

# **Wait, Insurers USE Captives?**

**Larson & Company Insurance Summit**

**November 19, 2024**

# Agenda

- I. Captive Profiles & Industry Overview
- II. Captive Value Proposition & Uses
- III. Captive Creation
- IV. Running a Captive
- V. Success Stories

# What is a Captive?

- A captive is an authorized insurance company specifically established to insure or reinsure the risks of its owner or affiliates and
- Is licensed and regulated by the state insurance department or (offshore) country equivalent,
- Allows owner(s) and/or participants to control and finance their own risks,
- Receives investment income from managing its own financial reserves and surplus rather than ceding profit to the commercial market, and
- Is a strategy for its owner(s) and/or participants to avoid co-mingling with disparate risk profiles that can drive premium increases.



# Common Types of Captives

## Single-Parent / Pure

- Owned and controlled by parent or related owner
- Primarily covers risks of owner and affiliates
- Control over insurance, total cost of risk savings, can tailor coverage to the insured's specific needs

## Group

- Formed by multiple unrelated organizations and each member is an owner and insured
- Members pool premiums, share risks, reduce overall costs
- Member access captive benefits without going it alone, can go to prefabbed group structure instead
- Heterogeneous = members from different industries; Homogeneous = members from same industry

## Association

- Owned by association or its members
- Only insures risk of association's members
- Economies of scale, can address hard-to-place risks, industry-specific coverage grants

## Sponsored (Cell / Condo / Rent-a-Captive)

- Usually managed by a third party, but each cell owned by individual participant
- Cells can be incorporated or unincorporated
- Allows multiple companies to insure their risks within the same captive license while keeping assets and liabilities separate
- Typically lower setup and operational costs compared to standalone captive

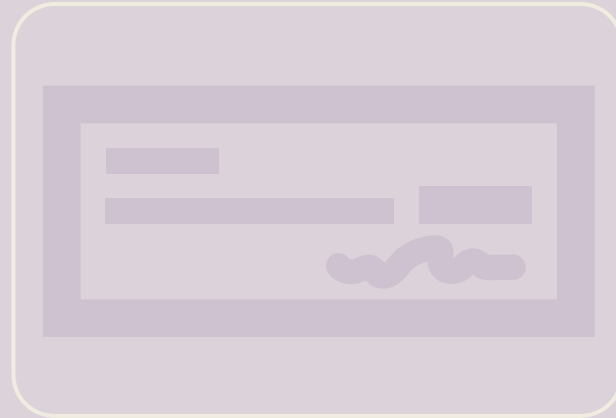
## Risk Retention Group (RRG)

- Capital and regulatory requirements midway between commercial insurers and pure captives
- Owners are insureds, and insureds are owners
- Can only write liability insurance
- Can register to direct write outside of domicile

# Captive Industry Overview



The first captive was widely regarded to have been formed in 1962 in Bermuda



Captives write ~\$60 billion in annual premium



Almost all Fortune 500 companies own at least one captive



More than half of the 6,000+ active captives in the world are owned by USA companies / organizations

# Captive Value Proposition



# Captives: A Wide Array of Uses



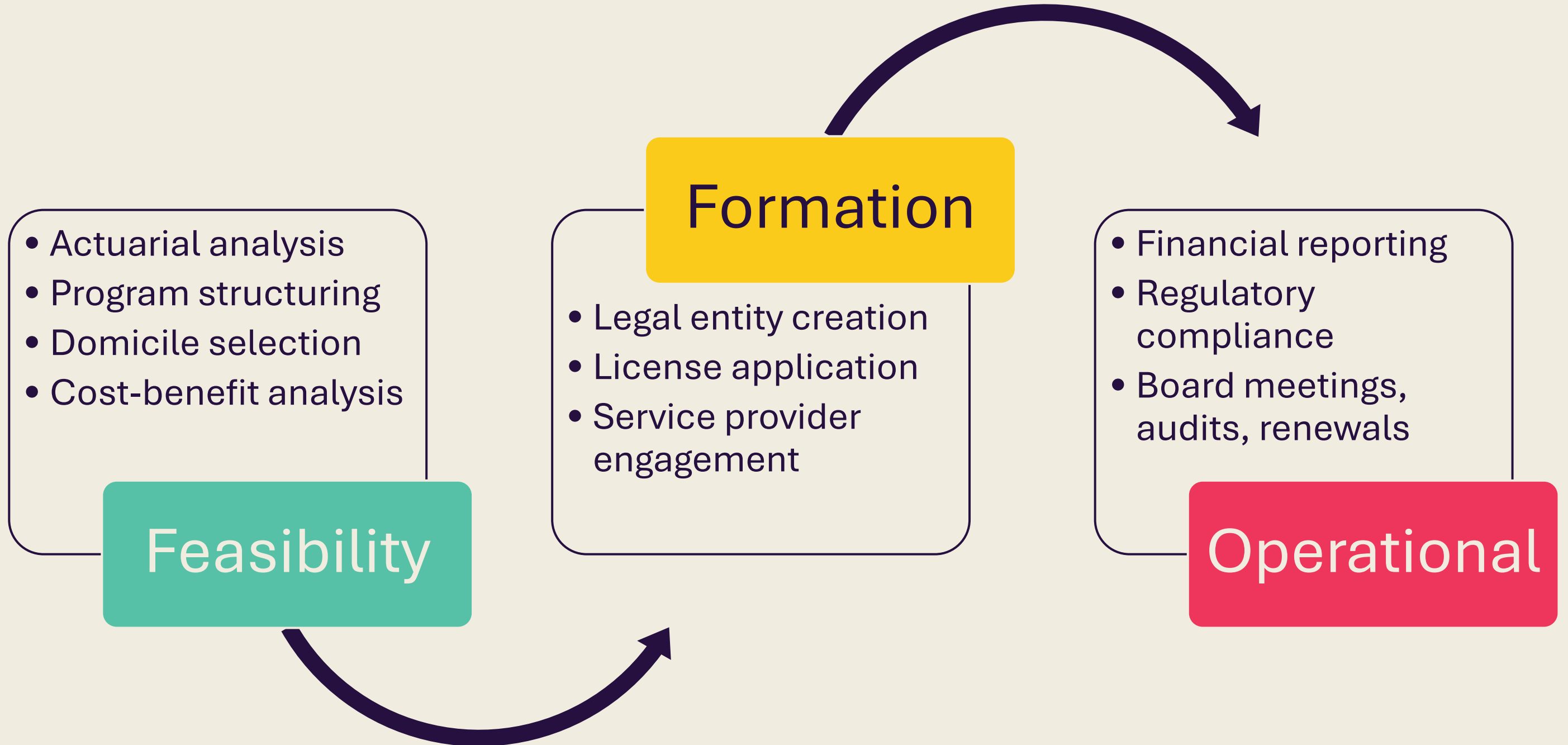
Coverages Only  
Limited to  
Commonly  
Accepted  
Characteristics of  
Insurability

Administrative Actions  
Adverse Party Legal Risk  
Auto Liability/Physical Damage  
Business Interruption/DIC  
Business Litigation  
Cargo & Inland Marine/DIC  
Contractual Liability  
Credit Default/Trade Credit DIC  
Cyber Liability/DIC  
Directors & Officers Liability/DIC  
Employee Dishonesty  
Employment Practices/DIC  
Environmental Liability/DIC  
Excess Liability/DIC  
Errors & Omissions Liability/DIC  
“Fat Finger” Insurance  
General Liability/DIC  
HIPAA/Billing Audit Liability

Labor Strike Reimbursement  
Loss of Key Employee/Person  
Loss of Key Customer/Contract  
Medical Malpractice/DIC  
Medical Stop-Loss  
Patent/Intellectual Property Infringement  
Political Risk  
Product Liability/Recall/DIC  
Professional Misconduct  
Property/DIC  
Property Wind/Natural Catastrophe Deductibles  
Property Management Liability/DIC  
Regulatory Change  
Reputational Risk  
Stock Throughput  
Subcontractor Default/Performance  
Wage & Hour Liability  
Workers’ Compensation

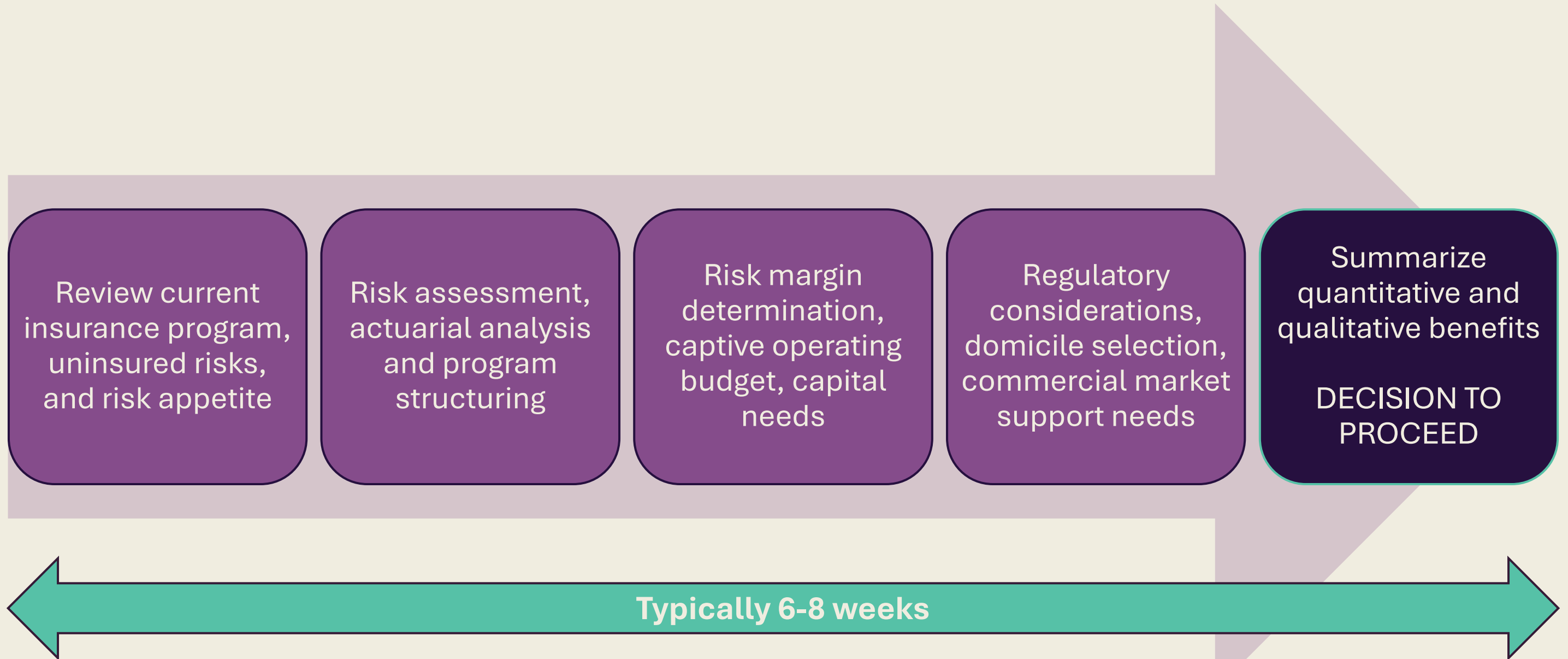
DIC = Difference in Conditions / Difference in Limits

# Captive Creation: Three Phases

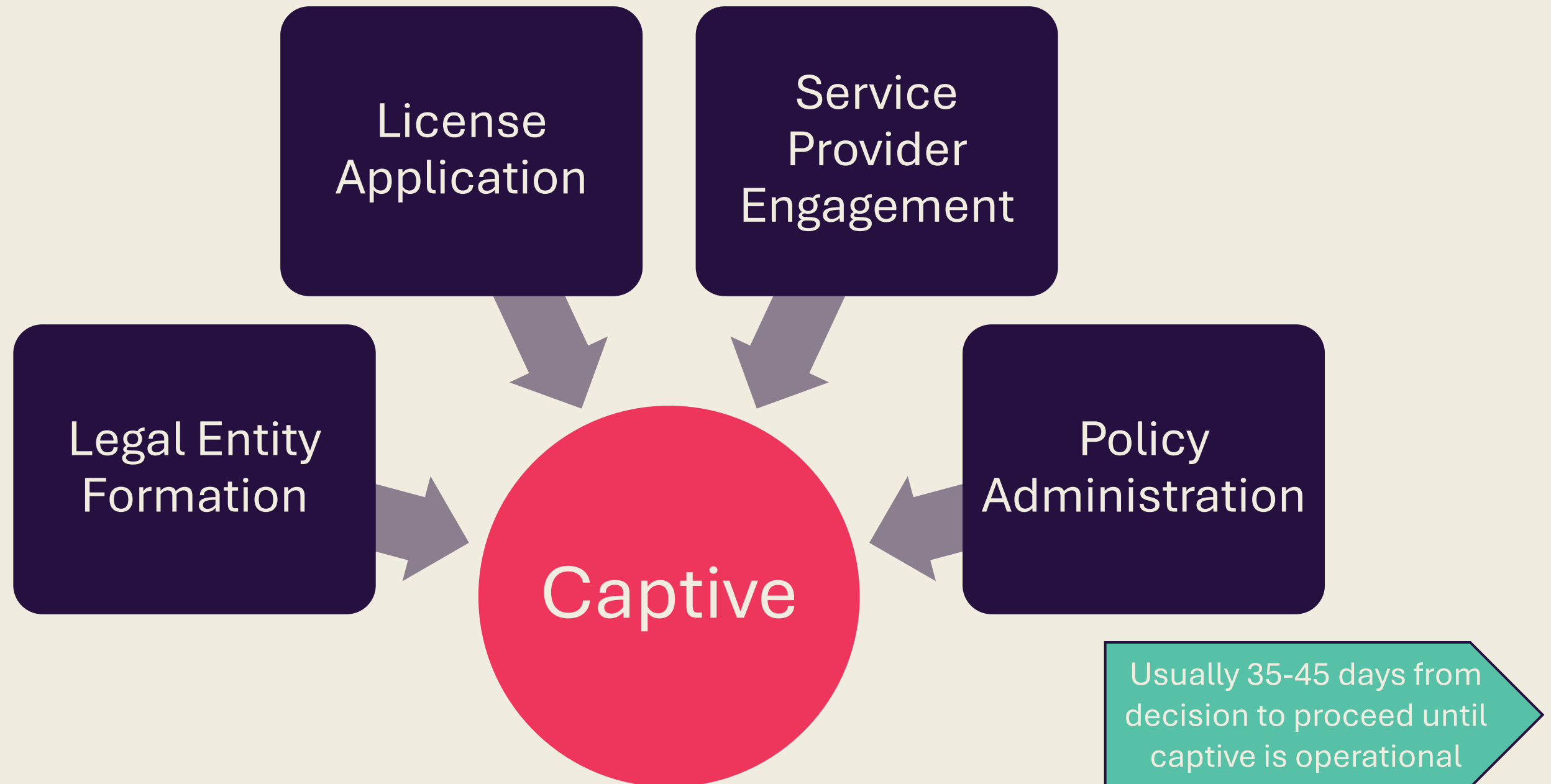




# Captive Feasibility Process



# Implementation Processes Run in Parallel



# Captive Service Provider Orbit



# Ongoing Captive Management Services

## STANDARD

**Financial Accounting:** Quarterly financial statement prep and review, premium tax filings, prepare and file income taxes

**Regulatory Compliance and Corporate Governance:** Ensure the captive is well-run and meets obligations of relevant statutes and rules, submit annual regulatory filings, function as regulatory liaison

**Operational Support:** Organize and facilitate annual board meeting, coordinate annual audit, maintain the captive's books and records, manage day-to-day captive operations

**Underwriting and Consulting:** Ad hoc consulting, annual renewal premium and policy administration

## A LA CARTE

**Evaluation & Implementation of Additional Lines of Coverage:** Coordinate analysis by the captive's actuarial consultant, program structure & premium development, capital adequacy review, and regulatory considerations

**Strategic Plan Development & Execution Accountability:** Chart goals, objectives, and projects for next 3-5 years

**Obtain Financial Strength Rating:** Support captive through the process of obtaining a rating from a nationally recognized statistical rating organization like A.M. Best

**Risk Consulting:** Assist with underwriting policies, managing claims, and implementing risk management programs

# Success Story: Group Captive



## Problem

Carrier lost 14 of its best construction accounts to a handful of homogeneous group captives over a 5-year period



## Solution

Sponsored and built private label group captive solution  
Provided fronting paper as well as excess and stop-loss coverage for primary layer



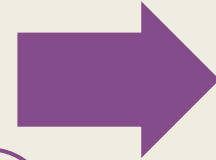
## Outcome

Did not lose any construction accounts for next 2 years (and counting...)  
Played offense with group captive to add 3 new accounts  
Sold more products to group captive members (e.g., several new lead umbrella accounts)

# Success Story: Pure Captive

## Problem

- Specialty property carrier struggling with decreasing reinsurance capacity and increasing premium
- Performance and balance sheet ratios continued to worsen



## Solution

- Formed pure captive to use as a reinsurer
- Subsidiary of insurance holding company and sibling to fronting paper entities



## Outcome

- Pushed reinsurance attachment points higher, shifting some reinsurance premium to captive.
- Shifted some retained risk to captive, improving certain ratios



**QUESTIONS**