

AM Best's Request for Comment Response: Best's Performance Assessment for Delegated Underwriting Authority Enterprises

In March 2021, AM Best introduced its initial draft of *Best's Performance Assessment for Delegated Underwriting Authority Enterprises* (PA for DUAEs). The revision process for this draft methodology extended throughout 2021 and entailed one request for comment (RFC) period, which began on March 15, 2021 and ended on May 3, 2021.

The methodology has been finalized and was released for use on February 1, 2022.

Feedback received during the period was considered and, if appropriate, resulted in some alterations to the original draft. Changes made to the *PA for DUAEs* methodology from the initial version published in March include the following:

- Clarified how AM Best reviews cases when it is appropriate to perform the analysis on a legal entity level or on a group level. Added a section outlining the process for assigning a “g” assessment affiliation code for the analysis of DUAEs that collectively operate as a coordinated group.
- Added a section describing AM Best’s analysis of DUAЕ ownership structures.
- Clarified that AM Best understands that underwriting data will vary depending on the business model. Clarified AM Best’s expectations of documentation for contract reviews.
- Under the Underwriting Capabilities component, added Commission Structure and Claims Management elements and moved the Participation in Profit Sharing element from the Financial Condition component to the Underwriting Capabilities component.
- Language added to the Technology in the Underwriting Process element to describe the process of investing in outside technology partnerships.
- Under the Governance and Internal Controls component, added language to the Alignment of Interests and the Binding Contracts elements.
- Under the Financial Condition component, changed the element Analysis of Financial Metrics to Analysis of Financial Results and Metrics and provided additional details for this element. Added Financial Strength and Impact of Related Parties as an element of this component to describe AM Best’s approach to considering the impact of the financial strength of affiliated parties on the DUAЕ’s.
- Under the Organizational Talent component, added language to the Organizational Structure element to describe potential staffing differences and AM Best’s approach to assessing a DUAЕ’s needs for certain staff members, and potential challenges for business continuity if these needs are not met.
- Where applicable, all exhibits were updated to reflect revised language in each sub-assessment.

AM Best greatly appreciates all of the responses received during the public consultation period. AM Best did not respond individually to comments received during the RFC but is publishing the 24 comments it did receive on the *PA for DUAEs* methodology. For respondents who chose to remain anonymous, best efforts have been made to shield the identity of both author and company by

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redacting any text that could be used to identify the commenter. Common themes and, when possible, questions and comments on specific topics have been grouped into general responses.

Industry engagement enabled AM Best to identify areas in the methodology in need of further revision or clarification; AM Best believes that the revisions made promote greater transparency. The changes made to the *PA for DUAEs* methodology between the initial draft release and the final version are addressed in the following FAQs. These changes resulted from both public feedback and internal review.

Please note that AM Best has also made minor editorial revisions to the final *Best's PA for DUAEs* methodology. These changes added clarity or addressed additional stylistic or grammatical issues.

Please note, any questions regarding costs or fees should be directed to [AM Best's Business Development Team](#).

FAQs

Process

How frequently is this assessment assigned and re-evaluated?

A PA can be assigned at any time upon a DUAЕ's request. Once a PA is assigned, the company will be subject to ongoing monitoring and formal annual reviews in accordance with AM Best's surveillance procedures. Any material change in the company's operations or operating environment may trigger an interim review and referral to an Assessment Committee for deliberation.

What is the time commitment expected of DUAEs requesting a PA?

The time required for the review will be commensurate with and appropriate for the complexity of the organization undergoing the assessment. To ensure the credibility of the PA, AM Best expects a certain level of disclosure from all DUAEs and engagement with the PA's senior management to assess the five components.

Does a DUAЕ request a PA or would a carrier request a PA for a DUAЕ?

The DUAЕ will request the PA, and the contractual agreement will be between the DUAЕ and AM Best. For further information on engagement, please speak directly with [AM Best's Business Development Team](#).

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Are PAs offered globally or are they only available in the United States?

PAs are offered globally. The assignment of a PA for a DUAЕ uses a global methodology applied in the markets that AM Best's offices service worldwide.

How will AM Best assess what is appropriate for a certain line of business or territory?

AM Best will use internally developed analytical tools and peer reviews by product and territory in its PA analysis to ensure consistency and transparency. Over time, AM Best expects to publish benchmarks for DUAЕs.

Will AM Best select DUAЕs, or will they volunteer for the review? What is the timeline to full coverage of the market?

The Performance Assessment is an interactive process. Any DUAЕ can approach AM Best to request a PA on a voluntary basis. There is no timeline set for full market coverage. AM Best expects that coverage will grow steadily over time, particularly in those markets where DUAЕs are very active.

How will AM Best address underwriting performance and IBNR/reserving when this can vary from insurer to insurer and portfolio by portfolio?

As part of the interactive assessment process, AM Best will seek to understand the appropriateness of reserves and the premium pricing adopted by the company since they can vary by company and product. An understanding of the reasonableness of reserving is important as the reserving approach may ultimately influence the underlying profitability (and commissions) of an insurer's portfolio, particularly for longer tail classes of business.

What plans do you have to engage with insurers/reinsurers on their views of assigning a PA to a DUAЕ and if they would use this in their selection criteria for incepting a new contract or renewing a contract with a DUAЕ?

AM Best gathered feedback from a variety of companies across markets, such as (re)insurance carriers, associations, managing general agents (MGAs), brokers, consultants, and regulators. Based on the feedback received, insurance carriers view the PA as useful information, but AM Best does not expect it to replace the existing due diligence performed by insurance carriers.

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Will AM Best be performing its own independent actuarial analysis of the historical and projected profitability of each of the DUAЕ's programs?

No. Although we are not committing to undertake actuarial investigations at any particular level of detail or frequency, AM Best will formulate its own opinion on the DUAЕ's Underwriting Capabilities through a review of historical performance and anticipated performance based on the DUAЕ's business plan, its ability to meet those plans and market conditions. AM Best will evaluate the performance of the portfolio subject to the materiality of the products, programs, and markets in which the DUAЕ operates, and how the performance of the book of business links to the alignment of interest with its business partners. Performance will be viewed on a legal entity basis, unless there is merit for a consolidated view of multiple DUAЕs. Consideration will be given to information provided by the company, third-party reviews, and other relevant information, such as reserving, claims management, commission structures, and other specific features of the programs (appetite, limits etc.).

Has this process been discussed with regulators?

Yes. As appropriate, AM Best apprises the applicable regulators on developments as it regards *PA*s for DUAЕs.

How does AM Best plan to approach contract analysis?

AM Best will evaluate the core product lines and the markets in which the company operates, and how the structure of these programs work in relation to its business partners. AM Best may request sample contracts from different segments and/or markets to understand any important differences between contract terminologies. AM Best's plan for approaching contract analysis does not include a review of every single contract into which the DUAЕ has entered.

DUAЕ and Carrier Relationships

What impact will the PA for DUAЕs have on the rating of an insurance carrier?

AM Best does not expect that the PA for a DUAЕ will impact the rating of an insurance carrier, as any materially relevant information on DUAЕs is already factored into the insurance carrier's issuer credit rating (please refer to [Best's Credit Rating Methodology](#)).

Will carriers be interviewed as part of the PA process?

Carriers will not be interviewed as part of the PA process. AM Best expects that there will be interaction with the DUAЕ's senior management; it does not expect that there will be interaction

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with other associated parties. Where appropriate, AM Best uses third-party audits, contract details and other information to formulate a more accurate assessment on the DUAE.

Will the PA add transparency to carrier ratings?

The expectation is that the PA will add transparency to the market and support a well- functioning insurance sector. However, insurance credit ratings and PAs measure different things. The Issuer Credit Rating (ICR) assigned to insurance carriers is an independent opinion of an entity's ability to meet its ongoing financial obligations. A PA for a DUAE is an independent non-credit opinion of the DUAE's ability to service its business partners.

Privacy and Confidentiality

Can a DUAE choose to have a private PA?

Yes. The company has the option to either make the PA public or private or not continue with the process. The PA will remain private and treated as confidential until the DUAE requests that it be disclosed publicly.

If a DUAE chooses a public assessment, what kind of information will be made publicly available?

Upon completion of the assessment, AM Best will publish a press release and an accompanying PA report. A press release will summarize the five components that were used in the analysis to arrive at the PA attained by the DUAE. A PA report will include the PA, an outlook for the PA and an explanation of the five components and relevant elements. Any public PA and its accompanying report will generally be updated annually, which will be in addition to AM Best's ongoing surveillance to ensure that the PA is current. The report may also provide some general background information on the DUAE and/or its respective group. In the event that a DUAE decides to withdraw a public PA, AM Best will provide a final public PA on the DUAE before the PA is withdrawn.

How will AM Best address confidentiality?

AM Best is a regulated credit rating agency. In accordance with regulatory requirements, AM Best maintains and enforces policies, procedures, and controls to protect confidential information from fraud, theft, misuse, or inadvertent disclosure. These policies, in part, state AM Best and all employees shall use confidential information only for purposes related to AM Best's business activities (any other use is strictly prohibited); and, actively protect and safeguard all confidential information from disclosure to any third parties, unless disclosure is required by applicable law or regulation.

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In order for the PA analysis to be thorough and rigorous, there is an expectation that DUAEs will provide sufficient information, which may include confidential information, so that an appropriate PA analysis can be conducted.

Structure and Strategy

How will AM Best view DUAEs that are part of a group?

AM Best expects that most DUAEs will be assessed on a legal entity basis, and where there is a group with multiple legal entities, we expect that the assessment will be performed on each entity individually. However, there may be instances where there are significant commonalities and/or strategic approaches which may have us take a group view for the assessment and when that is the case, the methodology has been updated for assigning a “g”, signifying group, affiliation code.

When you look at diversification, will you also look at whether the business mix is long-, short-, or medium-tail, and how the business mix affects the sub-assessments assigned to each component if this is a factor?

Yes. We will consider the mix of business generated by the DUAЕ. The mix of business will not directly influence the sub-assessments assigned to each component, but rather, will inform our opinion on the DUAЕ's expertise in the line of business.

How will AM Best approach the complexity of General Agency Agreements?

AM Best acknowledges that General Agency Agreements are complex. As described in the Underwriting Capabilities component, AM Best does not expect to review each individual agreement; however, we expect to review a sampling of contracts across different segments and/or markets to understand any important differences among them. Our review will include an analysis of profit commission clauses, management of multi-year contracts, and full or partial delegation of underwriting authority.

How will AM Best avoid penalizing smaller DUAEs since they will not have the same access to resources as larger DUAEs?

AM Best recognizes that DUAEs can vary substantially within and across markets and will not penalize smaller DUAEs in the PA analysis. The DUAЕ will be assessed on its merits, with due consideration given to the size and complexity of its operations. AM Best has vast experience rating insurance companies that vary in size and complexity.

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How would AM Best assess a seasoned underwriter that has previous experience with an established insurance industry participant and begins employment with a start-up DUAЕ?

AM Best takes into account the experience of management in its assessment. For start-ups, AM Best reviews the experience and qualifications of key management personnel. AM Best approaches new DUAЕ company formations by assessing its ability to bring (through its distribution network) quality business to the DUAЕ and a good understanding of the strength of business partners used, not just the strength of the underwriting team or track record. Further details, in terms of achievability and the robustness of its business plans, such as signed contracts/agreements, solid commitments of distribution partners and such, will also be important to the PA. However, uncertainties and opportunities are typically part of a start-up's circumstances, and AM Best expects to appropriately reflect such uncertainties and opportunities in its PAs.

How will the number and variety of products be considered in the assessment?

A review of products offered by the DUAЕ will be conducted to understand the structure and performance of these products, and the benefit these products provide to the DUAЕ and its business partners under the Depth and Breadth of Relationships sub-assessment. AM Best will conduct a review of the profitability and commission structure of the products on a gross and net basis. Benchmarking and peer reviews may also be conducted on a DUAЕ, market, product, or even a program basis.

Underwriting Capabilities

How will AM Best view the variety of underwriting strategies available across DUAЕs?

AM Best acknowledges that there will be variability among DUAЕs. Various underwriting strategies present an opportunity for differentiation and demonstrate the value of an independent PA. Underwriting Capabilities is a crucial component of the PA and is one of three components that carries twice the weight (up to 10 points) of other components in the analysis. Underwriting will play an important part in the stability and longevity of the DUAЕ model, and the DUAЕ must work effectively in conjunction with its business partners.

Will AM Best consider commissions in the PA?

Yes. Since the initial draft of the methodology, AM Best added Commission Structure to the Underwriting Capabilities component to explicitly reflect the consideration of the compensation structure that the DUAЕs have in place, and whether such structures enforce greater diligence in underwriting activities. Commission and fees will also be viewed in the context of the DUAЕ's business partners and alignment of interests. As such, the compensation structure for the DUAЕ

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employees and associated parties is important to the PA and is captured mainly in the Underwriting Capabilities sub-assessment.

How will AM Best view programs in run-off?

Issues pertaining to run-off portfolios that have implications for the DUAЕ with regard to reserves, commission payments, and other factors are considered in the Underwriting Capabilities component. Normally, contracts are structured so that responsibilities relating to run-off portfolios are clearly defined. If this is relevant to the PA, AM Best will seek to understand the mechanisms in place to manage portfolio run-offs.

How would AM Best assess variations in claims handling?

Where appropriate, claims management services will be reviewed to understand any positive or negative impact on underwriting performance as any item that is relevant to a DUAЕ's ability to service its business partners and that could affect one of the five components will need to be considered. This includes variations in claims handling. Recognizing the importance of this aspect in the assessment, Claims Management has been added to the Underwriting Capabilities component of the methodology.

Will AM Best consider diversification of income stream via different products?

Yes. Consideration is given for diversification by product and geography. Whether diversification brings stability and enhanced earnings to the operation will be assessed based on historical performance, expectations for future performance, the current operating environment, and the competitive landscape. AM Best will also consider, where relevant, the segmentation of a DUAЕ's business under which its partners would normally participate. The aim will be to appreciate the variability of a DUAЕ's performance and, consequently, the performance of its business partners.

Will AM Best provide additional information about the sub-assessment assigned to the Underwriting Capabilities component considering the complexities across DUAЕs?

Yes, the PA report will explain in detail the relevant sub-assessments that most impacted all five components of the PA, with the intent of providing greater insight to the reader.

How will AM Best handle specific loss data that may vary across programs?

AM Best will consider inconsistencies of specific loss data across programs by analyzing the effectiveness of underwriting, where the authority sits in the structure, and if this approach works well. The aim of the Underwriting Capabilities component is to understand the alignment of interests between the DUAЕ and its business partners and whether the adopted structure works in harmony with partners.

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Financial Condition

Will AM Best review reinsurance agreements given that they could have an impact on the overall financial condition of the DUAЕ?

AM Best will review reinsurance agreements as appropriate. The business model that the DUAЕ adopts is important to the PA. Aspects of Underwriting Capabilities, Governance and Internal Controls and Financial Condition should point to mechanisms that DUAЕs have in place to manage risk and support business partners. Any material risks, exposures, or concerns will need to be discussed case by case with the DUAЕ. Gross results will be a focus of the analysis to assess Underwriting Capabilities.

Organizational Talent

Will IT talent be considered in the assessment?

Yes. There is an expectation that IT systems are in place to ensure that risks are managed appropriately. This may be addressed in the Governance and Internal Controls component, but there should also be some consideration in the Organizational Talent component as it regards a DUAЕ's ability to attract and retain appropriate IT personnel. Additional detail was added to the methodology to accommodate this concept.