complaints. This question needed to be grounded in complaints related to claims and those candidates who did not realise this did not achieve good marks. However, there were some very good answers.

Question 6
The candidates who understood the role of the managing agent and answered within the Lloyd's context gained high marks on this question. However, some did not appear to understand what a managing agent's role was and therefore provided a general answer outside the Lloyd's context. The candidates who applied the mark allocation to the question were able to write a sufficiently detailed description to achieve the marks.

Question 7
Part (a) was a regulatory question and it was not very well answered. Many candidates identified contract certainty, but few identified all five compliance outcomes. Most answered in a list form which suited the question well. The legal and regulatory framework is an area which is not very well understood by candidates. In part (b), most candidates correctly identified staff training, although few could correctly explain it in enough detail to gain all the marks. Part (c) was very well understood with some excellent answers.

Question 8
Many candidates assumed that part (a) of this question was just about documentation issuance. In fact, a good understanding of the contents and operation of the contract of delegation was required and few candidates achieved all the marks available. Part (b) was very well answered.

Question 9
This was a well answered question with some very good answers, however, few candidates provided sufficient detail to achieve all the marks available.

Question 10
The majority of candidates explained the monthly bordereau, but few sufficiently justified this selection. Where a question asks for a justification, this means there could be more than one right answer and therefore, candidates need to take time to explain why they think, in this case, their selection of methodology is the most appropriate. Candidates who chose monthly bordereaux achieved some marks, but only those who went on to justify why gained maximum marks.

Question 11
A brief description was required for part (a), along with the identification of the benefits. Most candidates were able to identify some of the benefits. However, many candidates simply identified the benefit without a brief description and few achieved all five. In part (b), not many candidates correctly identified all four blocks of information, but most identified a few. Candidates understand the subject of delegated authority quite well, but Lloyd's specific processes, procedures and regulation, is not as well understood.

Question 12
Part (a) was very well answered with the majority of candidates identifying four practical steps. The one step that was often not mentioned was obtaining approvals. The verb identify indicates that only a very brief answer is required. In part (b), the focus was on the activities of a broker and many candidates did not mention this and instead spoke about what an insurer or just the coverholder might do.

Question 13
To answer part (a), candidates needed to understand what a service company was and to know something of the Lloyd's process. This part of the question was answered relatively well with many candidates identifying all five practical steps. Those who achieved less marks did not answer in the context of a Lloyd's service company. In part (b), only a limited number of candidates achieved maximum marks due to a lack of depth to their answers.

Question 14
Part (a) was a legal/regulatory question and the strongest answers included a simple diagram showing where each party, the insurer, coverholder and the insured, sit in relation to the contract. It is recommended that, even if not specifically requested, where appropriate a simple diagram is used if it can clarify an answer. It is also recommended that some explanation is also given to support the diagram. In part (b), there were some good answers, although few candidates identified all six potential remedies.

Question 15

This question was one of the most popular of the Part II optional questions. A general point to make is that candidates should manage their time carefully to answer questions as comprehensively as they can. If a candidate finishes before the end of the exam, they should go back and check their work and add to answers or fill in any gaps where appropriate. In part (a) of this question, the best answers were well grounded in the context and related back to the question. Overall, this was well answered by the majority of candidates. In part (b), some answers would have gained more marks if candidates had justified their answers. Part (c) was very well answered.

Question 16

Candidates who attempted this Part II question performed well. Part (a) was very well answered by candidates who correctly identified prior submit, pre-agreed rates and full authority. Part (b) was linked to part (a), therefore, candidates that had answered part (a) well also did so on this part. The best laid out answers used a table to capture their explanations, however, many candidates still gained maximum marks. This was a very well answered question with candidates clearly demonstrating they knew the subject well. Part (c) was less well answered than parts (a) and (b), but there were still some good answers and the strongest answers linked back to and focused on the question itself.

Question 17

This was another popular and well answered Part II question with the best answers relating back to the question. This question had three parts, part (a) financial, part (b) operational and part (c) regulatory considerations an insurer had to make when considering offering a delegated authority to a coverholder. The least well answered part of the question was the regulatory part, part (c). Candidates have a good general knowledge base of the operational, managerial and financial issues related to delegated authority, but are less knowledgeable of the legal and regulatory aspects.

THE CHARTERED INSURANCE INSTITUTE

P66

Diploma in Insurance

Unit P66 – Delegated authority

October 2017 examination

Instructions

- Three hours are allowed for this paper.
- **Do not begin writing until the invigilator instructs you to.**
- **Read the instructions on page 3 carefully before answering any questions.**
- Provide the information requested on the answer book and form B.
- You are allowed to write on the inside pages of this question paper, but you must **NOT** write your name, candidate number, PIN or any other identification anywhere on this question paper.
- The answer book and this question paper must **both be handed in personally by you** to the invigilator before you leave the examination room. **Failure to comply with this regulation will result in your paper not being marked and you may be prevented from entering this examination in the future.**

Unit P66 – Delegated authority

Instructions to candidates

Read the instructions below before answering any questions

- **Three hours** are allowed for this paper which carries a total of 200 marks, as follows:

Part I	14 compulsory questions	140 marks
Part II	2 questions selected from 3	60 marks

- You should answer **all** questions in Part I and two out of the three questions in Part II.
- You are advised to spend no more than two hours on Part I.
- Read carefully all questions and information provided before starting to answer. Your answer will be marked strictly in accordance with the question set.
- The number of marks allocated to each question part is given next to the question and you should spend your time in accordance with that allocation.
- You may find it helpful in some places to make rough notes in the answer booklet. If you do this, you should cross through these notes before you hand in the booklet.
- It is important to show each step in any calculation, even if you have used a calculator.
- If you bring a calculator into the examination room, it must be a silent, battery or solar-powered non-programmable calculator. The use of electronic equipment capable of being programmed to hold alphabetic or numerical data and/or formulae is prohibited. You may use a financial or scientific calculator, provided it meets these requirements.
- Answer each question on a new page. If a question has more than one part, leave six lines blank after each part.

PART I

Answer ALL questions in Part I

Note form is acceptable where this conveys all the necessary information

1. **(a)** Identify **five** types of delegated authority agreement. **(5)**

(b) Identify **five** activities that can be delegated. **(5)**

2. **(a)** Describe the purpose of the Lloyd's ATLAS system. **(5)**

(b) Identify **five** key areas covered by the application form on ATLAS. **(5)**

3. **(a)** Explain briefly why a standard binding authority contract has a different format to an open market contract. **(4)**

(b) Identify the **three** different parts of a binding authority contract document. **(3)**

4. **(a)** Define the term run-off period for a naturally expiring binder and explain what dictates its length. **(5)**

(b) Explain the role the insurer should adopt through the run-off period. **(5)**

5. Explain the need for good processes in relation to claims related complaints handling. **(10)**

6. Describe **three** of the minimum standards for managing agents, as identified by the Lloyd's franchise Minimum Standards for Delegated Underwriting. **(9)**

7. **(a)** Identify **five** compliance outcomes a regulator may seek to ensure, by placing requirements on insurers and, by definition, their coverholder-managing general agents (MGAs). **(5)**

(b) Explain briefly the most basic safety mechanism a coverholder-MGA can adopt to ensure regulatory compliance. **(3)**

(c) Explain briefly the key role of the compliance function of an insurer which has a large number of coverholder-MGAs. **(3)**

8. **(a)** Explain how the contract of delegation can assist the coverholder-managing general agent (MGA) when issuing documentation. **(5)**

(b) Explain briefly the benefit for an insurer when a locally based coverholder-MGA issues documentation. **(3)**

9. Explain how the delegated authority document assists with the performance and operational control of delegated authority. **(8)**

10. Explain, with justification, the most likely way in which an insurer will first identify any problems with the operation of a binder. **(5)**

11. **(a)** Describe briefly **five** benefits of Lloyd's central reporting standards. **(10)**

(b) Identify **four** of the blocks of information in which data is grouped by the Lloyd's central reporting standards. **(4)**

12. **(a)** Identify the **five** practical steps which need to be taken to set up a delegated authority agreement. **(5)**

(b) Explain briefly **one** activity a broker might undertake for **each** of the **five** steps identified in **part (a)** above. **(10)**

13. You are a Lloyd's managing agent considering setting up a service company.

(a) Identify **five** practical steps that Lloyd's suggest you should follow prior to establishment. **(5)**

(b) Explain how the Lloyd's service company should operate once established. **(6)**

14. (a) Explain the legal position of **each** party in a contract of delegation where the broker is acting as a coverholder-managing general agent. **(6)**

(b) Identify **six** potential remedies available to the principal if an agent fails in their duty. **(6)**

PART II

Answer TWO of the following THREE questions
Each question is worth 30 marks

15. You are the Manager for a managing general agent, BAC plc, which operates a number of delegated underwriting authorities. BAC plc's business has grown significantly over the last two years and you are considering seeking new capacity to write more business.

Your company currently operates a number of binders, some of which are for affinity groups, each for a distinct risk type, including small commercial, buildings, property owners and motor risks.

As a consequence of the growth in business, you are looking to employ more staff to support the existing team who are becoming increasingly stretched in terms of their work load. In addition, you are considering outsourcing parts of the business to assist with staff work load.

(a) Explain how a well written coverholder-managing general agent (MGA) business plan will assist you in obtaining more capacity to write business. **(5)**

(b) Explain, with justification, the **five** most significant topics you would include in your coverholder (MGA) business plan, which would assist you in obtaining more capacity from an insurer. **(15)**

(c) Explain **five** important considerations you would need to make when considering the future management of any new delegated authority agreements. **(10)**

16. You are the Underwriting Manager of a leading and respected insurer, looking to increase the volume of business they write and diversify their product portfolio without increasing their fixed cost base.

Traditionally, the insurer has operated in the open market, writing their smaller risks on a direct basis and their larger risks exclusively through insurance brokers.

You are considering approaching a number of your key brokers to discuss the possibility of offering them delegated underwriting authority agreements. Your compliance manager has expressed concern about delegating underwriting authority.

(a) Describe **three** ways in which underwriting authority could be delegated to a coverholder-managing general agent (MGA) providing different levels of control for the insurer. **(9)**

(b) Explain **one** advantage and **one** disadvantage for the insurer and the coverholder (MGA) for **each** of the **three** ways identified in **part (a)** above. **(12)**

(c) Explain **three** ways in which your marketing and business development team could work with a potential coverholder (MGA) to analyse the market and maximise the business potential. **(9)**

17. You are the Finance Director of an insurer. The Underwriting Director has asked if they can work with you to understand the cost implications to the business of offering a large delegated underwriting authority to a coverholder-managing general agent (MGA). The delegated authority would replace your entire low value property portfolio which is currently written on a direct basis.

You agree to work with the Underwriting Director to jointly look at the operational and financial implications of replacing your low value property portfolio with a delegated authority agreement.

When considering the delegation of the new underwriting authority, you and the Underwriting Director, quickly realise that there are compliance and regulatory considerations and approach the Compliance Director to work with you.

(a) Identify and explain briefly **three** key financial considerations when deciding whether or not to delegate authority to the coverholder (MGA). **(9)**

(b) Identify and explain **four** key operational considerations when deciding whether or not to delegate authority to the coverholder (MGA). **(12)**

(c) Identify and explain briefly **three** key compliance and regulatory considerations when deciding whether or not to delegate authority to the coverholder (MGA). **(9)**

TEST SPECIFICATION

October 2017 Examination – P66 Delegated authority	
Question	Syllabus learning outcome(s) being examined
1	1 – Understand the business benefits and risks for the use of delegated authorities
2	3 – Understand the setting up of delegated authorities
3	4 – Understand contracts of delegation and contracts of insurance
4	4 – Understand contracts of delegation and contracts of insurance
5	6 – Understand the management of claims by the coverholder/MGA
6	2 – Understand the legal and regulatory framework related to delegated authorities
7	2 – Understand the legal and regulatory framework related to delegated authorities
8	7 – Understand key business support functions within the coverholder/MGA
9	8 – Understand the monitoring and auditing of the delegated authority by the insurer
10	8 – Understand the monitoring and auditing of the delegated authority by the insurer
11	7 – Understand key business support functions within the coverholder/MGA
12	3 – Understand the setting up of delegated authorities
13	3 – Understand the setting up of delegated authorities
14	4 – Understand contracts of delegation and contracts of insurance
15	3 – Understand the setting up of delegated authorities 5 – Understand the management of underwriting by the coverholder/managing general agent (MGA)
16	1 – Understand the business benefits and risks for the use of delegated authorities 3 – Understand the setting up of delegated authorities 7 – Understand key business support functions within the coverholder/MGA
17	1 – Understand the business benefits and risks for the use of delegated authorities 2 – Understand the legal and regulatory framework related to delegated authorities 3 – Understand the setting up of delegated authorities 4 – Understand contracts of delegation and contracts of insurance 5 – Understand the management of underwriting by the coverholder/managing general agent (MGA) 8 – Understand the monitoring and auditing of the delegated authority by the insurer

NOTE ON MODEL ANSWERS
The model answers given are those which would achieve maximum marks. However, there are alternative answers to some question parts which would also gain high marks. For the sake of clarity and brevity not all of these alternative answers are shown. An oblique (/) indicates an equally acceptable alternative answer.

Model answer for Question 1

(a)
- Binding authority.
- Lineslip.
- Consortiums/Consortia.
- Group/Affinity programme.
- Master cover.

(b)
- Underwriting.
- Credit control.
- Document issuance and management.
- Claims.
- Subrogation/Recoveries.

Model answer for Question 2

(a) Lloyd's operates an online application and authorisation system for coverholders called ATLAS in which the coverholders can load all the requisite information for Lloyd's to consider. Brokers can also add the information on the coverholder's behalf if required. The system then manages all the ongoing information about coverholders, including changes to their approvals such as territorial extensions).

(b) *Any five of the following:*
- Company information: legal name, registration.
- Business strategy: details of the business and the business plan.
- Ownership.
- Key staff.
- Reputation and financial standing.
- Lloyd's and general binding authority experience.
- Professional indemnity insurance held.
- Accounts and financial information.
- Bank accounts including details of segregated accounts.
- Systems and controls.
- Business continuity plan: what to do if a disaster strikes the office.
- Licences: all authorisations and licences held.
- Underwriting and claims authority sought.
- Classes of business proposed.
- Territorial scope required: natural permission will be granted for a coverholder's home territory.

Model answer for Question 3

(a) The binding authority has a different format to an open market contract as it must capture the key details of the delegated underwriting contract, together with the other information, such as written lines, fiscal and regulatory information, subscription agreement and exposures.

(b)
- Binding authority schedule.
- Binding authority wording.
- Non-schedule sections.

Model answer for Question 4

(a) Run-off can be defined as the term where an insurance contract remains in force after a delegated authority has been cancelled. Insurance policies will normally remain in force during their contractual period of cover but will not be renewed when the term expires if the delegated authority is no longer in force. Claims will be paid in this period and service provided. The class of business involved will dictate the length of the run-off period, which will be until the risks naturally expire and all claims are finalised. A binder which accepted liability risks will generally take longer to run-off than a binder writing property risks. If not watched for, tacit renewals of underlying risks can increase the run-off time of a binder, even if the delegated contract has not been renewed.

(b) The insurer should continue to monitor the handling of the delegated authority all through the run-off period. For example, the insurer should be checking whether personnel are still employed who can handle any outstanding matters on the binder, such as claims. It should consider outsourcing that role should the coverholder-managing general agent (MGA) not have the requisite personnel going forward. The insurer will continue to honour the contract and continue to monitor performance.

Model answer for Question 5

Just as with any complaint, claims related complaints should be managed with good processes and procedures. Depending on the provisions in the binder, the coverholder-managing general agent (MGA) may have the authority to handle complaints. Alternatively, it may have to refer them automatically to insurers to handle. Whichever applies, there must be processes in place to capture the existence of complaints, the nature of those complaints and how they were resolved. Additionally, the very tight time frames imposed by the regulators for responding to complaints means that it needs to be possible to locate the claims file and forward it to insurers within a day or two of receiving the complaint. The Financial Conduct Authority's definition of a complaint is 'any expression of dissatisfaction, whether oral or written, and whether justified or not'.

It is very important that anyone handling business on behalf of an insurer knows how to recognise a complaint when it is made and to invoke the specific claims reporting and handling processes they have with their principals. Equally, it is important to appreciate that complaints do not just arise from the claims process but can also arise from the sales process as well. Whatever the trigger, a complaint needs to be recognised, recorded and dealt with appropriately.

The challenge for a coverholder-MGA and its processes occur when it has many binders with different insurers and the requirements under each are different. In this case, it is very important for the coverholder-MGA to be able to isolate the needs of each insurer and put in place strategies to ensure that its staff know which rules apply to each. The strategies can be quite simple ones, such as laminated sheets setting out the requirements for an expert appointment for each binder, through to more sophisticated options, such as inbuilt prompts in a computer system.

Model answer for Question 6

Any three of the following:

- The managing agent has a clear strategy for writing and managing delegated underwriting as part of its overall business plan. To evidence this strategy, there should be an executive summary outlining the objectives for the year, including financial, and a roadmap plan for how they will get there.
- The managing agent carries out thorough due diligence of the coverholder to which it intends to delegate the authority to. For coverholder-managing general agents (MGAs) that require Lloyd's approval, the lead managing agent will need to consider, as a minimum, the information required to be provided in the Lloyd's coverholder-MGA application form when it conducts its own due diligence.
- The managing agent has contracts in place with each third party to which it delegates authority. The managing agents need to ensure that there is complete, contract certain and signed documentation in place recording the binding authority prior to risks being attached to it. This code of practice sets out the detailed requirements which the market templates follow.
- The managing agent proactively manages delegated underwriting contracts once incepted. The code of practice requires that the managing agent ensures it has the necessary practical internal resources to monitor the contracts of delegation, for example through an in-house binder management team.

Model answer for Question 7

(a) *Any five of the following:*
- Ongoing permission to write the required classes of business.
- No breaches of sanctions.
- No failure to pay required taxes or charges.
- The contract is certain and satisfies the requirements of conduct risk.
- Ongoing permission to accept risks from a particular jurisdiction.
- The coverholder-managing general agent (MGA) remains approved by Lloyd's.

(b) The most basic safety mechanism is staff training on awareness of the issues and how to manage them. Coverholder-MGAs should be ensuring that all staff attends either internal or external training as often as required to keep their knowledge fresh and current.

(c) The key role of the compliance function will be to ensure that the sensible compliance/regulatory and legal steps that should be taken are taken, both before entering into any contract of delegation and during that contract.

Model answer for Question 8

(a) When it comes to issuing documentation, the contract of delegation/binding authority helps a coverholder in several ways. Firstly, the binding authority itself will set out the details of the wordings that have to be used in any particular risk bound. Some of these will be wordings that have to be attached to every risk and some will only be required depending on the type of business or geographical area. There may also be requirements that the coverholder-managing general agent (MGA) must follow in terms of the design and structure of the documents being issued. For a company market insurer, perhaps writing the risks 100%, then it could use its own branding and marketing to produce a document which shows, without a doubt, that it is the carrier.

For a subscription market placement, it is more difficult to utilise a single insurer's branding. But for those risks where the security is provided by Lloyd's syndicates, it is the Lloyd's logo that will be used as the central design on the certificate. This coupled, with the need to ensure that certain key clauses are always used, means that if a Lloyd's insurer wants to use non-standard certificates it has to get them specifically approved by Lloyd's first.

In the case of Lloyd's, instead of showing specific insurers, the certificate can show:

'Underwritten by XYX Co, on behalf of Certain underwriters at Lloyd's.'

(b) One of the benefits of using a coverholder-MGA is its local knowledge. Part of this knowledge should be knowledge of local regulatory requirements. A good example of this would be the fact that documentation must be issued in a local language or has to contain reference and contact details of the local regulator for complaints. A local coverholder will be much better placed to prepare documents in the local dialect and with regard to local laws and regulations. It can be an expensive process translating individual policy documents and there is also a regulatory risk if local regulations are missed.

Model answer for Question 9

The delegated authority document helps with the performance and operational control of delegated authority as a detailed delegated authority document sets out the parameters of the agreement between the insurer and those to whom the authority has been delegated. This gives both sides clear expectations of the other's performance. This then provides the base measure from which any monitoring of compliance with the terms of that contract can be done.

All parties to a contract of delegation must give due consideration to each of the contract's terms, remembering that it will face scrutiny for its compliance with the agreement. A relatively straightforward matter, such as a person with named authority leaving the coverholder-managing general agent (MGA) and being internally replaced with someone similarly experienced, may appear a domestic matter to the coverholder-MGA. However, it is, in fact, an important change in the contract provisions, which should be discussed with the insurer sooner rather than later. An insurer that discovers the change during a routine audit may have questions as to what other areas of non-compliance it might find.

Equally, for a consortium or lineslip, the parameters of the authority should be clearly set out in the contract of delegation and should be scrupulously followed, with referral as required if something is presented which appears to be outside the authority given but in which the insurers supporting the delegation might be interested.

Model answer for Question 10

The most obvious, but the most often overlooked, way of identifying issues is through a careful review of the monthly bordereau. This can often spot innocent mistakes, such as the acceptance of a risk outside territorial limits or of an exposure in excess of authority, where no referral has been obtained. Manual checks on bordereau that have varying presentation styles are both labour intensive and prone to errors. This is the reason there has been a move towards standardised data presentation. This, together with the ability to submit data in Association for Cooperative Operations Research and Development (ACORD) standard message formats, will enable insurers to use software solutions to electronically check the data being presented. This will not necessarily find all the issues but will enable many of the queries to be quickly identified. Auditing and monitoring are vital, but it is the monthly bordereau that will allow insurers to first identify any issues.

A recent Financial Conduct Authority review found that many insurers were not receiving enough data to enable them to consider whether service standards were being met or conduct-related behaviour carried out. It was recognised that monitoring would not always be the same and would depend on the nature of the product, distribution method and relative sophistication of the end customer.

Model answer for Question 11

(a) *Any five of the following:*

- A clear statement of the information the coverholder-managing general agent (MGA) needs to provide for the whole of the Lloyd's market. This provides a level of consistency and transparency.
- The freedom and flexibility for the coverholder-MGA to use its own systems and technologies, allowing cost efficiencies and time saving.
- Reducing the need for re-keying information and manual intervention. This not-only saves management and service time but reduces the likelihood of errors and mistakes occurring.
- Better informed decision making. Due diligence and monitoring is enabled against a consistent set of standards.
- Simpler standard information flows. This increases the ability to monitor, manage and control. But also contributes to contract certainty.
- A consistent list of requirements around which the coverholder-MGA can design its processes and systems.

(b) *Any four of the following:*

- Core risk information.
- Paid premium transaction information.
- Catastrophe exposure information.
- Class specific underwriting information.
- Claim information.

Model answer for Question 12

(a)
- Identify a suitable partner.
- Obtaining approvals.
- Deal direct or via a broker?
- Constructing the formal agreement.
- Processing and onward activity.

(b)
- Identify a suitable partner – brokers will have a wide range of relationships with insurers and may be able to bring an insurer together with a potential coverholder.
- Obtaining approvals – brokers will be able to assist potential coverholders with an insurer's approval process, especially if the Insurer is a Lloyd's Insurer and the broker is a Lloyd's broker.
- Deal direct or via a broker – the broker can of course act as the coverholder and they may well have a range of different agreements with different Insurers.
- Constructing the formal agreement – where the coverholder is a client of the broker, the broker may well prepare the first draft of the agreement and even negotiate on behalf of the coverholder to obtain wider policy wordings and coverage than the coverholder could have done on their own.
- Processing and onward activity – here the broker can be involved in moving data and/or funds between insurers and coverholders.

Model answer for Question 13

(a) *Any five of the following:*

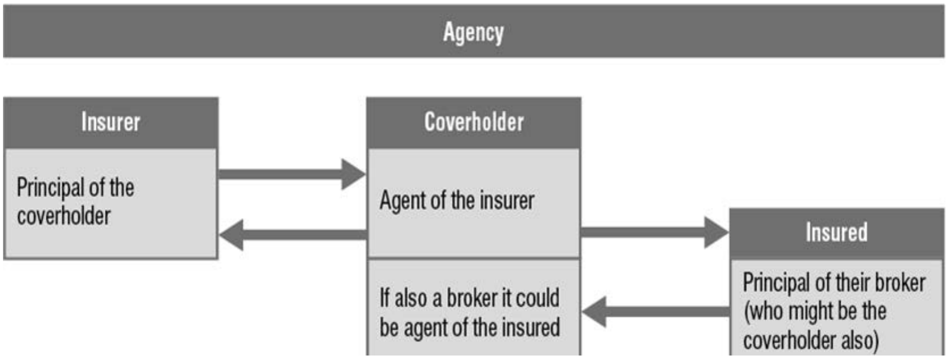
- Seeking legal advice to ensure it complies with local requirements.
- Considering the best option operationally – branch v company.
- Branding, both for Lloyd's and the parent entity.
- IT systems.
- Staff – expatriate v local.
- Tax issues both for staff and corporately.
- Capture and processing of data and funds.

(b) An insurance company, if it wants to write risks coming from a particular country, could choose to set up a branch office. This will enable it to take advantage of the benefits of local access to clients and brokers, but it will need to accept that there is a capital expenditure in the setting up of the office in the first place, which makes it an expensive choice. Lloyd's syndicates have the advantage of the very extensive Lloyd's licence network to be able to write business from around the world without ever moving from London. However, sometimes the brand is not enough. For exactly the same reasons as a managing agent might decide to enter into a binder with an external party, to get access to new markets, managing agents are now setting up subsidiary companies, backed by binders from the syndicate. These allow them to access different types of business while keeping it all 'in the family'.

A Lloyd's service company is a very particular type of coverholder and still requires approval from Lloyd's. However, here the starting point is a meeting with the delegated authority team at Lloyd's to discuss what is planned, the business plan etc.

Model answer for Question 14

(a) The diagram below shows the legal position of each party in a standard contract of delegation.



The actual authority that an agent has devolves from the contract under which the authority has been granted. However, there is always the danger that an agent will act outside its authority and bind its principal to something unexpected. An agent has a fiduciary duty, arising from a trust-based relationship, to their principal. So, a broker who is also a coverholder has duties in two different directions and must manage those situations so as not to prejudice either principal.

(b)
- Sue the agent for damages for breach of contract.
- In certain cases, sue the agent in tort.
- For a serious breach dismiss the agent without notice or compensation.
- Sue the agent (or the donor) to recover a bribe paid to the agent.
- If the breach is fraudulent, rescind any contract made through the agent and refuse commission.
- Sue for an account if the agent fails to disclose full financial details of its agency dealings.

Model answer for Question 15

(a) BAC plc must convince an insurer that it is good business sense to offer them a delegated authority agreement. It can do this through the coverholders business plan.

BAC plc has good affinity relationships and already operates a number of binding agreements across a range of different risk types. All of this is good information for an insurer who might also see the benefits of gaining more business without the time consuming and non-cost effective administration and underwriting of high volume, low value risks.

The business plan will assist BAC plc's chances of obtaining more capacity to write business as the insurer will be able to match the business and financial targets with their own and grant capacity in line with their own strategic plan and strategic goals.

(b) *Any five of the following:*

Topic	**Key points in the plan**	**Why important?**
Organisational structure	The key personnel and their experience – their CVs should be provided as part of the submission. Wider organisational structure including back office support functions.	The efficient and effective operation of a coverholder is important. The insurer will want to be happy it will get clear and accurate data regularly presented, together with good accounting for funds.
Capital and sources of finance	Is the coverholder part of a larger organisation? Where does the capital come from – is it just the principals?	The insurer will be wanting to deal with an entity that is well capitalised and capable of surviving difficult economic conditions.
Authority	Scope and levels of authority being sought.	The coverholder will probably pitch for more authority than an insurer will be prepared to give, at least in the early stages of the relationship. However, the prior experience of the personnel actively involved in the business will help persuade insurers to grant authority of any kind.
Which classes of business	If a coverholder is a specialist in a particular class of business, then this is not a particularly hard sell to an insurer. However, it could be that a coverholder is looking to expand its portfolio within a certain location and, therefore, must convince the insurers that it has the infrastructure to be able to handle any new class.	From an insurer's perspective, one of the appealing things about a delegated authority is the fact that the proposed coverholder is knowledgeable about a particular class of business. However, where the coverholder is looking to expand outside its previous area of specialisation the insurer must satisfy itself that the coverholder understands the business. Of course, it could grant prior submit authority, where the coverholder has to refer all risks to the insurer at least for the first year or so.

Locations	The coverholder has to consider its target market in terms of location, which may be far wider than where it is located as a business.	The insurer must be completely satisfied that the coverholder is authorised to accept business in any area in which it wants to operate and fully understands any regulatory requirements that might be in place. One of the challenges is that the requirements vary greatly from place to place. Finally, the insurer must also be happy that the coverholder will be able to source the same quality risks from any new locations.
Access routes	The coverholder can potentially source business directly, via brokers or using web-based systems.	The insurer should be considering how, in particular, ICOBS and TCF provisions can be complied with using web-based systems and how to make sure that the information provided to potential customers is clear and unambiguous.
Marketing strategy	When putting itself forward for a new piece of delegated authority a coverholder has to show how it will attract the business that will attach to this contract. Part of that is linked to the previous two headings of locations and access routes.	Quite simply, the insurer has to consider whether it thinks that the promises made can be realised or whether the coverholder's aspirations are unrealistic (perhaps because a particular market is already saturated with insurer capacity).
Premium estimates	This will include overall premium income projections and also pricing analysis for those risks where the coverholder would be making those decisions.	The insurer must ensure that the pricing strategy accords with the insurer's own pricing methods and that the premium income estimates fit within the wider business of the insurer.
Remuneration expectations	The coverholder should set out how it expects to be paid, for example, commissions, and how much it hopes those commissions will be.	The insurer may not agree with the proposed level of commissions of course.
Outsourcing	The coverholder should make clear those aspects which it would not seek to perform itself, for example, claims handling or credit control, and provide transparency within its explanation of its organisational structure in this area as well.	This allows the insurer to decide how it wants to handle these aspects. It might decide to engage others directly to handle claims, but be more relaxed about outsourced credit control, if given confidence that the coverholder manages that contract.
Holding of funds	Where a coverholder is handling claims it will often seek to hold a claims fund from insurers to enable speedy payments to be made without having to use the coverholder's own funds.	Insurers should be satisfied that the coverholder has internal processes for the management of funds, particularly if it holds funds for more than one insurer, so as to ensure that the funds are not intermingled.

Data capture and reporting	The coverholder has to demonstrate that its systems can capture all the necessary information relating to risks and claims that the insurers will require.	Insurers must be aware of their own requirements in terms of onwards regulatory reporting and therefore what data they will require from any coverholder.
Regulatory controls	The coverholder should explain in practical terms how it manages matters such as financial crime risk.	Insurers should be satisfied that the internal controls are satisfactory and cover all aspects, such as money laundering and bribery.

(c) *Any five of the following:*

Who will actually hold the underwriting authority?
The coverholder-managing general agent (MGA) must ensure that the person who holds the authority is given the tools necessary to enable them to carry out their role. A more important consideration, is that if that person leaves the organisation they will need to be replaced. The permission of the insurers will then need to be obtained for the new person for them to have the authority to bind.

Mix of business being accepted
If for example, the binder provides for both property and casualty to be written, the agreement might provide for the acceptable ratio between the two classes over the entire contract. A coverholder-MGA must ensure that it has the monitoring structures in place to ensure that any balance provided for in the contract of delegation is maintained. Even if there is no express split between classes contained in the binding authority agreement, it would still be good business practice to ensure a balanced book.

The type and size of risks being accepted
This should also be considered and monitored as part of balancing the portfolio. A book of business made up solely of a type of risk (for example, out of town retail units) is unbalanced and might suffer adversely from one type of loss for example, theft. A better balance might be achieved by mixing the retail units with some office type risks.

When accepting risks, a consideration must be made as to what is already on the books (the same concept applies to writing open market risks). Insurers will not want unexpected or unintended saturation or aggregation of risks which will lead to large numbers of claims arising out of single events.

Marketing and acquisition of risks
It is important to constantly consider whether the strategy set out in the business plan for marketing, and the expectations of the likely conduits through which business is going to be received, are actually proving themselves in reality. If the marketing ideas are not providing the inwards flow of potential new business desired, then the coverholder-MGA should assess quickly whether other options are viable.

An area linked to marketing and acquisition of risk, which was highlighted in the 2015 Financial Conduct Authority's thematic review of delegated authority, 'Delegated Authority: Outsourcing in the General Insurance Market, July 2015', is where products are being developed and marketed by the coverholder-MGA with little or no input or engagement from the insurer. Of particular concern were those products which, because of their likely customer base, were felt to be high risk (e.g. consumer client). Insurers are not considering the customer in enough detail and whether, for example, there is any risk of them being sold an unsuitable product. A good coverholder-MGA/MGA will be aware of the issues with conduct risk and will be engaging in behaviour that protects the customer but a less diligent one might not.

One area of concern for the regulators is if the message getting to the customers, via the distribution chain, is not good enough and this leads to potential mis-selling of a product. Ultimately, the insurers might end up paying claims it was not intending to and which are not valid. Whilst doing so is a good customer outcome, given that the customer was not to blame for the problem, this scenario highlights what can be described as a breakdown in the integrity of the distribution chain.

Premium

Writing business that is unprofitable is not evidence of good management of an underwriting portfolio. For those binders that are prior submit or pre-agreed rates, the risk remains firmly with the insurers. However, for those binders that give full rating and decision making authority to the coverholder-MGA, the challenge remains with it to ensure premium adequacy.

As with other matters, there may be a reference in the binder agreement to required average premiums. Even if there is not, there should be an analysis of the risks written to ensure that the rates being achieved are monitored, and a careful scrutiny made of whether the premium achieved is adequate for the risk being accepted. This is particularly important for business that is renewing to measure whether any change in the risk is reflected in the price obtained going forward. The insurer will also have a view on renewal success and rate strength expectations.

Locations

Any insurer should be keen to know in what locations it is accepting risks and where there might be a danger of aggregation of risks or exposures. For binders writing static risks, such as property, the issue is more to do with ensuring that the location related information is captured. For binders accepting mobile risks, such as recreational vessels, cargo or travel, there can never be any certainty before the incidence of a claim as to where risks may have aggregated together.

The binder agreement may have set out specific requirements as to the extent of any aggregate acceptable. This can either be in relation to specific locations, or in relation to the potential for particular natural catastrophe events in certain locations. A key part of location related portfolio management is inspection and survey work, which might include specific activities such as flood mapping if property risks are being accepted in areas known to be susceptible to such risks.

Profitability

While this is not going to be immediately obvious, a coverholder-MGA should be paying close attention to the claims figures, including any expert spend associated with claims. It needs to ensure that the loss ratios presented as part of the business plan are manifesting themselves or if there is a wider problem that should be addressed sooner rather than later. The types of problem that might arise is an unforeseen issue with a wording. Good portfolio management would involve addressing that issue with the insurers and being able to quickly see which risks were attached to the binder using that wording. This will enable the insurers to consider what, if anything, they feel should be done.

Model answer for Question 16

(a) Prior submit/no actual decision making authority delegated

In this situation, the holder of the binding authority actually has no specific authority to make decisions on its own. However, to an outsider, the coverholder-managing general agent (MGA) is holding authority on behalf of insurers, which itself is still an attraction. If any risk is presented to the coverholder-MGA that it believes might be appropriate to attach to the binder, the coverholder-MGA refers the risk to the insurers who gave it the binder for their agreement. Once insurers give their feedback, which will include the price, the coverholder-MGA can finalise the acceptance. The customer never needs to know that the coverholder-MGA does not hold authority. This is a good starting point in any coverholder-MGA/insurer relationship.

Pre-agreed rates

In this scenario, authority is delegated to the coverholder-MGA to decide and agree the acceptance of risks. However, it cannot decide the rate of premium to be charged completely independently. The insurers will provide a set of rates and criteria. Anything falling outside the criteria, but within the general scope of the authority, will have to be referred to the insurers for their agreement and pricing advice.

Full authority

In this case, the coverholder-MGA has authority both to accept risks and also to set the rates independently, without reference back to the insurers, as long as the risk falls within the criteria set within the binding authority document.

(b)

Insurer		**Coverholder**	
Prior submit			
Advantage	Disadvantage	Advantage	Disadvantage
High level of control	Time consuming	Access to insurer policy	Slow turn around
Pre-agreed rates			
Advantage	Disadvantage	Advantage	Disadvantage
Good control of rating	Inflexible Underwriting	No need to refer all risk to insurer	Inflexible underwriting
Full authority			
Advantage	Disadvantage	Advantage	Disadvantage
Minimum admin time	Least control	Fast service	Need high level of training

(c) Analysing the market

One of the key appeals of a good coverholder-MGA will be the particular knowledge that it provides of its own market, location or specialism. A coverholder-MGA must make a convincing case as to where it expects business to come from when presenting a proposal for the provision of capacity. The business can come from several different areas such as a niche market, an affinity relationship, existing clients or even new staff joining the business with their own relationships.

Distribution analysis

Just as an insurer has already considered distribution as part of its decision to utilise binding authorities, the coverholder-MGA can do the same thing to identify whether there are smarter ways of attracting business. One of the key ways will be the use of e-business formats by which enquiries, quotes and even binding can be done in an entirely e-enabled way. This format, when used for cargo type insurances for example, also allows the customer access to a secure certificate format whereby they can print off documentation. They can then provide this to their own clients as part of the sale contract for goods.

One further development of this idea is to have online portals trusted brokers have access to, and into which they enter answers to questions – immediately generating a quote. If the quote is accepted, the contract can be bound, and insurer contract documentation immediately produced. This provides all the benefits of wider distribution tools whilst retaining the underwriting control with the insurers.

Marketing the business

Even if a coverholder-MGA develops the most innovative product in the market, if customers are not aware that it is available there will be few sales, if any at all. Part of the marketing and distribution analysis will focus on the optimal way to reach the maximum number of the target audience.

The types of risks being placed, and the use or otherwise of intermediaries, will have an impact on the appropriate methods of marketing. Methods can vary from advertising in various media through to sponsorship of events or education seminars.

A prior analysis of the distribution network and target audience should improve the coverholder-MGA's business plan and make its presentation to the insurer more meaningful. It will also provide a more thorough understanding between the insurer and coverholder-MGA of each other's marketing philosophy. An insurer that works hard on its brand image does not want it damaged by unfortunate marketing activity carried out by a coverholder-MGA using its name. In the same way, a coverholder-MGA might seek financial support for marketing activity from the insurer to promote the product.

Model answer for Question 17

(a) Solvency/financial standing of coverholder

It is important to understand the financial standing of any potential coverholder before entering into any agreement. Depending on the contract of delegation, the coverholder could be handling both client and insurer funds and any solvency issues could impact on the insurer's bottom line as well as causing reputational damage.

Proposed financial targets/volumes

Any contract of delegation must be of financial benefit to the insurer and the coverholder. Both parties should agree achievable targets and volumes, so a detailed budget can be calculated, and the financial benefits clearly understood. If the figures don't add up, no agreement should be entered into. The targets can be used to assess progress on a regular basis.

Profitability/remuneration agreement

In the same way as financial targets and volumes, profitability and remuneration should be understood in advance of any agreement being made to ensure both parties achieve their desired profitability levels. Again, these profitability levels can be included in the overall financial plan.

(b) How to monitor

It is important that the insurer has a method of managing the coverholder's performance against the budget and plan. Are volumes being met, is the profitability as expected, is the coverholder operating the authority within the guidelines or are there breaches? There are many ways in which the insurer can monitor the coverholder, through the monthly bordereaux, and more formally through audit. The method of monitoring should be agreed, and all parties should understand the extent of monitoring prior to a contract of delegation being agreed.

Extent of delegation/control

The extent of delegation can be limited, or it can be wide (from prior submit to full authority). Limiting the extent of authority initially will give the insurer an element of control. Contracts of delegation can be wider in future years depending on coverholder performance.

Experience of coverholder staff/training

When deciding the extent of authority to be delegated, the insurer will need to understand the experience of the key staff who will be operating the binder on a day-to-day basis. The more experience, the wider the authority the insurer may feel able to delegate. With a full knowledge of staff experience in the coverholder, the insurer and coverholder can jointly agree the level of training required.

Policy wording and agreement

The policy wording is important as the insurer will need to offer wide enough cover for the coverholder to attract business, whilst ensuring profitable underwriting. This is where the experience of the coverholder in knowing their customers is combined with the experience of the insurer in writing policy wordings. The two combined mean that the coverholder can offer its customers a wording that suits their needs whilst at a sustainable and profitable price and breadth of cover.

(c) Reputation and make-up of coverholder's compliance team

The insurer will want to understand the make-up of the coverholders compliance team and the regulatory procedures they have. The prospective coverholder's compliance team are likely to have a reputation in the market. The insurer will be handing over authority to a coverholder and will want to ensure that the compliance procedures are at least as good as their own.

Which individuals have authority?

The insurer will likely limit 'the power of the pen' to those with the right experience to ensure the authority is managed and controlled. Experience and training are important and those with authority should be 'authorised persons' from a regulatory perspective.

Any regulatory history

The insurer will likely look at the regulatory history of the coverholder to see if there are any regulatory breaches in the past and understand why they happened. The insurer will be looking for any regulatory 'skeletons in the closet' prior to contractual agreement.