

General Insurance Convention, 14-17 October 2003, Cardiff

Developing relationships with underwriters

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Keywords

Underwriters, Communication, Relationships, Pricing, Reserving, Personal Development

Summary

In this paper we explore our belief that developing relationships with underwriters is an important aspect of our work as non-life actuaries. By “developing relationships with” we mean more than “communicating with”. The implication of a successful relationship is that it is a two-way flow of information that both parties feel is beneficial, and wish to enhance for their mutual benefit and the benefit of their employers or clients. We feel that this is an area that has often been neglected in the past and its value underestimated. We look to explore the reasons for developing these relationships, how to go about it and form some opinion of the state of these relationships at present.

Developing relationships with underwriters

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Developing relationships with underwriters

“When the Society was first organized the life actuaries and casualty statisticians engaged in casualty work were almost without exception untrained in any of the practical underwriting features of the business. On the other hand, the company underwriters were in general equally untrained in the statistical methods pursued by the actuary. Hence the frequent clashes between the two groups. But during the past ten years the gap between the actuaries and the underwriters has narrowed materially. The actuaries have learned much from the underwriters and, let us hope the underwriters have learned much from the actuaries. Despite the fact that there are times when the two groups seem as far apart as ever, they are consciously or unconsciously really growing closer together.

In fact just because it is called the Casualty Actuarial Society and because we require proficiency in the principles and applications of that science is no reason why we should not hope for the time to come when membership in our Society will be a stepping stone for promotion in the underwriting as well as the actuarial or statistical department of the company.”

Quote CAS presidential address William Leslie

1 Introduction

Is this your view of underwriters?

An actuary and an underwriter are watching the eleven o'clock news. A story comes on involving a man on a window ledge threatening to jump. The underwriter says, "I'll bet you fifty bucks he doesn't jump." The actuary says, "I'll take that bet." A few minutes later the guy jumps. As the underwriter reaches for his wallet, the actuary says, "Never mind. It's not fair. I saw it on the six o'clock news. The underwriter responds, "So did I, but I just didn't think it would happen twice."

Is this your underwriter's view of you?

An underwriter takes his two actuaries into a restaurant. The waiter asks the underwriter what he would like to eat, and the underwriter says, "I'll have the steak." Then the waiter asks the underwriter, "And for your vegetables?" The underwriter replies, "They'll have the steak too."

Then your relationship is not as it should be!

2 Scope

Every actuary realises communication is a critical tool in today's business environment. Forming relationships with those around you is an essential skill in any career. The most successful operations around the world are identified by the relationships between all the components in its business process. We suggest that for the actuary working in the non-life insurance market, the relationship with the underwriters is of fundamental importance. The link between actuary and underwriter will determine many things:

- For the pricing actuary, a good relationship is obviously important. The underwriter will often make the final decision on terms of the business written and needs to be furnished with the right level of detailed advice to assist in making an informed decision.
- For the reserving actuary, the understanding of the business being reserved will often originate from the underwriter. A good relationship should only increase this level of understanding and lead to more accurate loss estimation.
- For the consulting actuary, the relationship with underwriters will be very important in the success of assignments in any insurance operation, as it is vital to understand the business in order to provide the most appropriate advice.

We also consider how different the relationships are between the underwriter and:

- the in-house versus consulting actuary
- the actuary working in personal lines versus commercial lines
- the actuary working in the London company market versus those at Lloyd's.

The working party is comprised of actuaries who believe there is still some way to go in developing the ultimate relationship with underwriters. We wanted to understand the perception of the current relationship between the two parties from both sides.

In particular we sought to understand:

- the reasons for this relationship;
- the current success points and;
- perhaps most importantly, the current failings.

Indeed we feel an understanding of the failings should potentially lead to future improvements.

One of the key elements of our research in this area was to conduct a questionnaire of both actuaries and underwriters. Many of you will have seen it and responded which is much appreciated. By replying you have contributed to this paper allowing us to incorporate a broader range of views than just our own. The results of the questionnaire are outlined and the areas for improvement explored.

As part of the paper, and in addition to the questionnaire, we have also spoken to some insurance brokers, since they need successful relationships with underwriters to

place insurance business on behalf of their clients. We tried to incorporate their opinions and the methods they use to develop these relationships.

During the working party we have also been able to collect many anecdotes, particularly from those who have seen an ever-increasing role for actuaries in general insurance. Some of these are quoted in the paper.

We hope you find this paper enjoyable and stimulating. It is hoped the paper will be in some ways provocative and stimulate some debate at this year's GIRO. Further, we hope it may prove useful to those readers who at present have limited exposure to underwriters.

3 Why?

Why would actuaries want to develop relationships with underwriters? Does this question depend on the nature of the actuary's work? Is there more or less reason for a consultant to do this than the company actuary? Is it more or less important when one is looking at pricing, reserving or reinsurance? Is there a significant difference in the impact between Personal Lines and Commercial Lines?

Most actuaries in general insurance are employed, as the other staff are, to deliver profits to the owners of the business whether they be the shareholders of their company, the partners in the business, or perhaps the names participating on a Lloyd's syndicate. We believe that developing a successful relationship with underwriters will contribute to them optimising returns to all such stakeholders.

3.1 Understanding the business

Taking the general question first. By the nature of their work actuaries require data from which to work and a good understanding of the business underlying that data. Thus when presented with a task they often focus on the sources to provide that data. The sources can include the Finance Dept who already have it, or the IT department who provide new data extracts, or perhaps the claims department for their data extracts. Having obtained this data they often spend a considerable amount of time "cleaning" this data and reconciling it to other sources in the company to gain confidence in its validity. It is then that the "true" actuarial work takes place in terms of analysing, modelling and projecting using techniques deemed appropriate based on an understanding of the underlying business. Once a conclusion has been reached the results are presented to the person requiring the actuary's assistance.

It is clear from this that there is not necessarily any underwriter involvement in this process and it is our assertion that this is typically the case except perhaps if an underwriter is the recipient.

Items that may distort the analysis can include:

- Large claims; Zero claims definition;
- Change in portfolio mix;
- Change in cash-flow timings;
- Change in reinsurance arrangements;
- Change in policy wording;
- Change in legal interpretation of cover;
- Change in policy conditions, standard deductibles, limits offered.

While it is not always underwriters who are first to be aware of the above, they are likely to be the first in many of these cases and if not then probably the second. By

being the person interfacing with the client, often through a broker, they are in possession of more information than other employees and thus the most efficient point of contact for the actuary interested in any such developments.

3.2 In-house v. Consultants

Consultants, by their nature perform a different role from in-house actuaries. When they are gaining information for particular work projects they tend to interact with finance people and often rely on the accounting personnel to provide the requisite background information. By direct interaction with the underwriter they can ensure that the finance staff are not missing or ignoring key information and get a first hand understanding of the nature of the business being written and changes therein. It is often the case that the consultant is not given the desirable level of access for two reasons. These are that there is a more obvious cost to the organisation in setting up additional meetings between the underwriter(s) and the consulting actuary than in the in-house actuary meeting with underwriting colleagues, and that there is often a perceived risk that the underwriters will disclose information which is considered by other parties to be commercially sensitive. Moreover, underwriters often question the benefit of meeting with external consultants on their own book of business.

3.3 Pricing v Reserving

The pricing element of actuarial work, by its nature, requires interaction with underwriters. But is the requirement to develop a relationship any stronger than for other functions? It is possible to perform this role without a relationship with the actuary providing a support service. However the effectiveness of the actuary's input is likely to be greatly enhanced if they are performing this in tandem with the underwriter rather than in a vacuum. Such a close relationship is clearly beneficial to the reserving actuary to a similar same extent. Actuarial projections are likely to be much more accurate if they reflect changes as they happen rather than having to wait for them to emerge from the triangulations.

3.4 Reinsurance

Reinsurance is perhaps an area where the actuary already is more interested in dealing with the underwriters of the ceding companies than their finance people. It is our perception that actuaries are more involved in the pricing of deals in this sector, and that consequently these assumptions are available to those reserving the business. Thus, this is an area where we would suggest that the practitioners in the industry have already begun to realise the merits of the above arguments, and thus these relationships are already at a more advanced stage of development.

3.5 Personal and Commercial Lines

Personal lines business has been quicker to incorporate statistical methodologies into its management than Commercial business. The more extensive data, with better defined and less numerous rating factors, has been instrumental in this. But has this been an asset or hindrance to the actuary communicating with the underwriters to understand what is going on behind the numbers? The production of a statistically sound conclusion is rendered inappropriate if there has been some underlying shift in the portfolio not yet reflected in the data. We would suggest that a well developed relationship with underwriters, to make the actuary aware of this as early as possible is equally valuable to either business type.

4 How?

How do we develop relationships with underwriters? We now consider how to go about it. A comprehensive answer to this problem that covers all the individual situations is impossible. However, certain general principles will apply to most situations.

Developing relationships with people is something that we do constantly in both our working and private lives. We generally find it much easier to do this with people with whom we have things in common. Relationships are difficult to build in forced or contrived situations and these can lead to dysfunctional actuary-underwriter relationships. Actuarial principles are not the basis of most underwriters' education or thinking, thus it is necessary to respect this in order to foster the environment for a natural and workable relationship to flourish. When the basic relationship is right, words like 'synergy' and 'teamwork' start to mean something. However, it is easy to put the cart before the horse.

Most of us regard ourselves as adequate, if not good communicators and for all of us who have passed the communication paper it could be argued that there is clearly no issue communicating actuarial topics to a non-technical audience! We would suggest this is far from the truth, and suspect that we greatly overestimate how effective our communications with underwriters are. Often rather than admit their failure to understand they will just keep quiet and hope that this will not have a detrimental effect going forward. Or worse still, fail to realise they have not understood. It takes a good relationship to be quite happy to admit not understanding something and request further help to do so. It requires even more insight to realise that something has not been properly understood and resolve this with a different approach from the initiator.

Much of what follows may seem obvious, but this is an area that it is easy to neglect due to other priorities. It takes considerable work to develop a successful relationship but it is very easy to destroy one. Once destroyed effective relationships tend to be difficult to recover.

4.1 Devote time

It takes time to develop relationships and therefore it is necessary to be ruthless with the relationships you think it is worth pursuing. It is easy to think that there is no benefit in spending this time when you feel that it might be better spent building another model, doing the billing or at the cinema watching "About Schmidt." We have dismissed this as being shortsighted, but this still means the time devoted needs to be targeted.

Time spent looking to foster one relationship is time taken away from another. Think strategically about with whom you want to build a long term working relationship and be clear as to why that underwriter, or group of underwriters, is so crucial. Make sure that you choose the relationship that will pay dividends in the future – in terms of business done together, departments run together, or clients served together. Fewer deeper relationships are much more valuable from a business perspective than several more superficial relationships. In fact, the influence of one or two very good relationships will ultimately have much more profound implications for the business you do together over the course of a career.

In practice the time required may well be the time that the actuary is unaccustomed to giving up. Longer lunch hours, after work drinks events or golf days are not the forums in which many actuaries are typically used to working. However, failure to participate in such events will continue to allow the “them and us” view of each other to persist and is a missed opportunity for information gathering. Often people are much more forthcoming with information in such environments than meetings in an office. To get repeat invites to such events requires that the actuary “fits in” with the rest of the group. It is therefore useful to have topics of conversation other than the latest reserving software or the discovery of a new prime number. Sometimes a knowledge of, and opinion on, the weekend’s football results or latest “soap” romance is likely to prolong the period before you are left staring through the bottom of your glass at your shoes!

It is important to plan to spend time developing the relationship in whatever way you consider appropriate. Whether this is: asking the underwriter’s opinion on an issue; going out with them for a drink at lunchtime; or offering some training to the other’s department. The step may be very small or fairly large, depending on the context. Sometimes walls of hostility can be simply overcome from a simple proffering of some time and interest.

On some occasions, usually through a mutual interest, a relationship may develop without real effort. Such a situation should be looked on as a bonus, and so long as no great commitment of time is required to foster it, pursuance of a good relationship in this case is likely to have considerable benefits in mutual understanding.

4.2 Understand Yourself

It is important to understand yourself. Think about how you relate to people in other areas of life and try to work out why certain relationships are good, but others are difficult. What is it about yourself that makes relationships so hard sometimes? Don’t pretend that dealing with all underwriters is going to be easy. Be honest about why it is worth pursuing this relationship. If you honestly think that your relationship with underwriter X is number 115 down the priority list with good reason, then there is no need to worry any further. It really may be that the relationship is not worth pursuing.

Perhaps there are problems with management, which need to be sorted before issues with the underwriting department can be properly addressed. Perhaps it will be necessary to think small rather than big – a little bit more contact at next quarter's book closing, or a spontaneous courtesy call to say that you are looking at a part of the portfolio and would value some underwriting input.

This is not an excuse for failing to develop the relationship. The underwriter may not "be my type", but that is no reason for giving up the relationship. That said, do not pretend to be someone you're not. The aim is for the relationship to be natural and dynamic. That is impossible unless you show the other party something of yourself.

All successful relationships are built on "give and take". It is crucial in developing a relationship to understand where your motivations lie and what boundaries within which you can work. This self-analysis will then allow you to find the middle ground with the issues of the next section.

4.3 Understand the Underwriter

"....One hears a certain amount of complaint about the complications of the rate making procedure and from time immemorial the actuary has been criticized for being too theoretical. As sufferers of long standing we have learned to accept with a degree of equanimity both the complaint and criticism.

But we should be extremely careful to guard against an attitude of indifference, particularly in the matter of the complaint against complexity in rate making. It should be our constant endeavor to make our results readily comprehensible to company executives and underwriters as well as to the supervising officials and the insuring public...".

W Leslie

To develop a successful relationship with an underwriter requires an understanding of how they tend to differ from actuaries, in personality, work environment, training, expertise and personal performance objectives.

Why are underwriters like they are? What is their background? What do they want out of life and out of their career? What makes them tick? Spend some time thinking through what the answers to these questions might be. Be prepared to revamp the answers and possibly revolutionise them, given that they will be initially tainted by your own prejudices. The key is to be able to see things from another point of view.

Underwriters generally come from a wider range of backgrounds than actuaries. This immediately makes further generalisations difficult and emphasises the need to consider the individual. Our comments below tend to focus on work environment considerations that show a greater degree of uniformity.

Underwriters are used to working in a market place. The “best estimate” or “correct price” means nothing to them if they cannot sell it. They are constantly aware that the company cannot make any money if it does not write any business. However they seldom understand the argument that it may lose less money by not writing business. The perceived relationship between the volume of business they write and their job security is highly correlated.

In most cases they are not used to seeing statistical analysis and mathematical models as a key driver in their decision-making. Thus they tend to see it as a threat rather than a complement to what they do.

Underwriting is a profession with a long tradition and actuaries are essentially the “new boys on the block”. It is important to remember that we need to earn their respect and demonstrate we are contributing something extra to the process that will be beneficial to all stakeholders in the long run.

If you can see and understand the pressures the underwriter is subjected to (e.g. Brokers, Management), this will allow you to frame arguments that assist the underwriters in defending their position, particularly if the pressures are, in your opinion, unreasonable. This type of assistance can significantly enhance your relationship with underwriters but beware that the converse applies too and you may need to debate against the underwriter’s chosen stance. However, if they are convinced you understand their position they are likely to be more open to considering your point of view.

4.3.1 Identify a friendly underwriter

It may be advantageous to have first recourse to one particular underwriter for many of the more general questions. This enables you to obtain basic information without bothering a whole string of people. A suitable “target” for this could be a younger, relatively inexperienced, but well-regarded underwriter. Such individuals are likely to have more time and be keen to demonstrate their newly acquired expertise. In addition the input of new ideas from an alternative viewpoint provide them with the opportunity to expand their own knowledge.

4.3.2 Choose the time and place to ask questions

Underwriters typically work in open environments where they are the front line of the company’s interaction with customers. It is therefore not appropriate to ask (potentially stupid) questions to the underwriters in the presence of outsiders such as brokers. This could (or would) reflect badly on the organisation, and unnecessarily delay the transaction of the business between the underwriter and the customer. It is often more appropriate to note the questions at the time and come back to them at a more convenient moment.

Many of the more general questions can best be raised in a social rather than a work environment. In one organisation, that a member of the working party was involved with, after the daily debrief session, the majority of the underwriters repaired to the Red Lion for a pint or two before leaving for home. The discussions in the pub included work as well as football and office gossip! Therefore he made it his policy to accompany them at least on a day or two each week. These sessions were very valuable in extending his understanding of the business and learning more about the social interests of his colleagues. They were also very enjoyable.

4.3.3 Do not be afraid to show your ignorance

Despite the rigorous and extensive nature of the actuarial exams there will be occasions when discussions will arise on a subject where you have little knowledge. It is infinitely preferable to admit you do not understand something than to guess and get it wrong, or to ignore the issue and hope it will go away.

“I recall on day one of my Lloyd’s career, sitting in on a discussion between one of my underwriters and one of his principal brokers. Early in the discussion, there was reference to the business being offered being an excess of loss reinsurance layer “4x1” on a liability portfolio. I was aware of the basics of excess of loss reinsurance and was not stupid enough to imagine that anyone would buy a layer for £4 excess of £1. I was not entirely certain, however, what to make of 4x1, so after the broker had left, I asked my underwriter whether the layer was for £4,000 excess of £1,000. Of course, (as I now know), the layer was really \$4m excess of \$1m. This was just one of my naïve questions in the early days.”

Underwriters will typically welcome the opportunity to demonstrate their knowledge and it is a function of a successful relationship to be uninhibited in both asking for and imparting information.

4.4 Understand the business

Having an understanding of the underwriter’s personal situation and/or outlook is only part of the process. To be able to contribute or obtain valuable information it is necessary to understand the underwriter’s business.

Clearly if you have knowledge of a class of business this will make your dealings with an underwriter much easier since you can show you understand the important issues and will not make stupid errors in your assumptions or models. They will also see you as likely to be far more useful if they do not have to educate you about their account.

If you do not have experience in a business class, be prepared to learn from the underwriters. In general, underwriters are keen to talk about their own business to others who show an interest in the class and who can assist them write (and perhaps

more importantly be seen to write) better business. Your ability to generate a good relationship will be enhanced if you can discuss the nuances of the class of business and offer solutions to common problems the underwriter faces.

Often a greater understanding is achieved if it is possible to spend time with the underwriters at the underwriting box, or equivalent. “I recall a particular incident with a personal accident underwriter at the box when, during discussions with the broker trying to interest him in a particular risk, he passed me the underwriting slip, and asked me what I thought of it. After a brief study of the document, I responded that I could not understand what risk was being covered. He was delighted by this reply, as the risk in question was a kidnap and ransom policy, and every effort was made to ensure that details of coverage were kept very closely under wraps.” This demonstrates how intricacies of particular classes require special consideration. Not much would be gained by studying the underwriting slips for a book of such risks in contrast to most classes.

One of the best ways to gain knowledge is to listen in on underwriting discussions on business being written. A member of the working party was part of an organisation where the syndicate underwriter was more akin to what is now described as an underwriting director. He formulated policy, did virtually no underwriting himself, but was an adviser to those who were writing the business. His particular trademark was that, in the early evening, after the underwriters had returned to the office from the Lloyd’s Box, he would sit in the main office in the midst of the actual class underwriters, who were very young (all under 30 at the time). He would then go over all (or all of the main) risks offered during the day and discuss issues arising. This was a very relaxed session, but played an important role in the development of the underwriting team. Everyone, actuary included, was expected to participate and to listen in on his words of wisdom. It was particularly valuable because the opportunity was there to ask questions. Many underwriting teams or departments hold similar meetings with varying frequency. These are invaluable opportunities to be seen to be a valuable contributor to the team as well as a source of knowledge

4.5 Understand Mutual Objectives

Often the interests of the actuary and underwriter do not appear aligned and this can be a cause of friction. The actuary tends to look at the situation from the view of the company as a whole whereas underwriters tend to be concerned with their particular book of business.

Many underwriters feel that actuarial input into their process is one of corporate governance and that you may be more a hindrance than a help. It is likely that part of your remuneration is linked to company performance and this may be your only ‘proof’ that you are as interested in the underwriting and binding of profitable business.

4.5.1 Interest alignment

What incentive is there for working closely with the underwriters? How closely are their objectives tied with yours? If the linkage between the underwriting and actuarial objectives is strong, there is an incentive to work very closely together. It is in everyone's interest. When the objectives are not so closely aligned there can be tensions if the different objectives clash.

For both it is necessary to find the common ground between underwriting and actuarial work. The ultimate aim is usually the same, to understand the risks and the business well enough for it to be possible to make sound business decisions that end up making profit for the owners of the business.

The problem with this is that the benefits may take a long time to become apparent or may be difficult to identify with regard to the particular account or underwriter. This is an opportunity for actuaries to use their knowledge of items such as reserving and expense allocation to aid underwriters in understanding the implications of these factors in addition to the claims cost.

4.5.2 Define roles

Another element that is important is to make sure both parties' roles in the process are clearly defined. If this is not the case then there is likely to be friction that is counterproductive to good relationships.

It is not critical who has what role as long as it is clear where the responsibilities lie. Typically an underwriter will have final say in a pricing decision whereas reserve recommendation will be an actuary's responsibility. However, there are certainly companies where the opposite is the case.

The key to a successful relationship is working together and sharing all the relevant information. At this stage the actuary and underwriter should discuss their individual views. If there is any material disagreement between them, they should include an investigation of what could have caused this. Subsequent to this, one or other might amend their view to take account of factors that had not been picked up in the original evaluation. Based on the final pair of estimates, it then needs to be clearly defined whose responsibility the final decision is.

4.6 Use Common Language

As with actuaries dealing with non-actuaries there is always the communication issue in respect of actuarial terminology. Underwriters being part of the insurance industry

will have little difficulty with much of this, but it is important to remember they are seldom from mathematical backgrounds.

There is often the converse problem with underwriters that it may be the actuary who does not understand the vocabulary being used. Do not be afraid to ask for explanation of the 'jargon' used. Jargon can be your single worst enemy in that it excludes you from the general discussions within the underwriting function. Not wanting to appear foolish and lacking in knowledge is normal but exclusion is worse and may lead to fundamental errors. However, beware of who you approach to decipher the jargon because often, some of the more senior people may not be able to define correctly and your relationship will suffer if your quest for an answer makes them look foolish.

4.7 Select Location

As with any relationship distance is certainly a barrier to its development. Clearly there are a number of practical obstacles that can be placed in front of the actuary looking to develop underwriting relationships. The importance of these considerations may seem different for the external consultant as opposed to the in-house actuary. However, the points below remain relevant to both, and the consultant often has the choice between working at the client site or their own office.

Location is an area where the desired outcome can usually be achieved if the desire is there to make a particular situation occur.

4.7.1 Geographical separation

How close physically to the underwriters you deal with do you want to be? Across a floor? In the same building? In the same city?

If you are seated nearby then you probably regularly talk and exchange information. If you are in the same building then you probably have some sort of regular contact with the underwriter(s). In this situation you will in all likelihood have experienced that chance meeting in a corridor or lift that leads to vital information being imparted. But what if you are further away? The regular contact is probably limited to the odd phone call or meeting and the chance encounter never happens.

The further away you are, the more difficult it becomes to ensure that the information flow is adequate. Even if the relationship between actuary and underwriter is good, it is hard to maintain the same level of contact if you are in different cities as you can from adjacent desks.

There is no substitute for close physical proximity. This allows you to both gain a chance to appreciate social interests and to get to know the day-to day issues

applicable to the class. It is easy to underestimate the amount of detail that you may overhear that is of direct relevance to your job. Think how far you would be prepared to go to ask a simple but not crucial question. It is easy to shout over to the next desk, somewhat more effort to walk down the office and progressively more so to go to another floor or building. Now consider how far an underwriter will go to find out something minor from an actuary.

The disadvantage is being exposed to distractions and interruptions and here compromise is clearly necessary.

4.7.2 Organisational separation

This may or may not be linked with the previous section. It is common nowadays to have complicated matrix type working structures. Is a pricing actuary a part of the actuarial team or the underwriting department? In all likelihood the answer is both. We would advocate that the best and most rapid way to develop relationships with underwriters is to be part of the underwriting structure. This sense of ownership alleviates some of the “them and us” attitudes that are often present and make it easier to convince the underwriters that you are “on their side”.

Often the best organisational structure is not put in place because the underwriters feel uncomfortable supervising actuaries and/or the actuaries do not have the confidence to be placed in an exposed position away from the security of an actuarial enclave. While there are valid points on both sides the mutual benefit to be gained from each understanding the other’s issues is much more accessible if there is direct and daily exposure.

4.8 Explain Analytical Thought Process

“...History records the many valiant struggles that have taken place between actuarial theory on the one hand and underwriting judgment on the other in the development of rates from limited statistical bases “.

W Leslie

There is often reluctance by underwriters to discuss the standard elements of a premium basis. Our actuarial training teaches us to break down the problem into frequency, severity, expenses, commission, reinsurance costs, investment income and profit loads. An actuary, new to an underwriting team, may find that these items have never been considered or that there are casual ‘rules of thumb’ employed for example: ‘We target an underwriting profit because we cannot include investment income but this is notionally offset by expenses anyway’. You might find that you spend a good deal of time trying to counteract these ‘rules of thumb’. However, the demonstration of the numbers involved on a real life risk can get your underwriting colleagues thinking and acting to address these items. Try to focus on frequency and severity

separately. If an underwriter is prepared to offer terms on a risk, they should be able to tell you

- How many claims they expect on the policy;
- The average approximate value of these claims;
- A general discussion on the spread of these values;
- How much time is required to manage the account; and
- If reinsurance will cover some of the frequency and severity.

It is amazing how many underwriters will not be able to give you these items and one could argue that if this is the case, they should not be binding risks! Here your role may be to help arrive at these statistics (possibly on your own or with the help of assistant underwriters). Once you can define a method or tool, then the ability to debate these 'hard' numbers will place you in a strong position to discuss the pricing basis with underwriters and hence allow you to develop your relationship.

There are some classes of business where these statistics may not make sense and there are many other 'softer' issues at play. Here, your role is to tease out the relativities between new business and existing business. Even with these numbers agreed, there may be other 'client specific' factors that you need to allow for. Try to reduce the debate into how this affects expected or modelled frequency, severity, expenses or all the elements of the pricing basis.

4.9 Be Approachable and Helpful

In the early days, it is often the case that help that can be provided is in relation to general questions of a mathematical/actuarial nature, rather than questions requiring a detailed knowledge of the business. Actuaries can help underwriters whether the question relates to their mortgages or a structured settlement on a liability claim. The subject does not matter as much as the fact as it helps to develop the relationship.

One member of the working party found a useful "in" with a professional indemnity underwriter was being able to explain the funding of pension schemes where they were looking at insuring the liability of the trustees.

Part of being approachable is to demonstrate that you can be persuaded with reasoned argument. Much of the skill involved in actuarial pricing is the ability to place a value on an intangible item of information. When arriving at the assumptions to use in a pricing basis, you will be presented with items of information that may or may not warrant a change to certain assumptions e.g. a new risk management programme is introduced at a client's premises. Do you reduce your frequency/severity assumption? The key here is to ask the underwriter to make a case for the amount by which you should reduce the assumption. Has the introduction in other client's premises led to a

reduction? How long would it take before the reduction would become apparent? If a credible case is advanced, then you need to make a judgement.

If your involvement with the underwriter is new, you are a new resource to them. Since we are all under increasing time pressure any additional resource is valuable. This provides an opportunity for the actuary to add value to the underwriter by doing what may be relatively simple tasks. Helping with a few of these may give a starting point for further interaction which can then be built upon.

Finally beware of the politics!! Underwriting departments see themselves as the profit generating centres of an insurance organisation, by whom and when this profit is generated are always contentious issues. Care is needed not to allow yourself to become a convenient scapegoat when things go wrong.

4.10 Practicalities to Facilitate a Successful Relationship with Underwriters

Here we outline a series of practical points that the actuary might adopt or consider in attempting to develop successful underwriter relationships. In some ways this can be viewed as a summary of this section of the paper. Not all items will be relevant to all situations and as with any such list it will not cover all eventualities.

In many underwriting environments, there may be an impression within the underwriting function that the actuaries with whom the underwriters are 'required' to work are essentially controls of the management and are more interested in stopping the underwriters from writing what they consider to be 'profit generating business'. Usually, this is a feature of underwriting departments where there has been traditionally little or no actuarial involvement. From an actuarial perspective, there are a number of key steps that actuaries would be well advised to follow before attempting to develop the relationship further.

4.10.1 Ensure you believe that you can add value to this market area.

Be confident that you can add something to the company/area/department you are going to work with. Even if you are not intending to spend your entire career in a front line role with underwriters (and more particularly, offering pricing advice to an underwriter) you can add some short-term value to the underwriting process. Often a short-term actuarial role within an underwriting environment can bring about some positive changes and can perhaps introduce good practices to this function.

One member of the working party knows of a situation where terms were offered on a risk that subsequently produced a loss of £275k in excess of the premium received.

Had they been employed three months earlier they would have certainly spotted the under-pricing and saved the company this loss.

4.10.2 Meet the underwriters.

Before accepting either a new appointment or an internal transfer, meet the underwriter(s) with whom you will work. This may sound obvious but there are many instances where underwriting personnel will not necessarily welcome your presence and ultimately you may find that there is little that can be achieved without much upset. For your own well-being, you may be better focusing your efforts elsewhere.

4.10.3 Management support.

Ensure that the management of this area/division are keen to have your involvement. Moreover, ensure that they will back you if and when you conclude that some practices need to be changed. Many actuarial forays into the underwriting room have stumbled in this regard.

4.10.4 Locate yourself in the underwriting team.

Being part of the underwriting team both physically and organisationally makes it much easier to integrate into the team and more quickly assimilate knowledge about the business written, office procedures and personalities.

4.10.5 Be modest

Asking questions about terminology, being open to alternative opinions and understanding the pressures the underwriters are under will make you far less likely to alienate them and provide the opportunity to influence them in the future from a position of mutual respect.

4.10.6 Introduce the analytical thought process.

Work to get underwriters understanding the analytical thought process of the actuary. This includes breaking down a premium into its constituent parts explicitly. Helping them to think about the quantifiable items makes it much easier to have productive discussions about your actuarial input. It is then more likely to generate discussion of the underwriting factors that are not included in the model.

4.10.7 Develop Tools

If you can develop tools (i.e. computer programmes & spreadsheets), make these simple but applicable to the class of business. Underwriters love when they see tools

that apply to their class being developed that can assist in the pricing part of the underwriting process, saving them time and effort.

4.10.8 Look at entire account/book

Try to ensure that you see all the risks being underwritten. Many actuaries say ‘but we tend to be consulted on the bigger risks...’. This is a dangerous practice and should be discouraged if possible. Here actuaries risk being selected against in that the risks brought to them are not the ones that will cause problems. It may be impractical to review all risks quoted and in these cases, there should be some procedure that is followed, perhaps the use of an actuarially developed tool.

4.10.9 Interact over reserving

Be prepared to assist the underwriter with discussions about the reserving. This is an area where underwriters often develop prejudices against actuaries. Here you can act as an interpreter of the implications and limitations of the numbers coming out of a reserving exercise. An example of this might be where an immature account is being reserved using a Bornhuetter-Ferguson method and substantial weight is being given to an initial expected loss ratio. This has short-term implications for the apparent profitability of the account but as experience unwinds over time, the result may change.

4.10.10 Beware of politics

As in any organisation there are political elements at work, with everyone looking to protect their own interest. As with the government, it is very difficult to recover from a failed political campaign. Be aware of the implications of tasks that you may be asked to undertake and consider the uses to which your findings may be put.

5 Successes

The next two sections of the paper look at some examples where the relationship between the actuary and the underwriter has been successful or failed. The object of this being, to draw out some pointers to take these forward. Many will be practical demonstrations of previous points. One thing that becomes clear is that success in a relationship is often not clearly measurable or quantifiable.

5.1 Proprietary

Attempting to assess where the successful relationships between actuaries and underwriters exist will always be difficult due to the proprietary nature of the relationship and the associated success. Many practitioners recount anecdotal stories of having worked alongside co-operative underwriters with whom they have developed a good relationship, which usually led on to some type of commercial success. One problem is that there is often a long period of time before the results of a good working relationship can show up in the final results. Even then, the objectives of a reserving process may obscure the underlying positive effect of the good working relationship.

Often the ingredients that lead to ‘commercial success’ may include the existence of a very healthy relationship between a non-life actuary and an individual underwriter but there may be many other and possibly transient factors that overshadow the cause and effect that leads to the commercial success. These factors can include the insurance cycle, shock losses, changes in personnel, market conditions, short-term management objectives and reserving fluctuations. Consequently, it often takes three to five years before the fruits of a successful actuarial/underwriting relationship are acknowledged. Despite this there are sometimes ‘quick wins’ that can be implemented and yield substantial results.

The following may be good indicators of the existence of the good working relationship

- Low turnover of staff;
- Low frequency of internal staff re-shuffles;
- Innovative product design;
- Participation in industry/professional seminars;
- Broker feedback; and
- Loss avoidance

The last item above is possibly one of the more obvious yardsticks of underwriting success, but is often surprisingly difficult to track down. If an underwriter avoids a loss due to effective underwriting discipline (in conjunction with actuarial advice), the

details (and even the existence) of the loss may never become known to the underwriter because they receive no claims data. It is only on small markets where every loss is known (e.g. satellite) that this feedback can be obtained. Where this can be proven, this is perhaps the most effective management tool to demonstrate the effectiveness of the underwriting procedure including the actuarial/underwriting relationship where this exists.

5.2 Avoiding the Market Pricing approach

One member of the working party's own anecdotal success story centres on the conversion of the underwriting and pricing process from a 'Market Price' approach to the 'Elements of the Premium' approach which is based on the analysis of frequency/severity.

Initially, the underwriter's approach to the pricing of a new/renewal risk was based on the expiring premium. The process involved assessing whether the exposures were changing and what the percentage increase or reduction should be. There were sharp intakes of breath when the actuary suggested that the premium should be the sum of a number of different parts, the main items being the expected loss cost (which would come out of an analysis of the past claims) together with expenses and a specific profit/cost of capital load. This process would see the estimation of the expected number of claims over the prospective policy period and their expected severity. These estimates were open to debate but the other items such as expenses & profit loadings were largely fixed by management. Over a six month period, the new process was accepted and the underwriters became quite adept at submitting their own frequency and severity estimates. From then on, underwriting meetings were spent arriving at agreed frequency and severity estimates. Once agreed, the premium quoted was purely a bi-product of the parameters.

Another interesting aspect of the above was that the skills that underwriters have (in the area of policy wordings, policy forms and inclusions/exclusions) became part of the selection of frequency and severity, particularly in the area of setting deductibles and sub-limits on certain perils.

5.3 Rate monitoring

The area of rate monitoring, assessing the relative movement of prices charged versus risks assumed between renewals, is often an awkward area that falls between a reserving and a pricing/underwriting function. It is however an area where good relations between actuaries and underwriters can assist the reserving, pricing, underwriting and planning processes considerably. In companies where no direct actuarial pricing role exists, this may be one of the main areas of co-operation

between the actuaries and underwriters. It is often part of the work that can benefit actuarial consultants who require initial expected loss ratio for Bornhuetter-Ferguson reserving methods.

The difficulty here is to assess the exposure and policy terms & conditions changes that may have taken place. Considering a single policy, the premium may be the same, the exposure measure may not have changed (e.g. same number of employees) but the deductible increased 15%. Where there is a strong relationship between the actuaries and the underwriters, these types of small differences can be picked up and utilised in the rate monitor review. There is great scope for these details to be missed if either party fails to communicate effectively with each other.

The advantage with this type of exercise is it often an occasion where the actuary is seen as helping the underwriter to establish and quantify the impact of his actions to management. It thus has the benefit of being of clear value to the underwriter to work closely with the actuary.

6 Failings

What are the implications of the relationship between the actuary and the underwriter being poor or non-existent? They can vary from no impact to, in the extreme, severe financial problems for the insurer as discussed in earlier sections.

6.1 Speaking a different language

This is probably one of the more common failings. The training received by actuaries and underwriters is different so it is not surprising that the terminology used can differ. Different companies use their own internal expressions. A good relationship makes it easy to question the actuary or underwriter to gain clarification.

A real life example. The underwriter requires the latest results for a customer to review the profitability of their account to see if the business should still be written. He asks for net premiums. A simple matter you may think but what if the underwriter means net of commission rather than net of reinsurance? It could make the difference between retaining a profitable account or declining to renew it.

6.2 Lack of understanding of the needs of the other party

Does the underwriter understand what you need to do your work? Do you understand what he or she needs? It is in the nature of the ways that insurance companies work that information tends to go through several intermediaries from the provider to the user. Each of these is often looking to simplify their own role and tends to filter the information, often with the intention of helping the recipient. However this requires a detailed understanding of the recipient's requirements. This frequently results in the actuary getting less than complete information and consequently increases the possibilities of failing to take account of a significant factor.

This is a process of education of the underwriters that can only happen if both parties are prepared to spend time doing it and understand the benefit, or possible cost.

6.3 Information is not volunteered

This is closely related to the previous point. If the underwriter obtains information that is important to you, will they contact you straight away, or pass it on at all? Actuaries are frequently confronted with information requiring fundamental changes to their analysis after they have performed it. The underwriter may be planning to quote on a basis that excludes or limits much of the historic claims, or a significant subset of them. An additional cover may have been included in a standard policy a

couple of years ago that could lead to additional claims occurring to those from previous periods.

The actuary needs to be constantly trying to extract this type of information from the underwriter to be able to pre-empt nasty shocks coming through in the results.

6.4 Analysis not understood

Underwriters are not used to interpreting the caveats that are often taken for granted by actuaries. If you give an underwriter a numerical answer they will take that as the answer. They will not usually appreciate whether you believe this is the answer $\pm 50\%$ or $\pm 5\%$. They will just say the actuary said the answer is X. Getting the underwriter to understand the difference between these and make suitable use of them requires a strong relationship. This is an example of the underwriter not being aware of the actuary's analytical thought process.

6.5 Becoming a scapegoat

When involved in the underwriting process the actuary is exposed to the risk of being used as an excuse where things go wrong.

One member of the working party was once consulted on a potential deal where the client had obtained an independent actuarial opinion as to the run-off of its liabilities. The underwriter wanted to price the deal at a lower cost than this suggested. The actuary's view was that the consultants view was optimistic and also pointed out that this deal fell outside the company's underwriting guidelines. In an ad-hoc conversation with a member of the management some time later the actuary was astounded to hear that the deal was still under consideration and had been actuarially reviewed!

This type of misrepresentation can easily occur where there is a lack of understanding of what the actuary is providing to the process and just as importantly what they are not.

6.6 Stay informed of final outcome

Some actuaries recount stories where an adequate premium was quoted for a risk. Some weeks later, an inspection of the policy revealed that during the final negotiations, the broker succeeded in having a profit commission added which altered the adequacy of the terms. The underwriter felt that since a portion of the profit was only returned following good experience, the economics in a loss scenario was unaffected and hence the change need not concern the actuary!

7 Survey

To investigate the perception of both underwriters and actuaries about the current state of these relationships we conducted a survey. This took the form of a questionnaire set up in an excel spreadsheet. It was distributed electronically to the GIRO mailing list and to underwriting contacts at Lloyds and within insurance companies for onward distribution to underwriters.

The overall response was disappointing in terms of the number of completed surveys returned. This may well have been a result, at least in part, of technical difficulties with the Institute e-mail system during the distribution period.

7.1 Questionnaire

The questionnaire comprised four sections:

- Background Information to allow us to group the responses by type of company, actuary or underwriter and area of involvement;
- Assessing the Current Relationship where questions were designed to measure the degree of interaction at present and the perception of the strengths and weaknesses in the current situation;
- Developing the Relationship asked questions to try and identify where it was felt the relationship could be improved;
- The fourth section was a chance to provide any anecdotes and a bottle of champagne was awarded for the most interesting.

Questions were answered by a series of drop down boxes with typically a range of six answers. This should have enabled easy completion in less than ten minutes.

Responses were sent to the Institute and collated from there by the working party.

7.2 Results

The results that we have obtained need to be considered in light of the relatively small numbers involved. A brief overview is included here with more detailed analysis to be drawn out for presentation at GIRO 2003.

7.2.1 Respondees

Interestingly three quarters of the actuarial responses came from in-house actuaries as opposed to consultants. We suspect this reflects the perceived relevance to the respective streams, a thought process we have challenged above.

Of the underwriter responses, over half were from those dealing with personal lines. This was quite surprising given the distribution was expected to be dominated by London Market underwriters.

7.2.2 Current position

Over half the actuarial responses claimed daily underwriter interaction, whereas only one underwriter indicated this frequency of involvement indicating a mismatch of the two populations responding. Both groups indicated that face-to-face contact predominates which makes the mismatch even more surprising.

Overall the rating of the relationship from both sides was “good”. The underwriters particularly rate the actuaries technical ability and were most questioning of how useful/relevant the actuaries experience is. The actuaries recognised the underwriters understanding of the market but are less sure of their technical ability.

Both sides regard the relationships as important yet the actuarial side are considerably more interested in working to develop them.

7.2.3 Barriers to development

The main barrier to the relationship improving from both sides is lack of time. Apart from this the underwriters see few barriers except possibly infrequent involvement, perhaps reflecting their greater exposure to a wider range of personalities in their normal environment. Actuaries see more problems; differing priorities; educational backgrounds; lack of common interests; language and underwriter attitude all “sometimes” a barrier. “My own attitude” is rarely a barrier - although one actuary (and one underwriter) put that their own attitude is always a barrier!

7.2.4 Questionnaire summary

In general there were no major unexpected results from the survey. From the underwriter side it would be interesting to know whether those who felt we needed to work on this were the ones that replied, or those who do not see a problem. Both views have been expressed. The indication from the actuarial responses is that they are predominantly from those with heavy underwriter involvement and a generally positive outlook. Thus the breadth of responses was not as widespread as hoped for. Having said this it is encouraging from both sides that there were very few negative comments suggesting that those involved to date have made a positive impact.

8 Conclusion

“...On the other hand, the actuary who has come in contact with the practical side of the business and who has been graced with what we call "horse sense", will know where to draw the line between theory and practice. The practical actuary and the logically minded underwriter should have no trouble getting along together but the theoretical actuary and the illogically minded underwriter had better keep away from each other.”
W Leslie CAS Presidential Address 1924

Many of the comments made in the exerts from William Leslie’s CAS Presidential Address ring true today. That these points are still issues today raises the question as to how much things have progressed in the last eighty years? We would suggest that although most actuaries acknowledge the need to develop relationships with underwriters and recognise the difficulties involved when it comes to devoting the time and energy required other priorities often intervene.

It is clear there has been progress just from the number of actuaries now involved in General Insurance in the UK. This is to some extent driven by the more statistical approach adopted in the US and the globalisation of insurance. It is also clear that the more mathematically rated classes such as Motor have been more accommodating than the more traditional markets such as Marine.

It is also generally recognised that younger underwriters are more receptive to actuarial involvement than their older counterparts. We suspect that, besides a natural factor of youth, this reflects the more professionally educated nature of modern underwriters with greater emphasis on qualifications such as the CII.

There are gradual changes in the insurance market environment that make life easier for actuaries looking to develop relationships with underwriters. But as with any relationship it comes down to the individual. If you are looking to develop relationships with underwriters you need to recognise it is likely to require a different skill set and consider whether you have what is required. Since the time involved is likely to be significant it is also important to have this available.

As with all roles the importance to you of relationships with underwriters is a function of your responsibilities. Therefore be selective in using the advice contained in this paper. But we would encourage you, if you get the chance, to get to know your underwriter. You never know, you might enjoy it!

