

Contract Certainty

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Contract Certainty Definitions

- **London Market**

- “Contract certainty is achieved by the complete and final agreement of all terms (including signed lines) between the insured and insurers before inception.”
(from Contract Certainty Code of Practice)

- **US Market**

- May be referred to by different names and defined differently by different brokers/other parties. But generally involves a broker’s proprietary initiative to ensure that full reinsurance contracts are agreed by the effective date of the reinsurance coverage.

Contract Certainty Timeline

	1970s	1980s	1990s	2006
Negotiation	Negotiation is generally based on slips that contain key terms and provisions only, leaving rest of terms and conditions "TBA"		Slips are increasingly detailed and often attach clause wordings	Negotiation is increasingly conducted on the basis of draft contract wordings
Finalization	"TBAs" negotiated later, and formal contracts signed months or years later – in some cases, not at all		By mid 1990s, contracts are to be signed within 9 months of inception due NAIC 9 Month Rule	Increasing expectation that all contractual terms and conditions will be agreed on or before contract inception
Market Participants	Increasing number of participants entering (for example, growth of captive insurance companies) and exiting (for example, insolvencies, companies in run-off, etc.) the insurance/reinsurance business.			
Technology	Typewriters, some Word Processors	Centralized Word Processors	Desktop Word Processing/Document Editing	Electronic transmission of documents

Why Change Now?

- Backlogs of unsigned contracts (including renewals of unsigned contracts)
- Insurance and reinsurance disputes have increased
- Increase in the number of participants entering/exiting the business (i.e., fewer long term relationships between parties)
 - The stakes are larger than ever
 - Threat of regulatory intervention

Recent Key Developments

- World Trade Center litigation
 - Calls attention to what are seen as the insurance industry's questionable business practices
- Spitzer investigations in the US
 - More unfavorable attention for the industry
- Sarbanes Oxley
 - Need to provide fully signed contracts when auditor or insurance regulator requests are received
- FSA chief executive John Tiner's December 2004 speech calling for end of "deal now, detail later"
 - Sets 2-year deadline for London market to achieve contract certainty or face regulatory intervention

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Pros and Cons of Contract Certainty

- **PROS**

- Underwriters know what they're pricing
- Buyers know what they've purchased
- No 9 Month Rule concerns
- Agreement reached while all parties still at their respective companies
- Agreement reached before actual disputes arise
- Voluntary solution precludes regulatory action
- Standardization of wordings

Pros and Cons of Contract Certainty

- **CONS**

- Common renewal date
- Limited staff resources
- Company structures separating Contracts and underwriters/brokers
- Late submissions
- Changes after the inception date
- Standardization of wordings

Where are We Now?

- London Market's Market Reform Group has issued:
 - Contract Certainty Code of Practice
 - Contract Certainty Checklist
 - Additional guidelines on measurement, signed lines and binding authorities
- Thus far, London market data shows it exceeded its own targets for achieving improvements in contract certainty at the end of 2005.
- To satisfy FSA, minimum 60% of placements by 6/30/2006, and 85% of placements by 12/31/2006, should achieve Contract Certainty

Where are We Now?

- US Market

- Nine Month Rule, but no further regulatory intervention to date
- Reinsurance intermediaries are adopting contract certainty/contract at placement initiatives
- Slips are still seen, but draft contracts are seen more than slips
- Process is evolving

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- **Implications Going Forward**

- Resources – Do we have enough knowledgeable contracts people?
- Process – “Front-loading” of terms and conditions negotiations
- Platforms – New technologies and software
- Wording Standardization?

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- **Questions?**

