



Binding Authorities: True Love or a Marriage of Inconvenience



PRESENTED TO:
INSURANCE MARKET CONFERENCES
6TH FEBRUARY 2014
BY:
BERND G. HEINZE, ESQ. – AAMGA EXECUTIVE DIRECTOR



Coverholder Tribunalisation Approved





Who are the AAMGA?

AAMGA



- Organised 1926
- Minimum membership requirements
- Membership composition:
 - MGA's
 - US & UK Markets
 - Business Services
 - State Surplus Lines and Stamping Offices
- 1987: Education Foundation created
- 1991: Under Forty Organisation

AAMGA



- **Wholesale Insurance Membership Criteria:**
 - Underwriting facility with delegated binding authority
 - ✦ MGA, MGA, Program Administrator/Manager, Aggregator, Broker
 - One Market (Admitted/Excess & Surplus Lines)
 - One Line of Business
 - US\$ 1 million AWP
 - 3 letters of recommendation from other existing Wholesale Insurance members
 - Certification of Compliance with AAMGA Code of Ethics
 - Approval by Board of Directors

AAMGA Membership Composition - 2014



- 258 Wholesale Insurance members
- 132 US and international risk bearing (80%) and non-risk bearing (20%) Associate members
- 59 Business service members
- 14 US State Stamping & Surplus Lines Offices
- 463 Total Corporate Members
- 407 Under Forty Organisation Members

The Present



- **258 Wholesale Insurance/Coverholder members**
 - 78% transact business as wholesale MGA/MGU with binding authority
 - 29% transact business as Program Administrators/Managers with binding authority
 - 22.5% transact business as Aggregators with binding authority
 - 20% transact business as Broker Producers without binding authority

AAMGA Membership Composition



- 258 Wholesale Insurance member demographics
 - 31.2% are 20 – 30 years old
 - 26.7% are 31 – 40 years old
 - 28.4% are 41 – 50 years old
 - 13.7% are over 50 years old
- 57.9% are under the age of 40 years old

The Present



- 258 Wholesale Insurance members
 - Underwriting facilities with delegated binding authority
 - Total AWP:
 - ✦ 2013: US\$22.4 billion
 - ✦ 2012: US\$20.6 billion
 - ✦ 2011: US\$19.2 billion
 - ✦ 2010: US\$16.4 billion
 - AWP Broked into Lloyd's:
 - ✦ 2013: US\$3.26 billion
 - ✦ 2012: US\$2.73 billion

AAMGA Current Efforts



- Strategic Planning Progress
- Student White Paper Contest
- Lloyd's & London Market Education Tract
- Expansion of communications and outreach
 - “@AAMGA” Newsletter (every other month)
 - Social Media Channels (Facebook, LinkedIn, Twitter)
 - “Wholesale Insurance News” magazine (1.2 million distribution)
- Appointment of Peter Barrett of Bell + Clements to Associate Members' Position on Board of Directors

AAMGA Digital NewsRoom



**Sharing Expert Commentary on the Issues and Opportunities
Impacting the Wholesale Insurance Marketplace**

AAMGA Current Efforts



- Focus on technology and young insurance professionals
- Facilitating efforts of 10 volunteer committees
- Increasing educational opportunities and professional development on-line and in person; advancing business competencies , LOB specialisation and profitability
- Enhancing the value proposition by advocating the distribution of insurance products and services on a wholesale platform and underwriting expertise of AAMGA members
- Enhance existing and create new relationships with College and University RMI programs as pipeline for new wholesale professional talent
- Active engagement in legislative and regulatory affairs

AAMGA Current Efforts



- Liaising with domestic and international trade associations and all segments of the wholesale insurance market
- Fostering of relationship and efforts with London Brokers and Lloyd's
- Embracing the principles articulated in Lloyd's Vision 2025
- Enhancing diversity and inclusion initiatives to better represent the entire wholesale underwriting community
- Networking among Coverholders and all stakeholders of the wholesale insurance market
- Advocacy to federal, state and international regulators and legislators, rating agencies and trade organisations

Market Rates & Movements

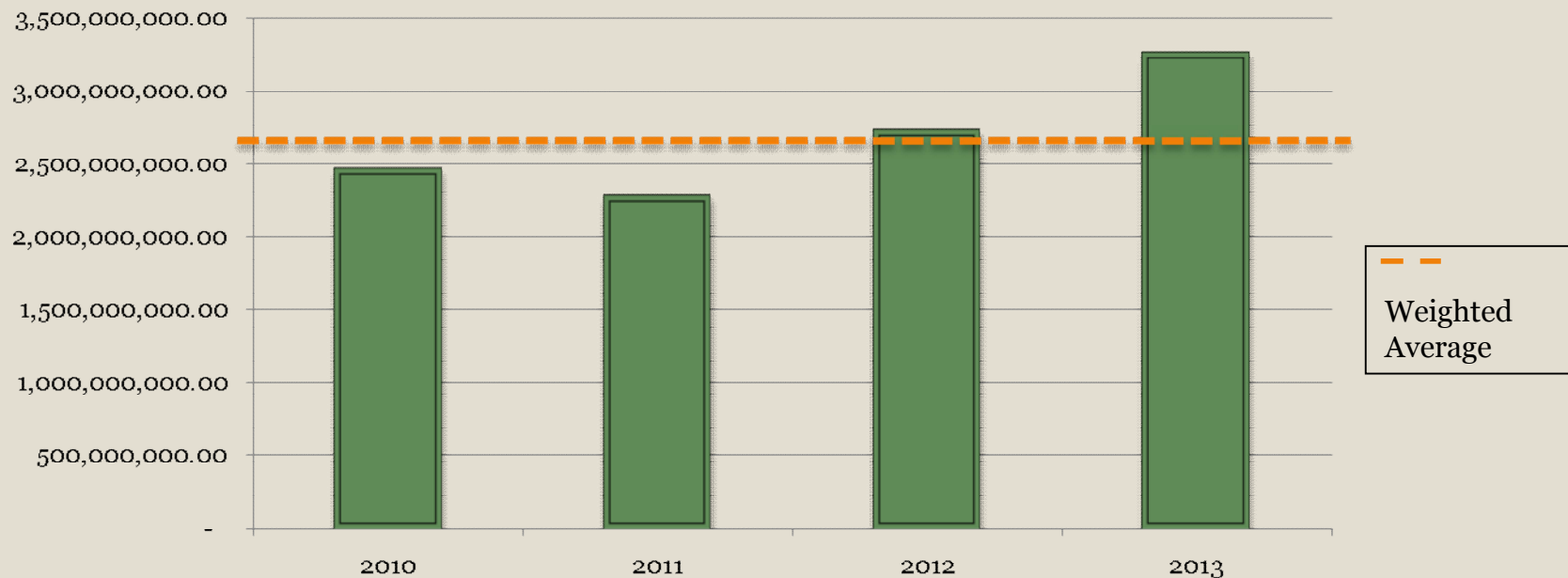


- 2014 E&S Drivers:
 - E&S outpacing domestic P&C industry
 - Considerable returns on operating profits and returns on revenue and surplus
 - Moderately aggressive release of prior-year loss reserves
 - Unstable US economy
 - ✦ Underemployment, unemployment, interest rates
 - ✦ Tapering of QE
 - ✦ Congressional dynamics
 - Significant market capacity
 - Continuing withdrawal of admitted markets from traditional E&S LOB's
 - Emphasis on bottom line profitability vs. top line organic/revenue growth
 - Underwriting expertise
 - Freedom of rate and form

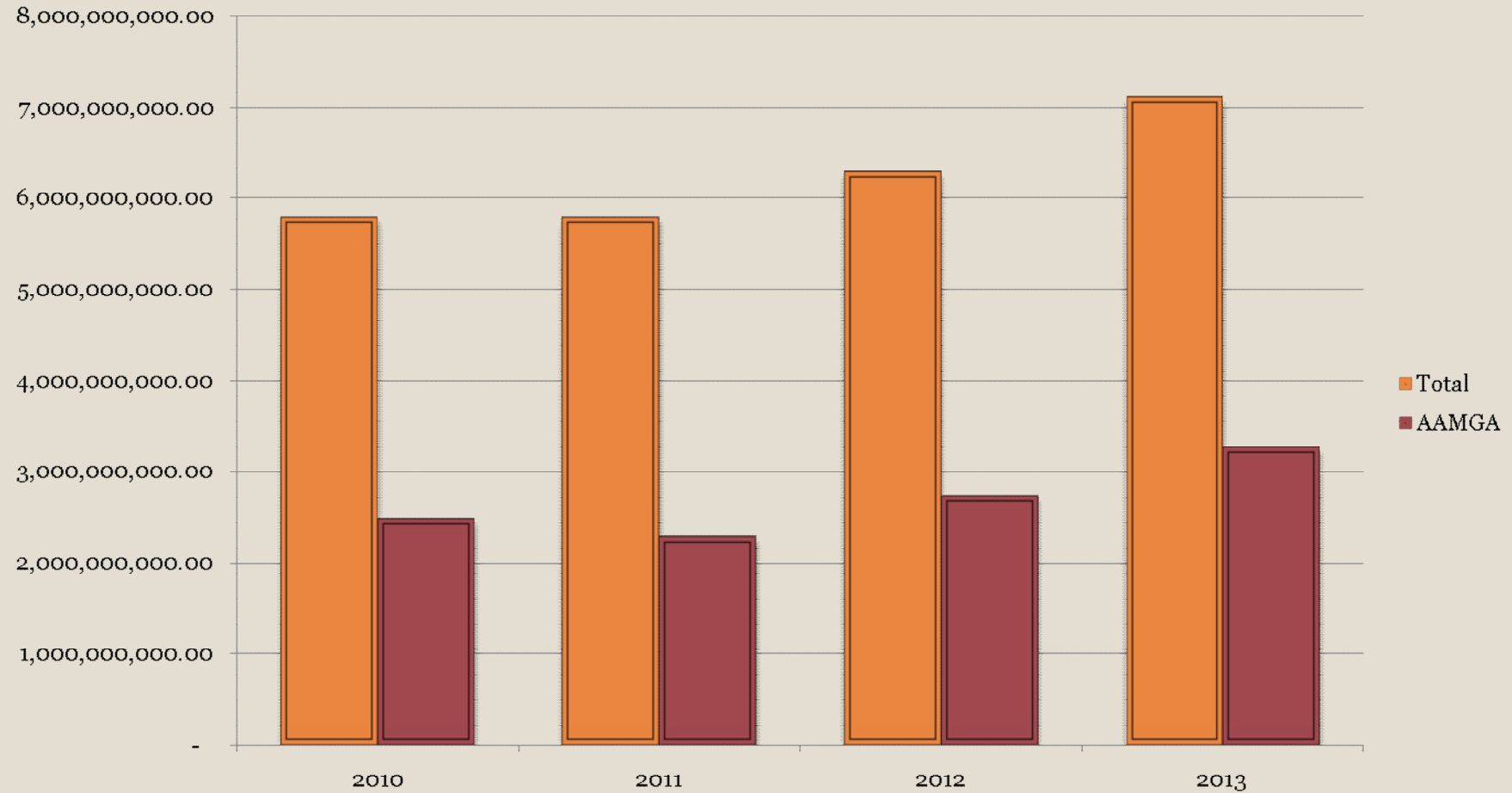
AAMGA Member AWP Broked Into Lloyd's



- Risks placed through trusted relationships with Lloyd's Brokers
- 2013: US\$3.26 billion
- 2012: US\$2.73 billion



AAMGA Coverholders AWP vs. Total Lloyd's US AWP



Collaborative Efforts with Lloyd's



- Coverholder Guidance
- Audit Scope
- Regular communications / joint presentations with Lloyd's and Lloyd's US on matters impacting Coverholders and domestic wholesale market
- AML/OFAC Guidance
- Tribunalization
- NAIC/FIO/FCA/NFIP efforts
- Enhancing Coverholder competencies and business acumen



New Opportunities



- Cyber Liability
- Supply Chain Liability
- OFAC E&O
- DIC & Earthquake
- Property CAT
- E&O / D&O (NPO) / KRE
- Business Owner Policies
- Excess & Umbrella Covers
- Relentless appetite for more aggregate

New Opportunities



- Automation & Technology
- Coverholder E&O
 - NRRA vs. AM Best ratings
- The models & RMS predictive analytics/Big Data
- Impact of investment interest on rates: “Flat is the New Up?”
- Impact of continuing mergers & acquisitions
- Succession & continuity plans
- Disintermediation
- Relentless underwriting discipline
- Education & Professional Development
- Attracting and retaining competent and young professionals

Coverholder Business into Lloyd's Developments & Trends



- AAMGA members anxious to increase revenues into Lloyd's
- Appreciate and acknowledge UK regulatory environment
 - Understand varying risk appetites and business operations among Managing Agents and capital providers
- Hurdles and operational costs associated with compliance vs. underwriting, production and marketing specialisations
 - Impact on business flowing seamlessly into Lloyd's
- Prepared to continue ensuring compliance with necessary, non-equivalent/non-redundant regulations and guidance

Coverholder Business into Lloyd's Developments & Trends



- Balancing Lloyd's objective in establishing model Wordings that will protect the franchise and ensure uniform interpretation and application of compliance standards, with
- Coverholders in the United States being afforded the opportunity to access the Lloyd's trading platform without burdensome/non-essential regulations that do not add to the operational transfer of risk or the quality of underwriting.

Coverholder Business into Lloyd's Developments & Trends



- “Model Wordings” allow the parties to freely amend as required or to create bespoke wordings so long as they meet Lloyd's requirements – however –
 - Issues on varying interpretations of Model Wordings by individual Managing Agents/Syndicates

Coverholder Business into Lloyd's Developments & Trends



- Temper proportionate and consistent application of balanced regulatory and claims requirements
 - Hurricane Sandy
 - Financial Crime
 - Binding Authorities Guidance
 - ✦ §26 Complaints or Proceedings
 - ✦ Financial Crime Provisions
 - Audits
 - Contract Renewals / Continuous Contracts
 - Automation & Technology
 - Predictive Analytics & Modeling
 - Office of Federal Assets Control (OFAC) (US & European)
 - Foreign Assets Tax Compliance Act (FATCA)

Issues & Opportunities



- The consistency of inconsistencies:
 - Varying Interpretation(s) of Lloyd's Guidance
 - Audits
 - Audit Scope
 - Hurricane Sandy coverage declination letters and claim practices
 - Time and process required to renew Coverholder Contracts
 - ✦ Prospect for expedited procedures or a form of Continuous Contracts
- Prospect of regulatory compliance and enforcement sanctions impeding creative solutions to specialized risks and the freedom of rate and form; and

Coverholder Objectives



Why all the fuss?



- Wholesale insurance delegated binding authority market has basic tenets:
 - Freedom of rate and form
 - ✦ Manuscript forms written around the risk vs. ISO form terms and conditions
 - ✦ Domestic and international regulations, sanctions, guidance
 - ✦ Quickly become the most regulated unregulated segment of the market
- Independent stakeholders mutually/exclusively dependent on one another



Why all the fuss?



- Wholesale insurance delegated binding authority market has basic tenets:
 - Specialty cover for unique risks
 - ✦ New enterprises
 - ✦ New inventions
 - ✦ New risks
 - ✦ Risks without adequate or no loss history
 - ✦ LOB's the admitted market has exited
 - ✦ Non-traditional / manuscript wordings
 - ✦ Disciplined underwriting

Why all the fuss?



- Wholesale insurance delegated binding authority market has basic tenets:
 - Coverholder trusted relationships with retail producers and Markets
 - ✦ Entrusting the underwriting pen
 - Coverholders compete in entrepreneurial marketplace on rates and forms
 - Marketing and specialised product knowledge
 - Maintaining relevancy of the channel
 - Business continuity and succession planning

Today's Theme



**True Love isn't
Found.
It's Built.**

pdf (2011)

Benefits of Coverholders



- Enhanced premium volume and distribution channels
- Reduces need for in-house staff (salaries, benefits, etc.), bricks and mortar, and run-off severance
- Local Presence / Local Knowledge / Good will
- Unique Market/Product Niche or Geographic Segment
- Knowledge and existing relationships with producer network
- Some MGA's/MGU's already have reinsurance treaties in place for LOB

Coverholder Best Practices



- **AAMGA Member**
 - Membership vetting process
 - CMGA / CIW certification
- **LOB specialisation**
 - extensive industry experience in both management & operations
- **Up to date technology and automation platform**
- **Performance/trending data**
- **Succession Plan**
- **Business Continuity/Disaster Plan**

Coverholder Best Practices



- Positive reputation among industry peers
- Quality of other markets represented and performance experience
- Relentless focus on education & professional development
- Empowerment of young professionals
- Understanding and compliance with rules and regulations
- Skin in the game



Current Challenges



- Technology
- Talent
- Perpetuation & Succession
- Costs of licensing and compliance
- Market cyclicalities
- Predictive modeling
- Threats of disintermediation
- Investment market / mergers & acquisitions
- Remaining relevant

Spotting the Problem Coverholder



- Power of the Pen/No Skin in the Game/Incentive to Generate Premium Without Accountability for Bad Risks vs. MGA's executing best practices and tying results/commissions to key performance indicators and risking loss of binding authority and/or reinsurance for poor results
- Power over Funds/Information and Process Control
- Record keeping
- Commingling of premium and trust/claim accounts
- Slow Pays/No Pays
- Disputes (once in a dispute, information flow grinds to a halt)

Spotting the Problem Coverholder



- Is the Coverholder adhering to the underwriting guidelines?
- Is the Coverholder selecting the right retail producers and proper risks?
 - U/W Guideline should include a section describing the characteristics of a target risk.
- Is the program achieving the desired results?
 - Target loss and combined ratios
 - Mix of business (e.g. state, class and limits distributions)

Monitoring Methods



- Individual account referrals
- Reports
 - Underwriting results
 - Rate and price monitoring
 - State and limits distributions
- Audits

Monitoring Methods



- Individual account referrals
- Accounts where the PA does not have binding authority
- Criteria defined in the underwriting guidelines
- Typical criteria:
 - Premium/exposure threshold
 - Higher limits
 - Hazardous class
 - Location (e.g. CAT zone)
 - Poor loss history

Monitoring Methods



- Reports
 - Underwriting results
 - Rate and price monitoring
 - Renewal ratios, new vs. renewal split
- Profiles
 - State/territory
 - Limits
 - Classes
- Submit/quote/bind ratios

Monitoring Methods



- **Audits**
 - Underwriting
 - Claims
 - Actuarial
 - Financial Protocols
 - Systems
 - Bank Account Trust Fund
 - License compliance
 - Human Resources/Hiring/Firing
 - Continuing Education
 - Law suits against Coverholder/Liens
 - Wrap-up meeting

Starting Solution



Communicate
Communicate
Communicate

Starting Solution



Preventing Pitfalls



- Due diligence before inception of relationship
- Underwriting Controls (Guidelines Must Be Detailed and Attached to Agreement)
- Premium CAPS or maximum annual premium volume must be stipulated
- Identify basis of rates to be charged
- Document and verify types of risks to be written
- Enumerate maximum limits of liability
- Identify applicable exclusions

Preventing Pitfalls



- Note territorial limitations and detail exclusivity, if any
- Document policy cancellation provisions
- Classify renewal criteria
- Establish maximum policy period
- Verify each of the above elements on a regular basis by independent audit

Preventing Pitfalls



- Claim Controls
 - Delineated with specificity in the Agreement
 - ✦ How and to whom to report claims
 - ✦ Coverage/Bad Faith Issues
 - ✦ Settlement authority issues
 - ✦ Life cycle of claim

Closing Views



*“In the end you can always count on the Americans
to do the right thing...
After they have tried everything else.”*

Winston Churchill

Take Aways



- Every relationship starts with a courting process
- Know your business partner
- Transparent exchange and alignment of interests
- “Trust but verify”
- Exit strategy





Embracing *Tomorrow's Opportunities*

88th Annual Meeting
18th – 21st May 2014
Hilton Waikoloa, Hawaii

Thank You



Bernd G. Heinze, Esq.
610 Freedom Business Center
Suite 110
King of Prussia, PA 19406
+610.992.0022 (o)
+610.992.0021 (fax)
bernie@aamga.org
www.aamga.org