

# Captive Webinar: The Efficiency and Profitability of Captives

Moderator: Richard Cutcher, Editor, Captive Review

Panelists:

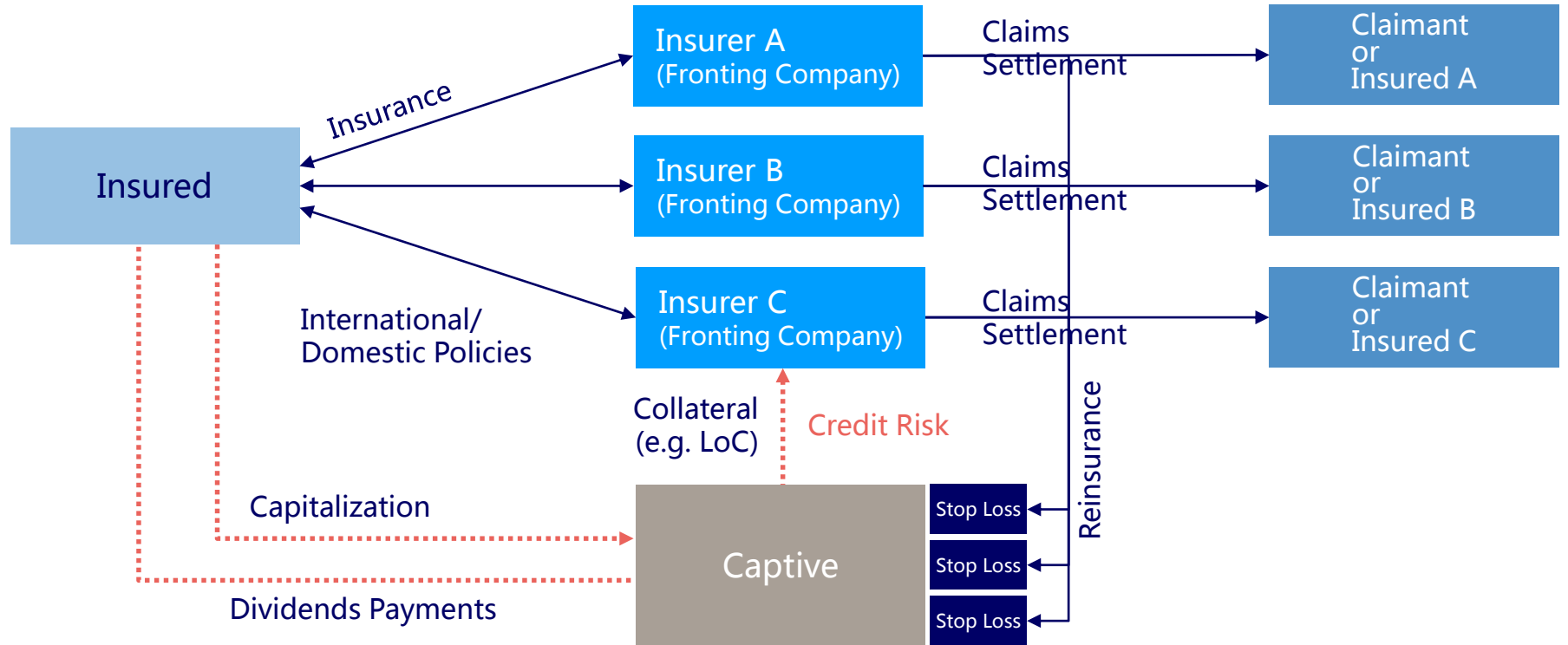
Paul Woehrmann, Head of Captive Services, Zurich Insurance Company

Todd Cunningham, Head of Strategic Risk Solutions, Zurich Financial Services

Paul Wagner, Vice President for Alternative Risk Techniques, AGL Resources

# Captive integrated structure

## Single parent reinsurance captive

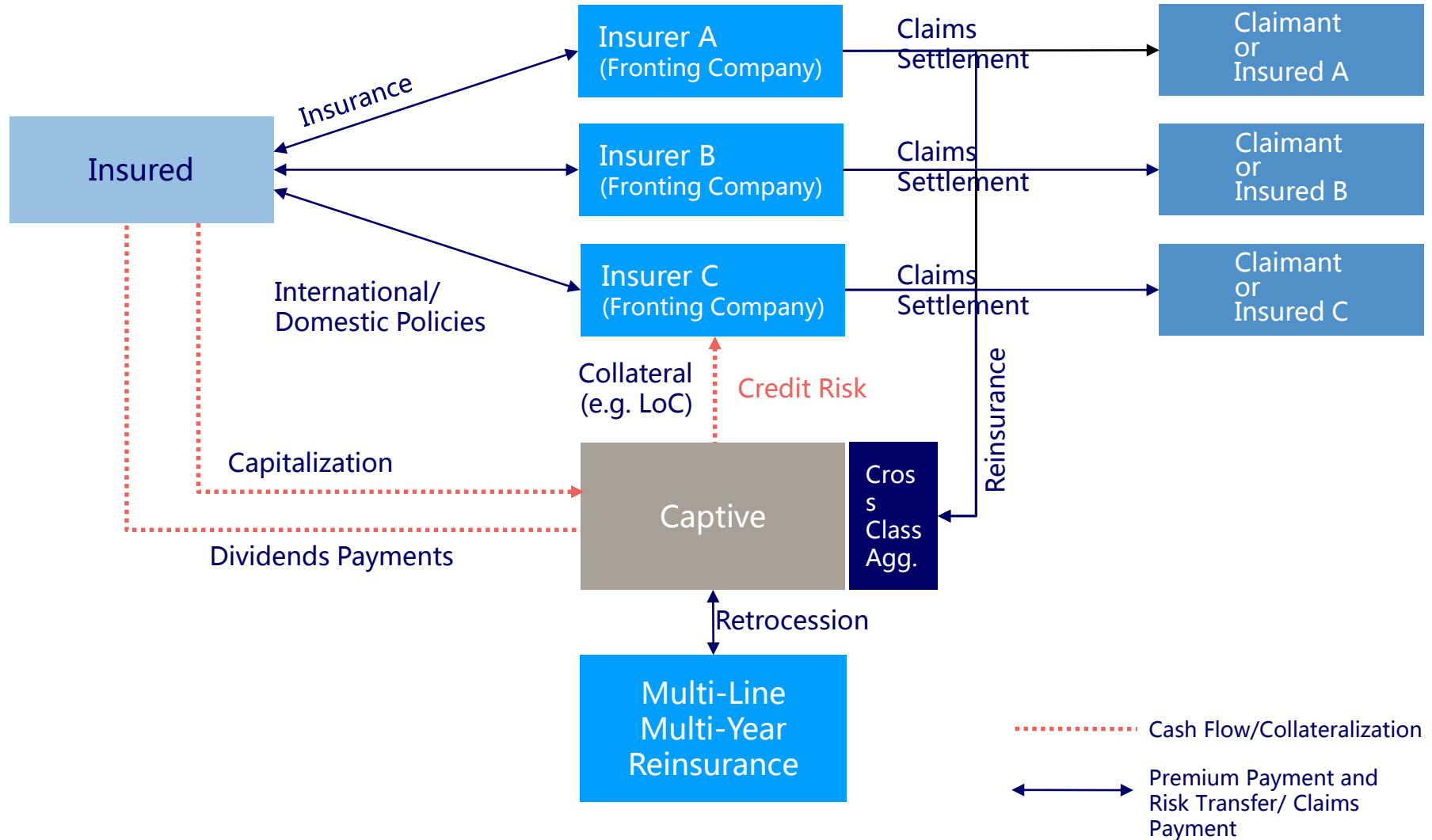


..... Cash Flow/Collateralization

↔ Premium Payment and Risk Transfer/ Claims Payment

# Captive integrated structure

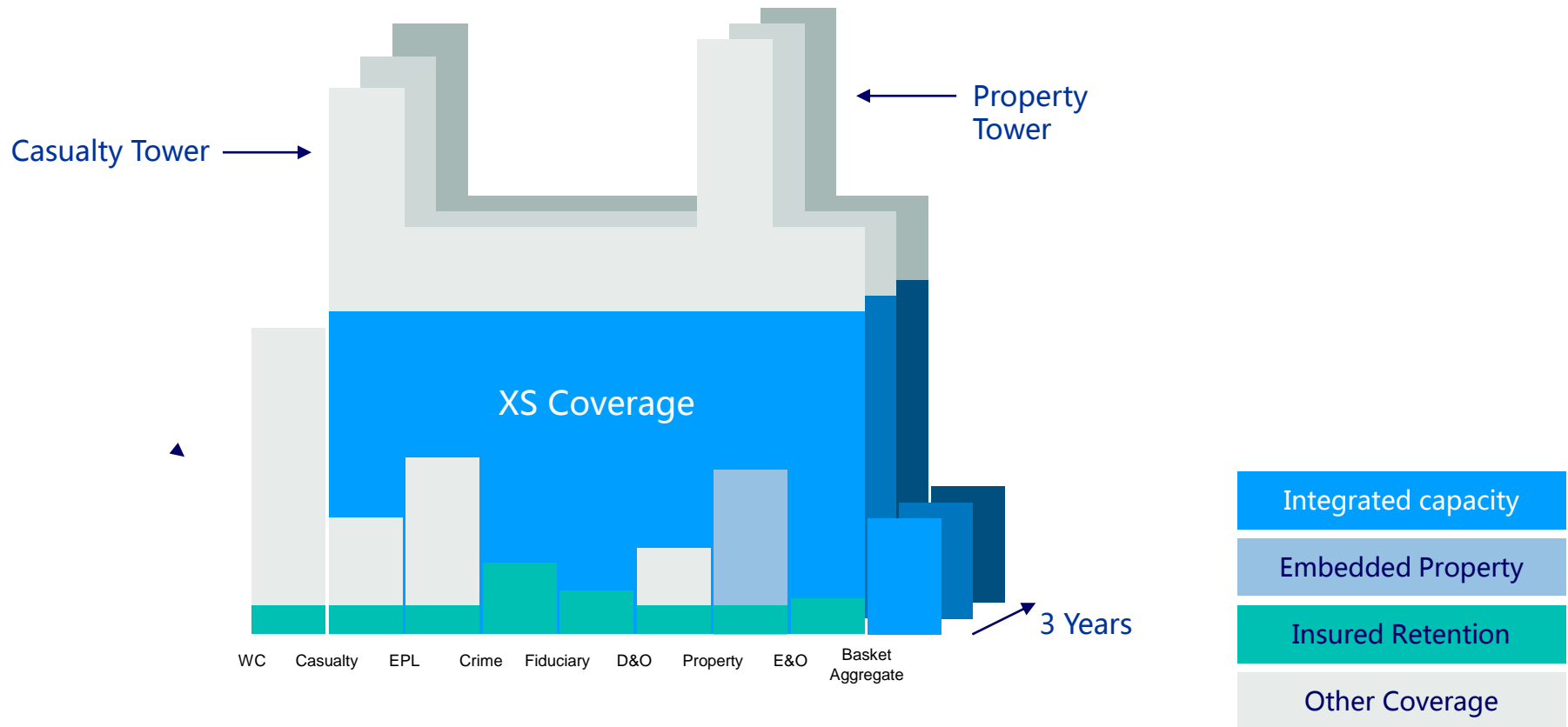
## Single parent reinsurance captive



# Integrated solutions

## Overview

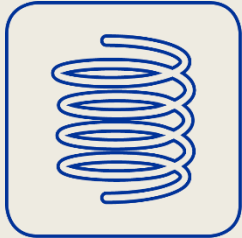
Multi-year programs that allow our customers to spread a single block of coverage across multiple lines of business



# Integrated solutions

## Value proposition

### Why would customers be interested?



Flexibility



Innovation



Reduced volatility



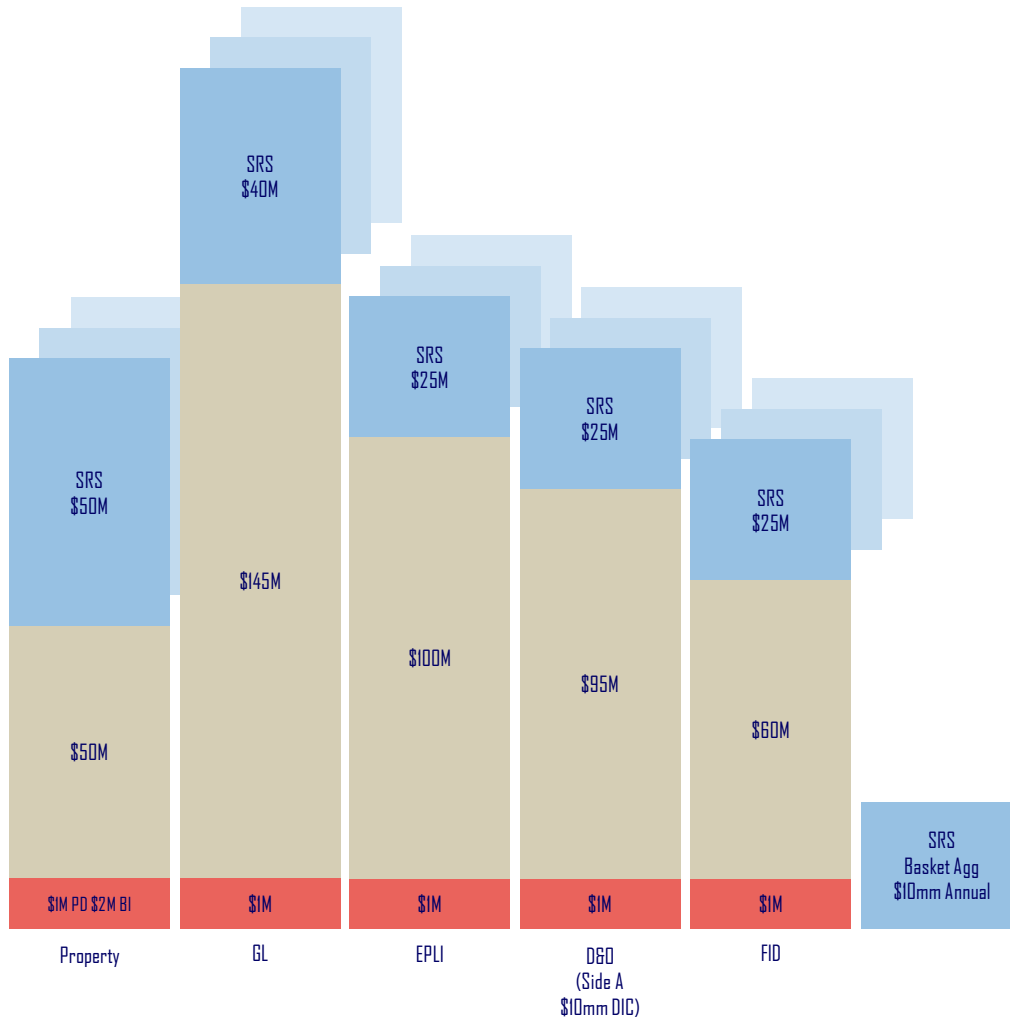
Increased stability

### How do integrated programs deliver?

- Multi-year/Multi-line policies
- More efficient use of insurance capacity
- Catastrophic limits spread across multiple lines
- Coverage for a myriad of exposures in a single solution
- Creates a strategic risk financing platform for capital management
- Basket aggregate coverage provides protection across retentions
- Administrative efficiency
- Optimization of retentions
- Single or reduced Insurer relationships
- Knowledge, people and products to address tough risk management challenges

# Integrated example: 'Super Umbrella' (with basket aggregate)

Limit: \$50mm/\$100mm/\$100mm

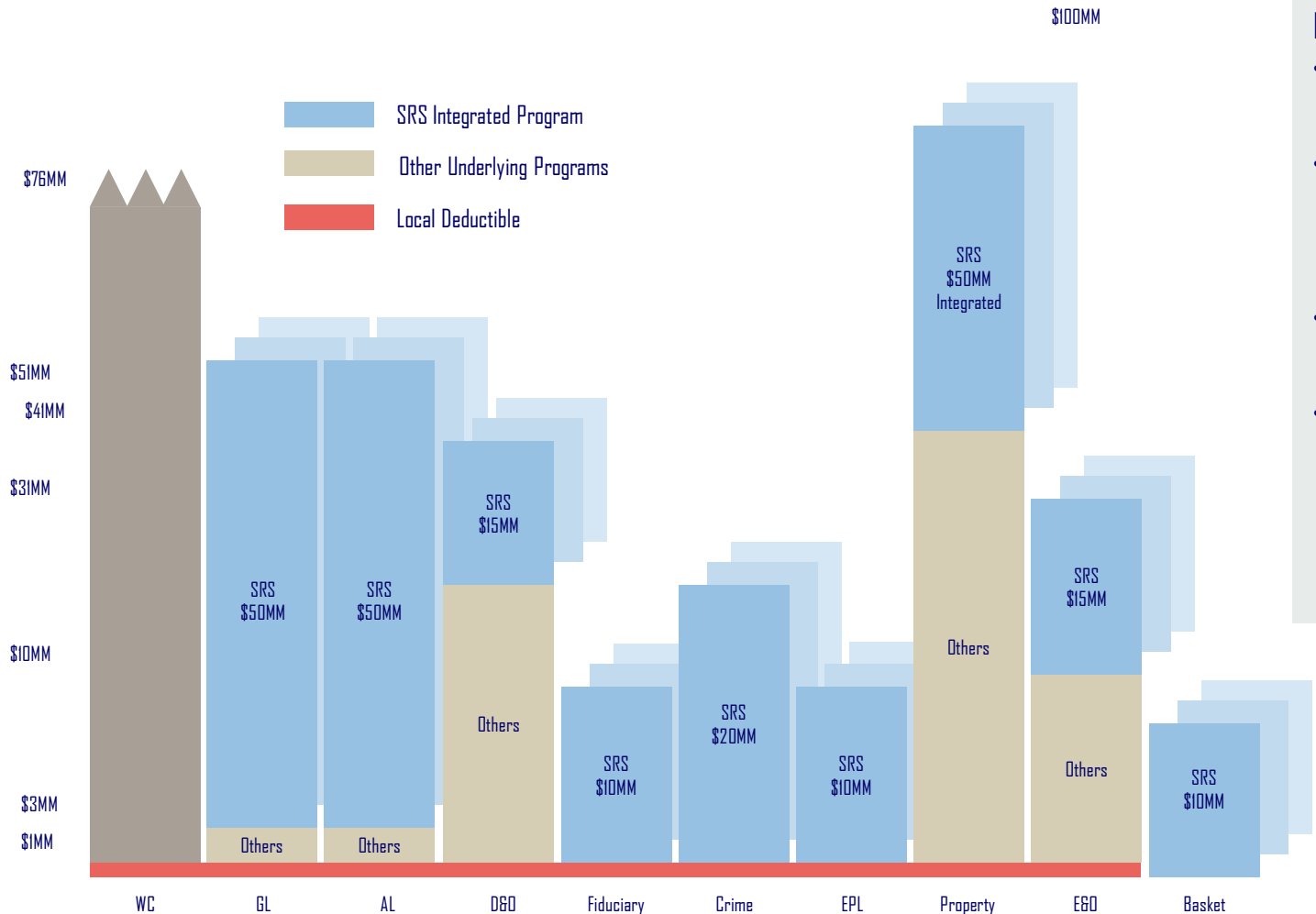


## Benefits

- Significant administrative efficiencies as SRS reduced  
15 renewal submissions/ policies down to 1.
- Allowed client to concentrate to focus carrier relationships down to a handful.
- Stop loss provided 'sleep at night' coverage to Treasurer and provided him/her with ability to know when to 'stop writing a check' for losses.
- Fixed multi-year term provided budget stability/certainty.

# Integrated example: various attachment points

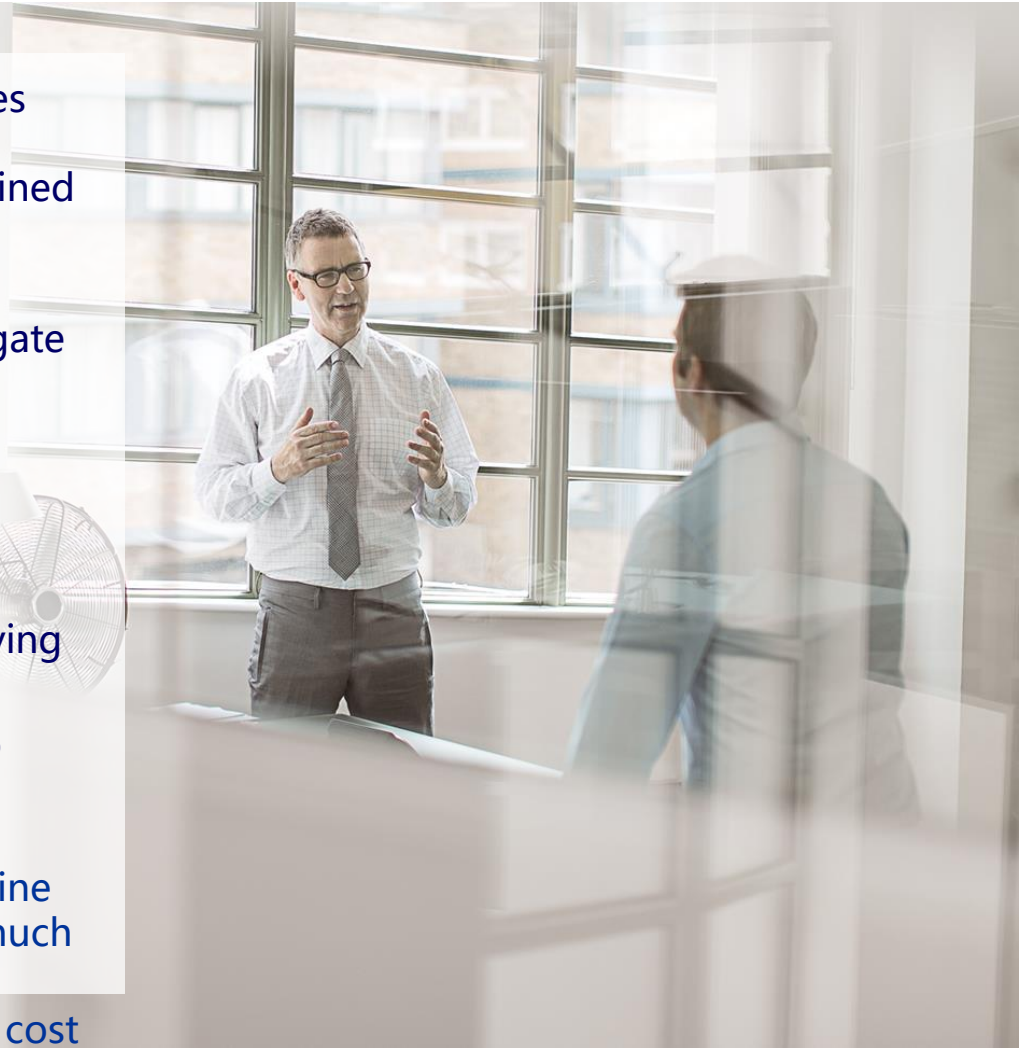
Limit: \$50m/\$100m/\$150m



- ### Benefits
- Significant administrative efficiencies as SRS reduced 21 renewal submissions/ policies down to 1.
  - Client key driver was lead umbrella. Providing \$50m in capacity on a multi-year basis for the lead, allowed for leveraging to incorporate other lines into the program.
  - Integrated coverage allowed SRS to incorporate additional \$15m of EGO capacity.
  - Fixed multi-year term provided budget stability/certainty.

# Basket aggregate

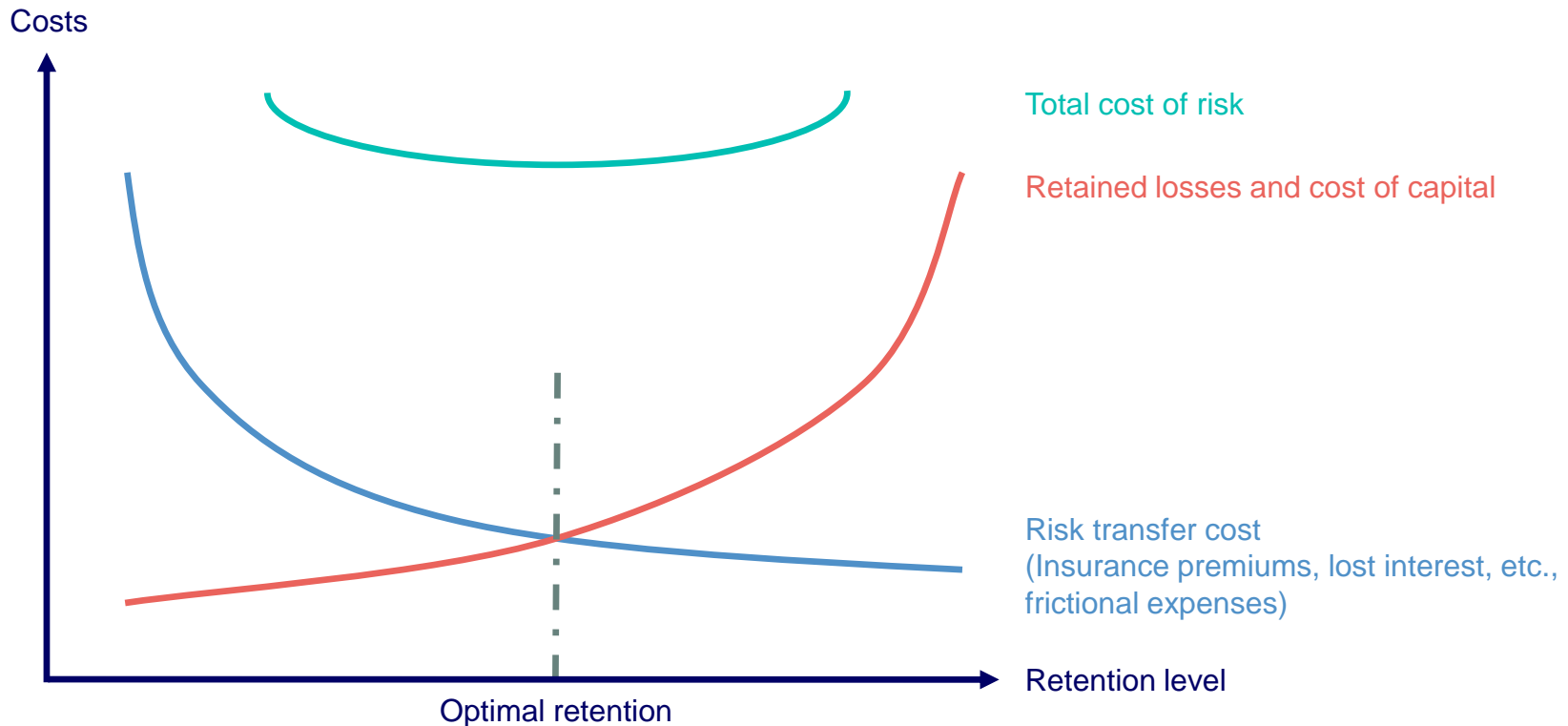
- A basket aggregate coverage provides protection excess of aggregate attachment for SIR/Deductible combined for multiple LoBs
- If the combined losses within the retentions exceeds the basket aggregate attachment, then Zurich pays the difference
- Other names – Aggregate Stop Loss, Multi-line Stop Loss, Cross Class Aggregate, Second Event Coverage
- Drop down provision is similar to having an aggregate stop loss
- The basket aggregate can be used to **optimize** insurance retentions:
  - With a basket aggregate in place customers can safely increase per line deductibles without creating too much risk
  - Premium savings and a lower total cost of risk





# Risk financing as an important part of corporate finance

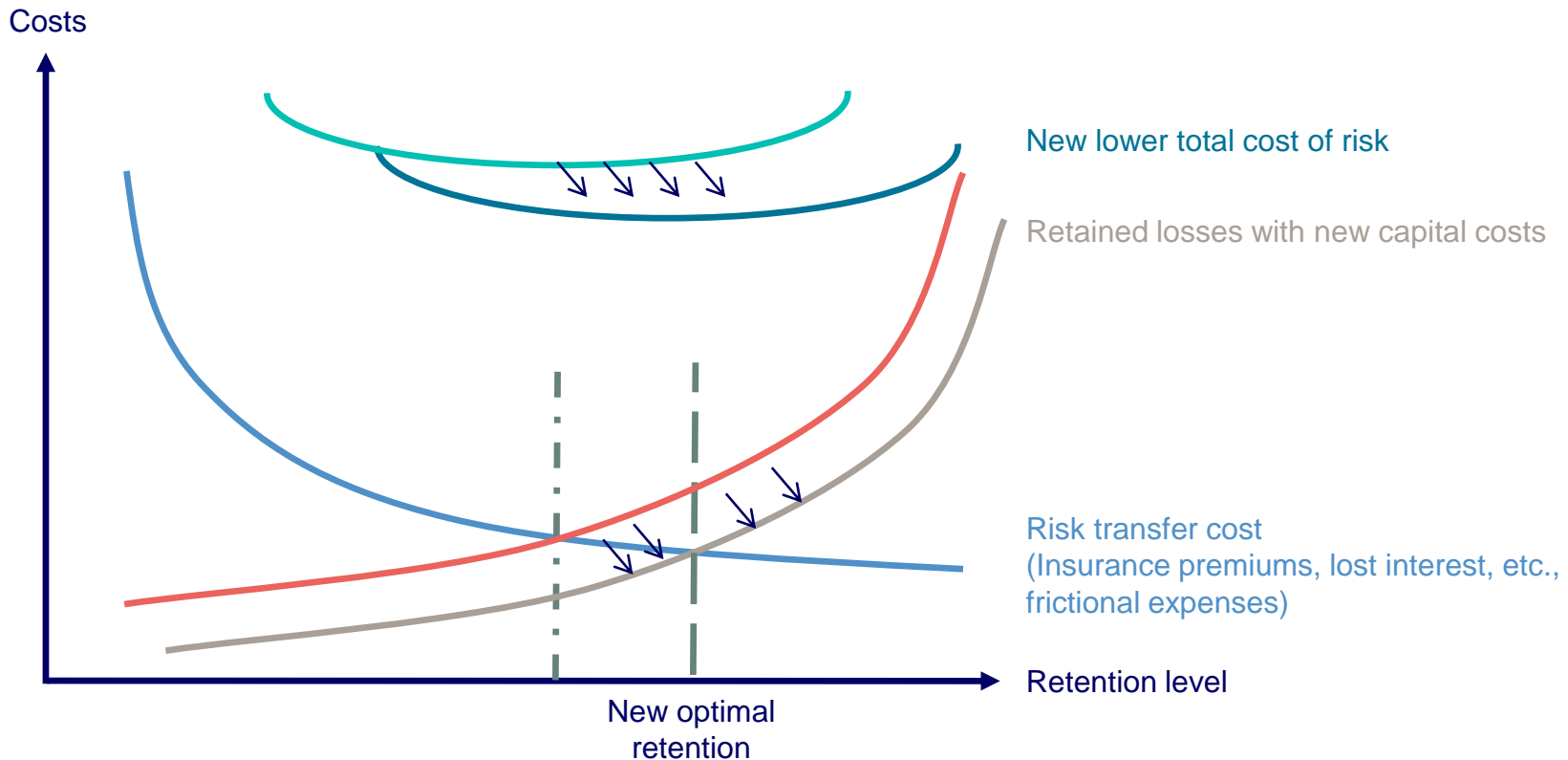
## Evaluation of the optimal retention level...



...in order to efficiently allocate the company's rare capital to the most adequate risk carriers and to minimize the total cost of risk

# A basket aggregate can lower your capital needs improving trade-offs

Retaining more losses, cutting frictional costs, but lower capital usage...



...with protection against total losses not just large losses less capital is needed lowering capital costs



Just like a basket aggregate, but in the context of a captive can be even more valuable

- Can safely increase company retentions ceded to the captive.
- Can make a captive more efficient from a capital perspective: less need to hold excess capital and potentially reserves with sufficient protection.
- For captives with a credit rating, reinsurance may help enhance the credit rating.



When combined with a dual trigger programs (presented later) it supports the captive to retain and consolidate non-traditional risk

- Supports the risk manager in larger Enterprise Risk Management solutions.

# Structured programs

## Design elements

Programs are **highly** tailored to address specific customer needs and may have:

- Customized limits, retentions, and coverage
- Flexible premium payments
- Multi-year policy terms with guaranteed rates
- Blend of risk retention, financing, and transfer
- Provisions for profit sharing
- Incorporation of capital market instruments (e.g. dual trigger policies)
- Customized claims administration and risk engineering services.



# Structured programs

## Three main categories



### Loss sensitive programs – outside of primary casualty

- A blend of risk financing and risk transfer for excess casualty, property and specialty lines, often in combination
- Can act as a 'virtual captive' for customers who want to retain risk but where financing a captive does not make sense
- Limited fronting capabilities for specialized risks as well
- Certificates of insurance may be issued in many



### Dual trigger – incorporating a blending of traditional and non-traditional risks

- Often a part of a basket/ captive aggregate program



### Research and development programs

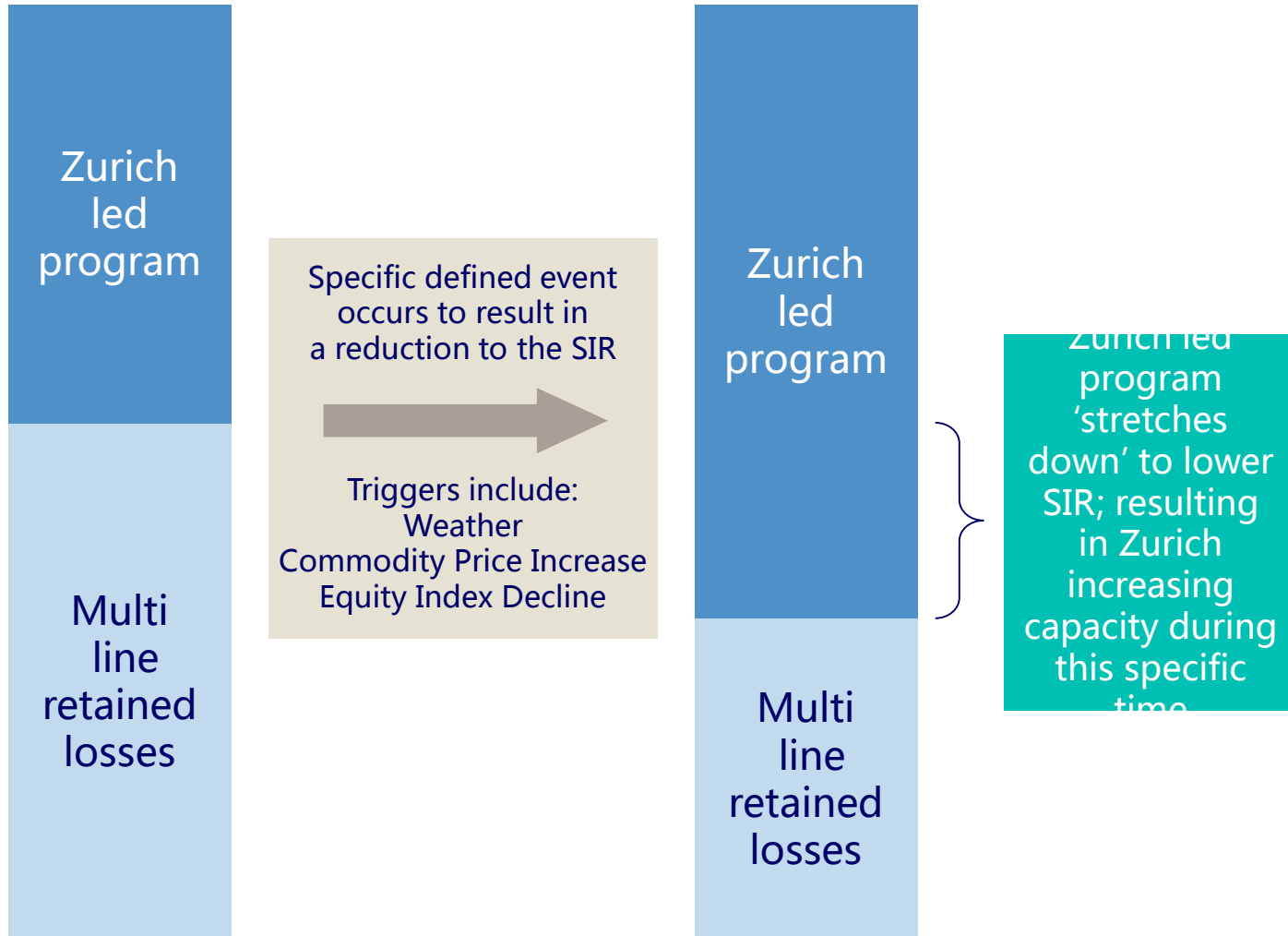
- For unique and highly specialized risk transfer needs when it can be successfully underwritten



## Common features

- Multi year programs and premium financing to diversify losses over a longer period.
- Experience account balances to fund losses, to track profit sharing and as a source of funding future risk management plans.
- Commutation clauses for termination.
- Swing plans for premiums – better experience means lower premium.
- No claims bonuses.
- Aggregate deductibles and limits to optimize risk sharing.

# Dual trigger illustration



*In this case study, we'll explore how to cost effectively implement and build an ERM template including:*

- **WHY A CAPTIVE?**
  
- **WHY MULTI-LINE**
  
- **WHY MULTI-YEAR**
  
- **WHY A CAPTIVE & ERM?**



**The Right  
Combo**



- **Strategic Partners**
- **Multi-Line Multi-Year Program**
- **Captive Domicile**



**2001**  
**ALTERNATIVE RISK  
TECHNIQUES**

**2001**  
**CAPTIVE**

**2002**  
**ZURICH  
MULTI-LINE  
MULTI-YEAR**

**Collaborate**

**Achieve  
ERM**

- ***Risk Management***
- ***Finance***
- ***Human Resources***



AGL Resources is the largest natural gas-only distribution company in the United States. Its business segments consist of:

- Distribution Operations
- Retail Operations
- Wholesale Services
- Mid-Stream Operations

AGL Resources has safely served customers with efficient, reliable natural gas for more than 150 years. The largest segment, Distribution operations, operates 7 utilities serving residential, commercial and industrial customers in 7 states:

Georgia  
Virginia  
Florida

Illinois  
New Jersey  
Tennessee  
Maryland



### Quick Facts

**Headquarters:** Atlanta

**Employees:** ~ 5,000

**Utility Customers Served:**  
nearly 4.5 million

**Retail Customers Served:**  
1.1 million

**Ticker Symbols:** GAS (NYSE)

**Newspaper Listing:** AGL Res



**Power  
of  
Captives**

# **GLOBAL ENERGY RESOURCE INSURANCE CORPORATION (GERIC)**



**Power  
of  
Captives**

# GERIC OVERVIEW



## STRUCTURE

- Single Parent
- Domicile
- AGL Resources Inc.
- Hawaii

## PREMIUMS

Direct Write	—————>	\$14.4 Million
Reinsurance	—————>	<u>\$ 6.0 Million</u>
Total Premium	—————>	\$20.4 Million
Cede	—————>	<u>\$10.1 Million</u>
Net Premium	—————>	\$10.3 Million

## STRATEGIES

- Risk Financing
- Multi-line, Multi-year limits
- Aggregate Basket
- Enterprise Solutions



# Coverage Types

## Casualty

General Liability

Pollution

Auto

Workers' Comp

## Property

All Risks/Inc Wind/Quake

Boiler & Machinery

Crime

## Executive Risk

D&O

Fiduciary

EPL

## Other

Trade Credit

Weather

Cyber

## 3rd Party

Employee Benefits

Extended Warranty

Wrap-Up Construction

Surety Risk



# WHY A CAPTIVE?

## 3 Power Drivers

- I. Direct Access to Reinsurance
- II. Optimize Risk/Capital
- III. Optimize Premium/Retention

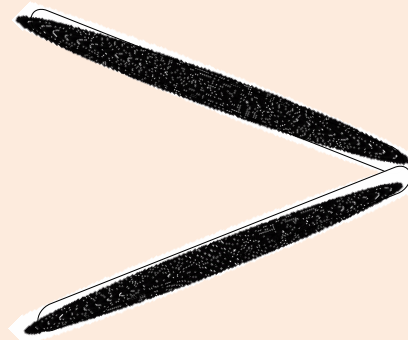




# WHY I



Direct

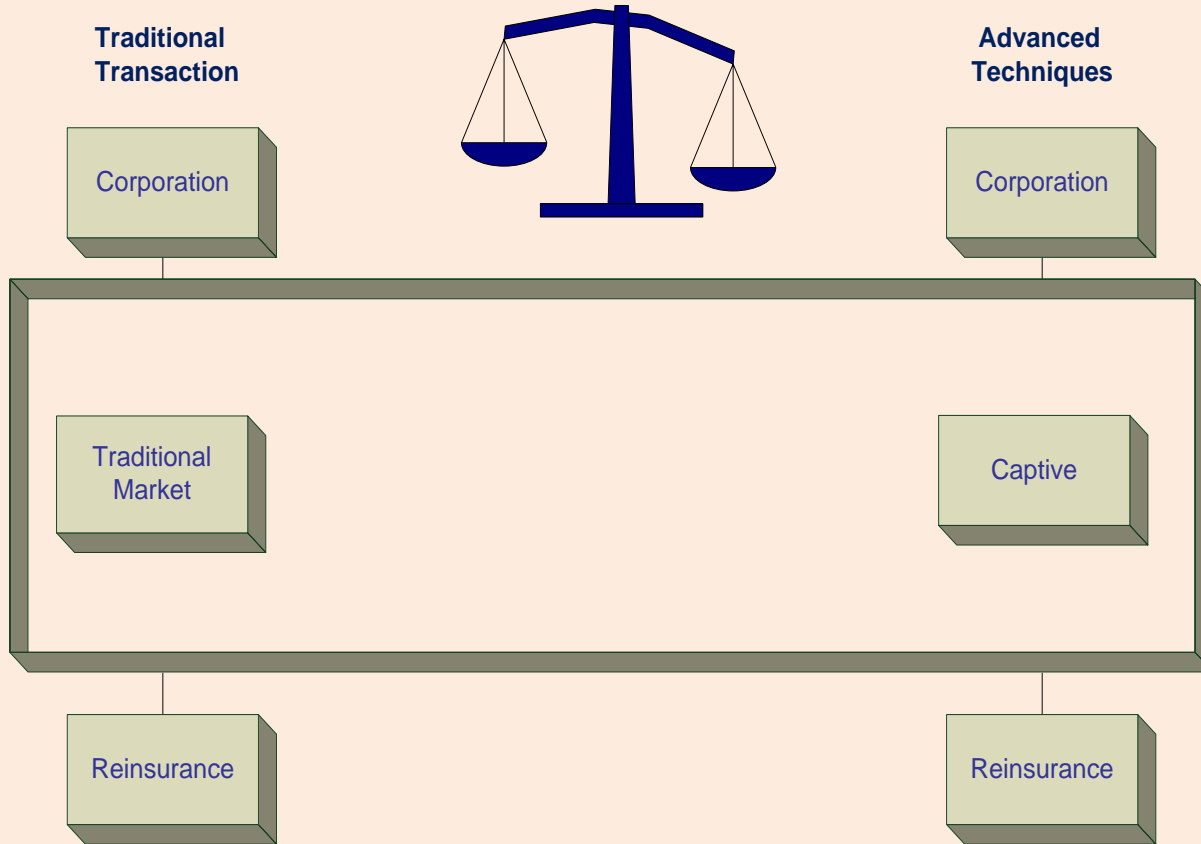


Reinsurance

Access



# WHY

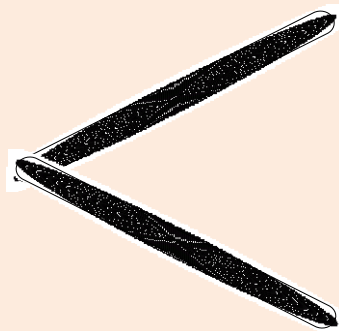




# WHY II



OPTIMIZE

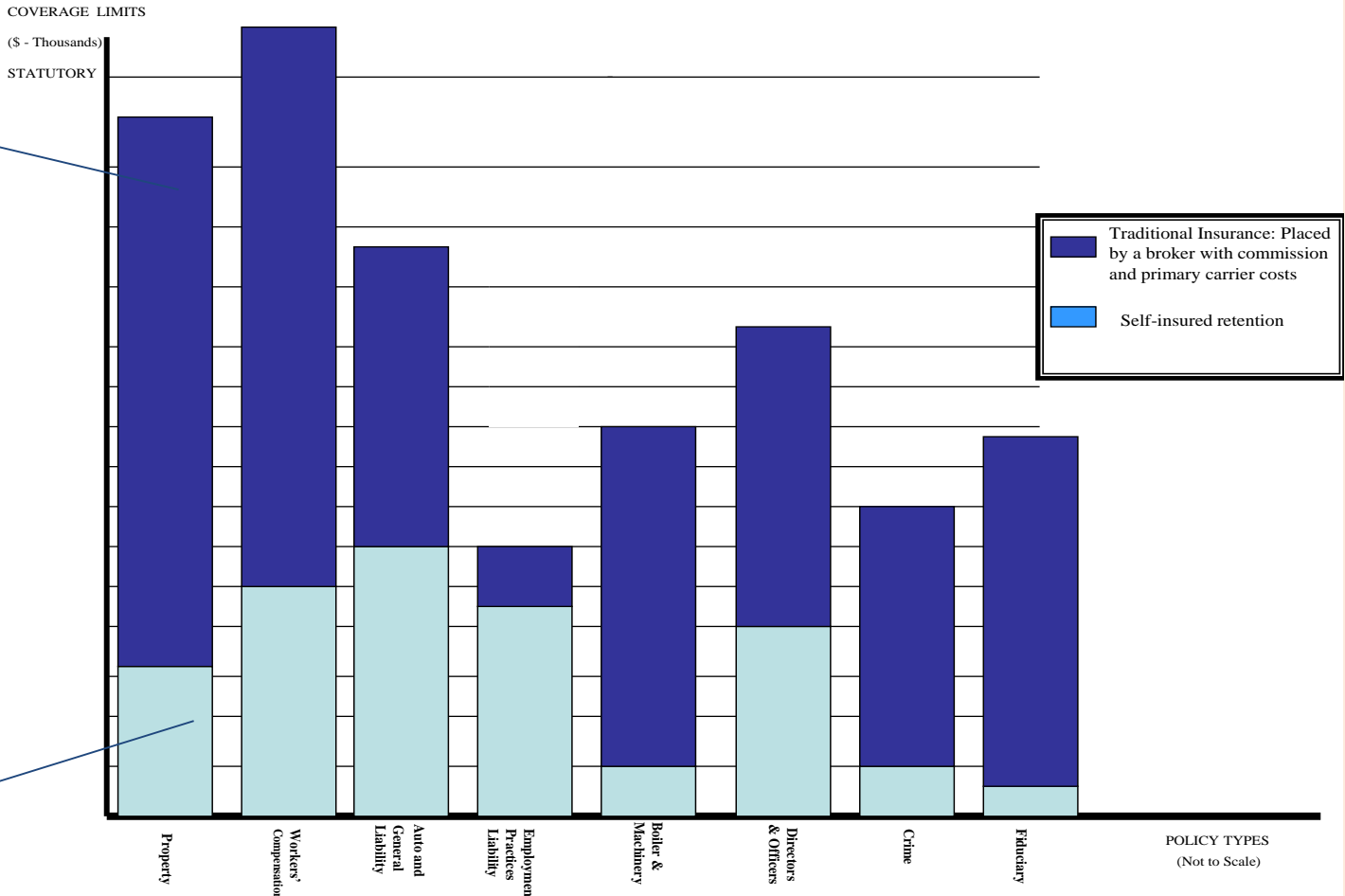


CAPITAL  
&  
RISK

# Insurance Program Pre-Captive



In a typical Traditional Market, each line of coverage has a separate large limit.



Each silo represents one line of coverage.

# CAPITAL OPTIMIZATION

## Traditional Market



<u>Silo</u>	<u>Limits in Million</u>
Property	\$400
Boiler Machinery	\$250
General Liability/Auto	\$500
Employment Practice Liability	\$125
Directors' Officers	\$165
Crime	\$ 10
Fiduciary	<u>\$ 90</u>
<b>Total Annual</b>	<b>\$1540</b>

## Captive Multiline

<b>Total Annual Blended</b>	<b>\$900</b>
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# CAPITAL OPTIMIZATION



## Traditional Market

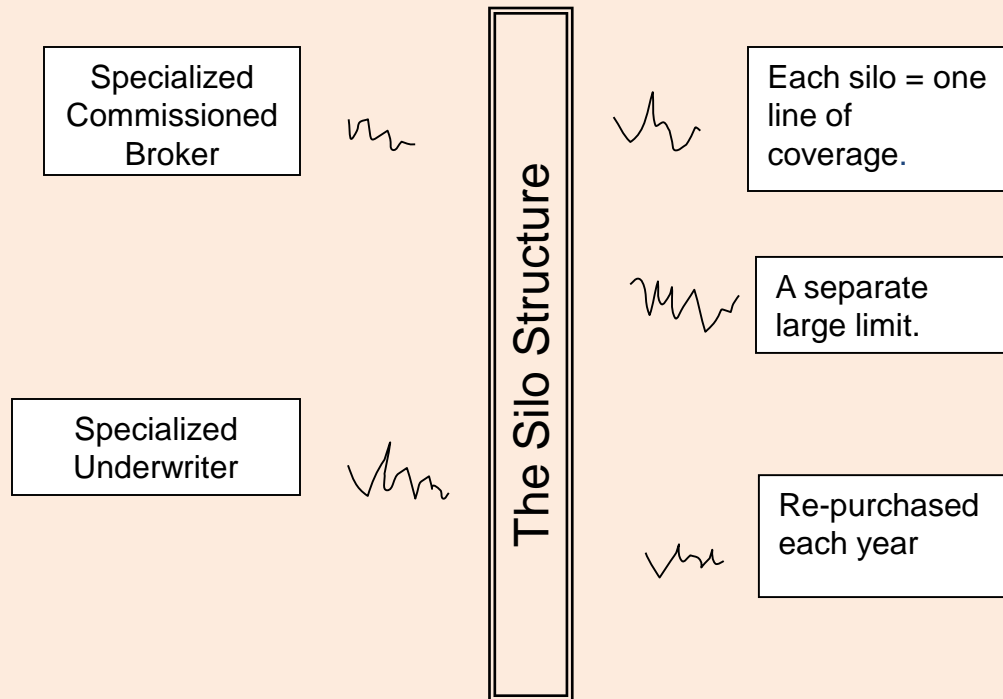
Annual Limits	1.540B
	<u>      x3</u>
	4.620B

## Captive Multi-Year

Limits	.900B
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# Traditional Market

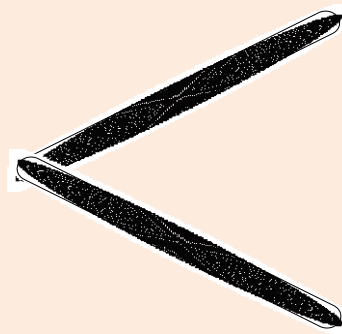
## Friction Costs





◆ **WHY** ◆  
III

OPTIMIZE

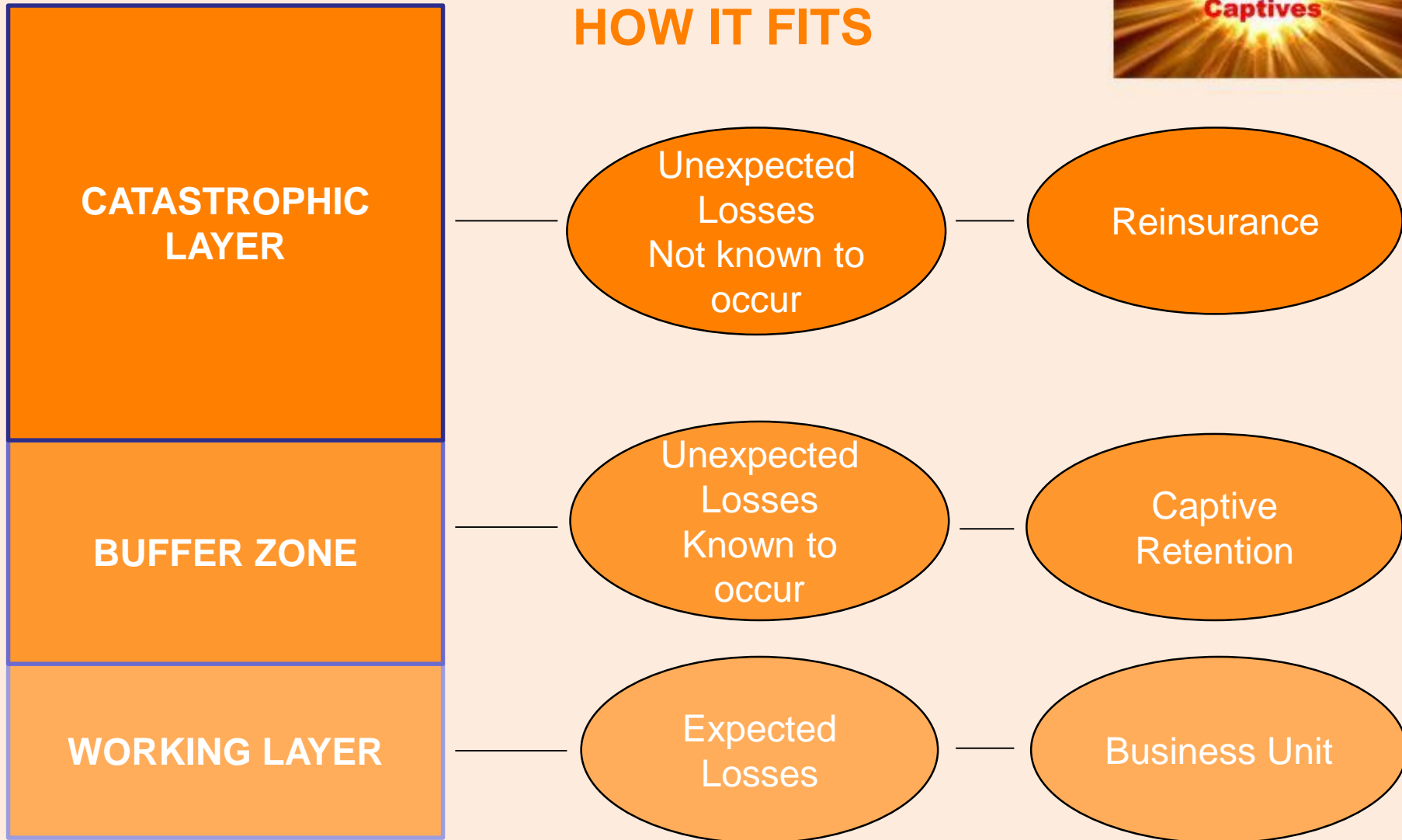


PREMIUM

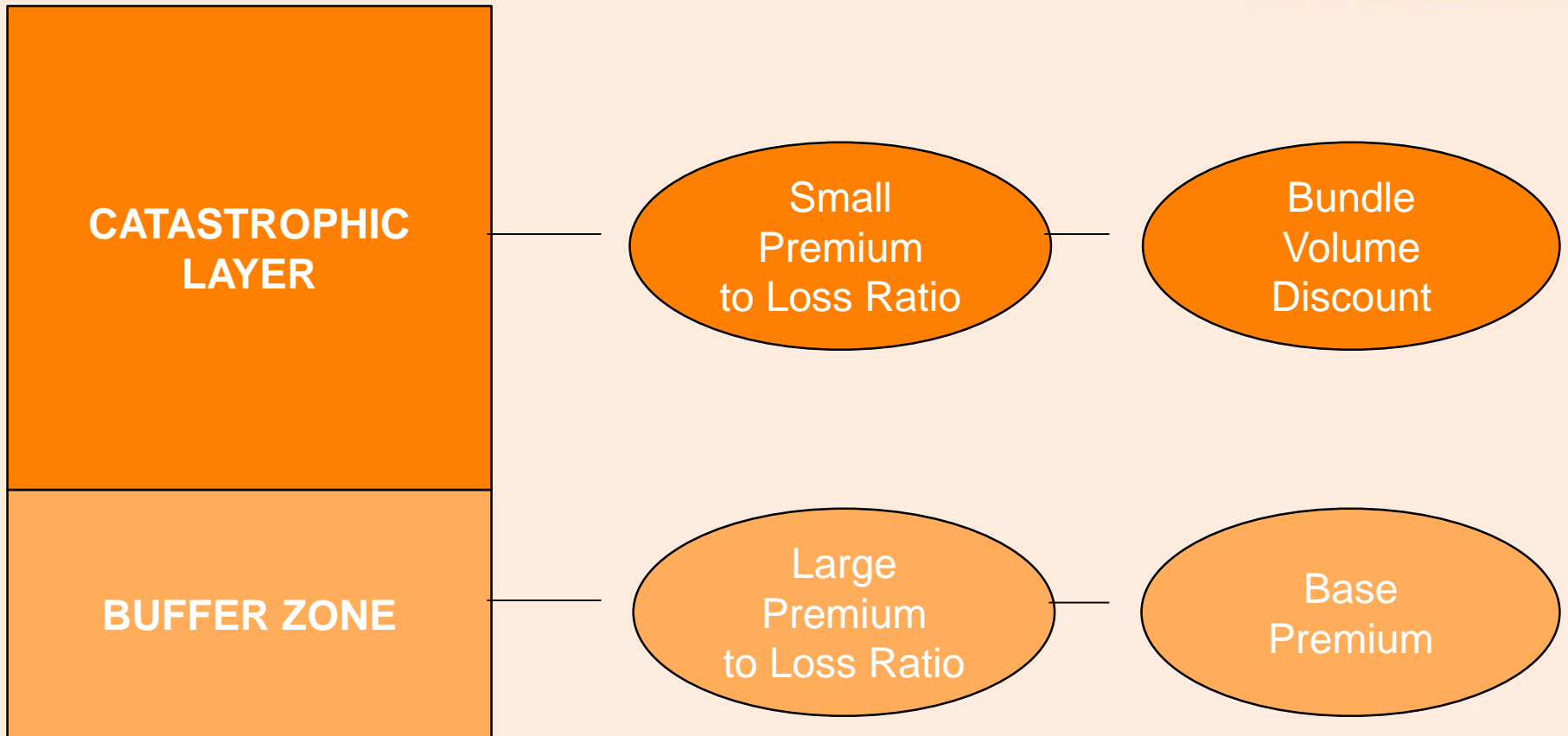
RETENTION



# BIG PICTURE HOW IT FITS

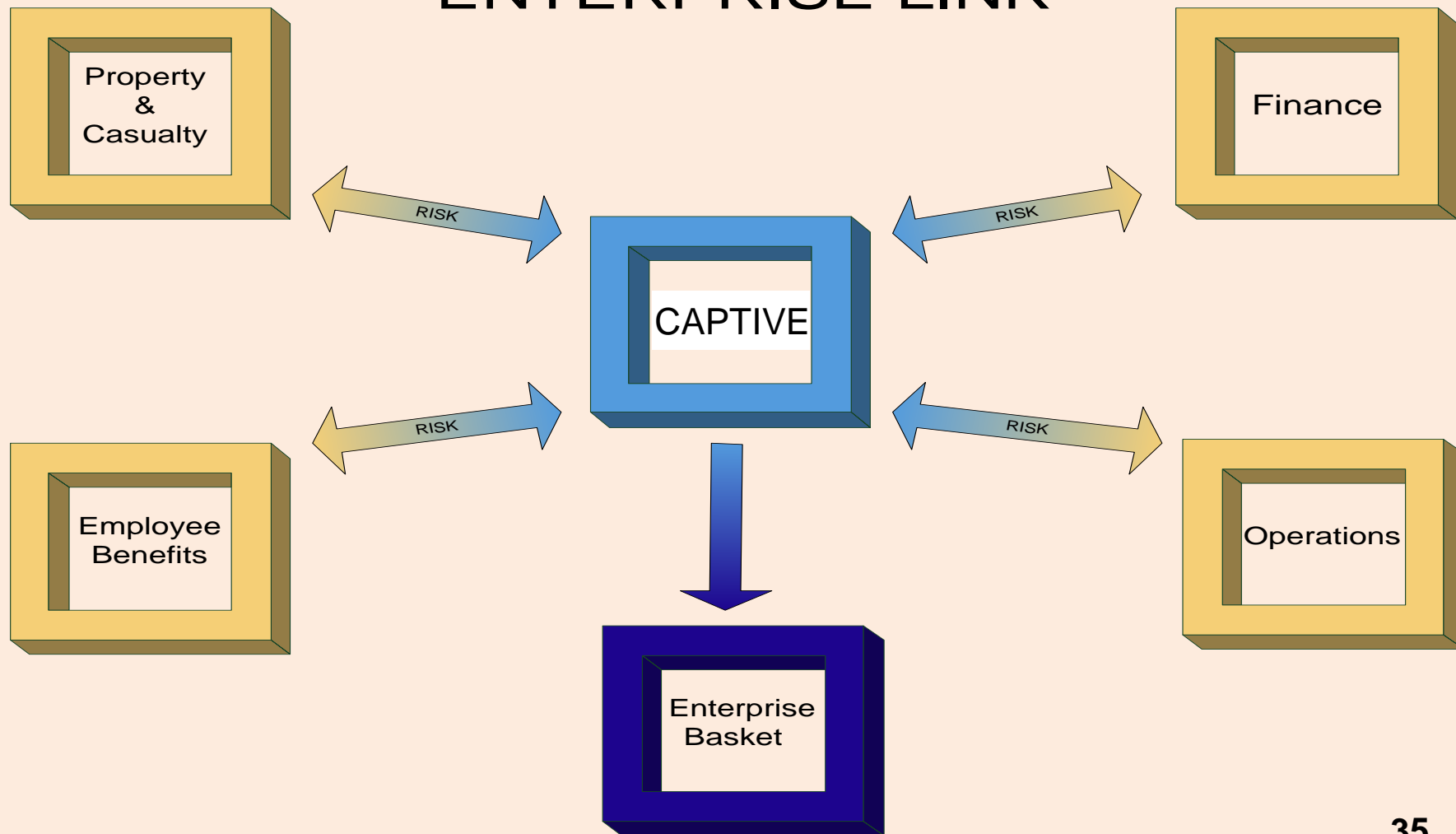


# BIG PICTURE HOW IT FITS





# ENTERPRISE LINK



# ENTERPRISE BASKET



**Within a Captive, a 3 year Stop Loss Feature (Basket) optimizes Enterprise Expense/Risk that includes Operational, Financial & Employee Benefits Exposures in a Pool.**

## **Strategic Structure:**

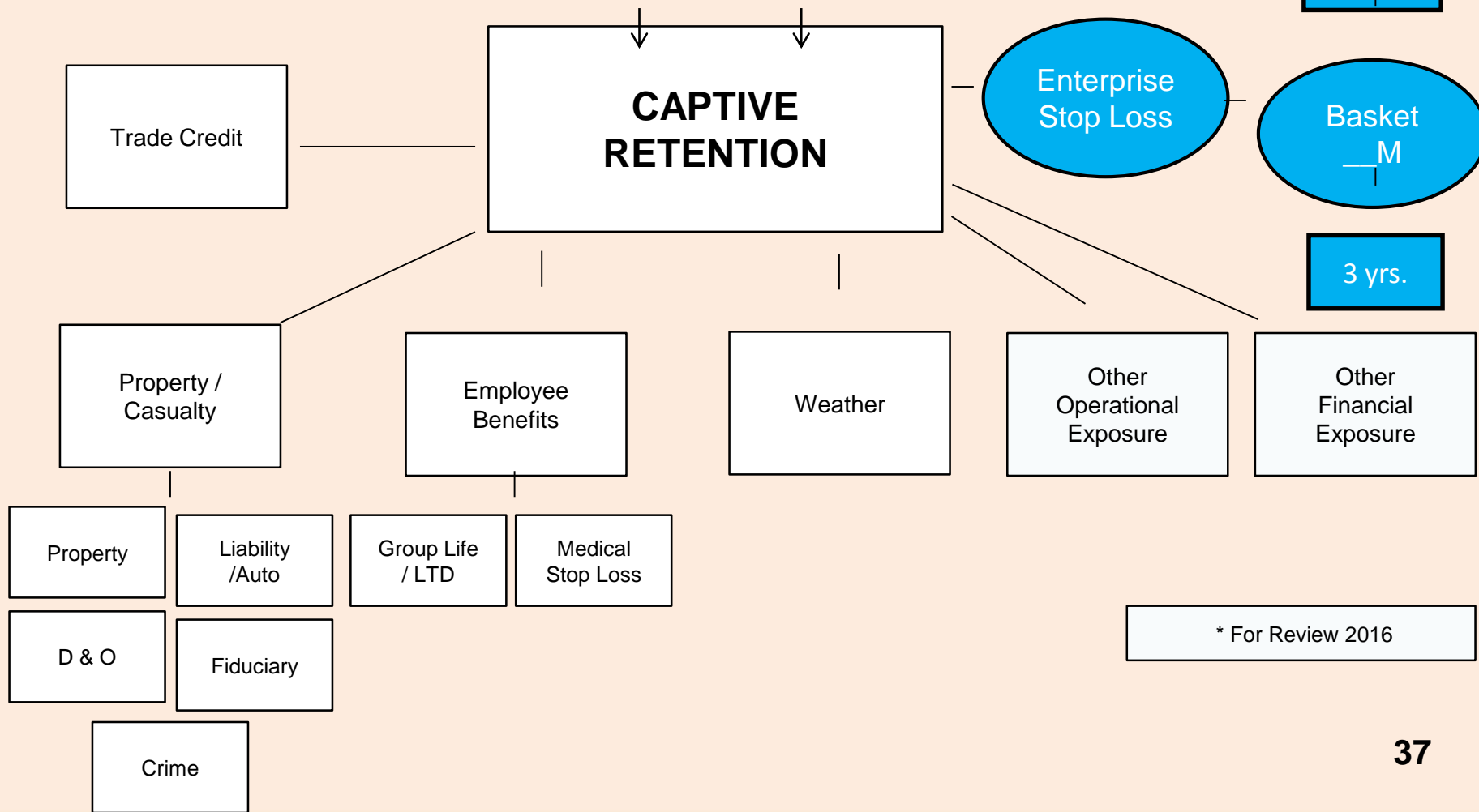
- **Unexpected , Non-correlated Exposures**
- **Spread the Risk**
- **Pool the Premium**
- **Share the Loss**
- **Manage the Volatility**

**Limits and Retention Levels for the Portfolio are selected to maximize Enterprise Net Premium Savings.**



# BIG PICTURE WHY IT FITS?

## BUFFER ZONE



# ADVANCED RISK TECHNIQUES



## Strategic Summary:

### **DIRECT ACCESS TO REINSURANCE**

Reduce Friction Costs

Program Design/Control

Long Term Relationships

### **OPTIMIZE RISK/CAPITAL**

Multiline/Multi-year

Blended Coverage – Shared Limits

### **OPTIMIZE PREMIUM/RETENTION**

Cost vs. Exposure Analysis

Risk Appetite – Buffer Zone

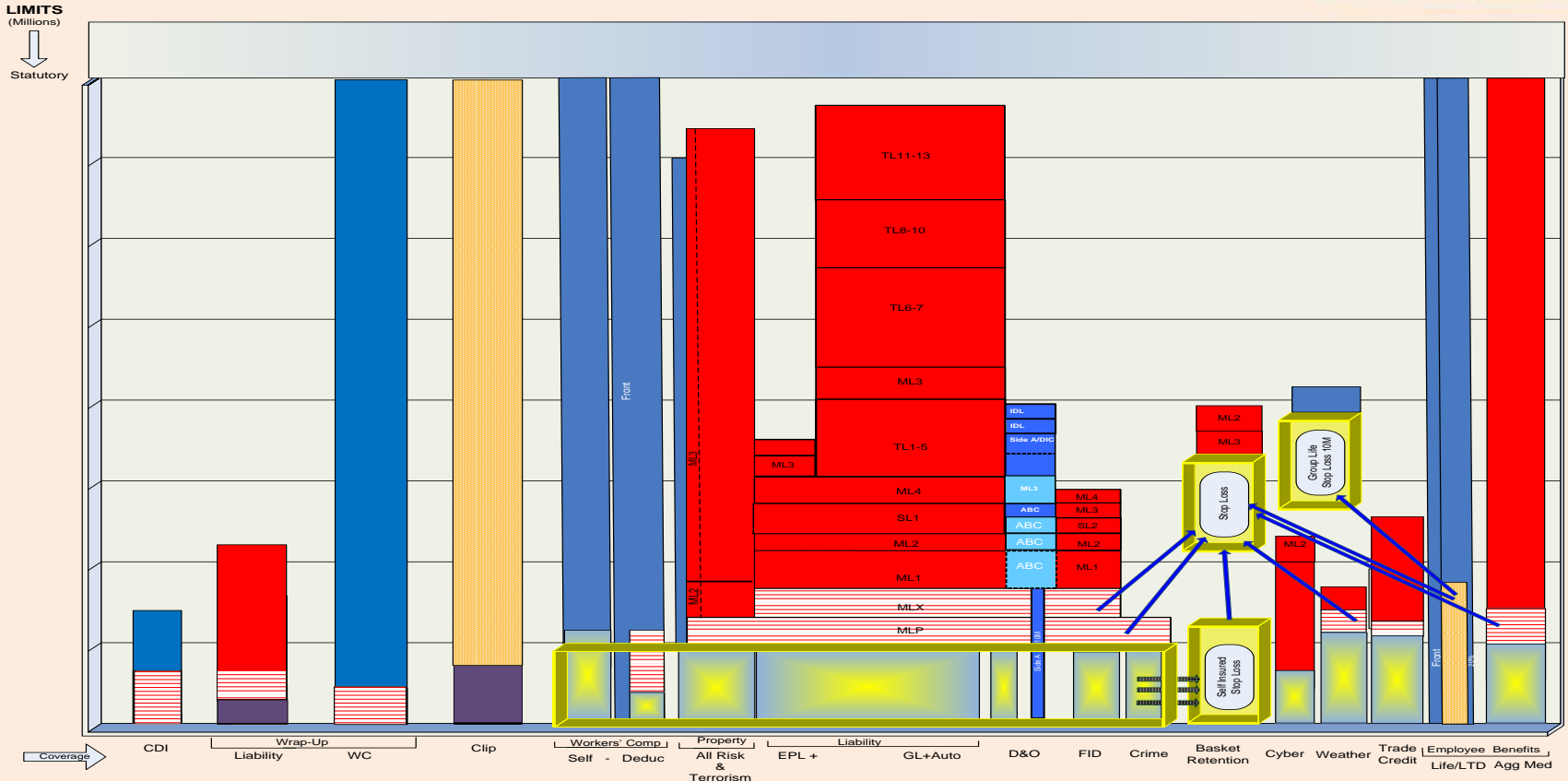
Stop Loss Baskets

Establish Premium Structure



<b>2001</b>	<b>Direct Reinsurance</b>
	<b>Blended Liability and D&amp;O Limits</b>
<b>2002</b>	<b>Shared Multi-Year Multi-Line Limits</b>
<b>2003</b>	<b>1<sup>st</sup> Buffer Zone &amp; Retention</b>
<b>2004</b>	<b>Integrated M&amp;A</b>
<b>2006</b>	<b>Employee Benefits</b>
	<b>Aggregate Primary and 1<sup>st</sup> Excess</b>
<b>2007</b>	<b>Blended Primary Property</b>
<b>2008</b>	<b>Medical Stop Loss</b>
<b>2009</b>	<b>Salt Cavern Integrity</b>
<b>2010</b>	<b>Enterprise Stop Loss Basket</b>
<b>2011</b>	<b>Integrated M&amp;A Corporate Program</b>
<b>2013</b>	<b>Reinsured Wrap-Up Construction; Warranties</b>
	<b>Trade Credit; Contractual Insurance Default (CID)</b>
<b>2014</b>	<b>Weather HDD Protection</b>
<b>2015</b>	<b>Cyber B.I. &amp; Enterprise Stop Loss Basket Expansion</b>

**ILLUSTRATION**



**COVERAGE LEGEND**

- Standalone
  - Shared Limits
  - Retention
  - Direct 100% Cede
  - Direct Retained
  - Reinsured Retained
  - RRG
- Policies issued by commercial carriers direct to AGL

Revised  
2015  
Not to Scale



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