



CAPTIVE FUNDAMENTALS

FROM YOUR MANAGER, LAWYER, AND ACTUARY

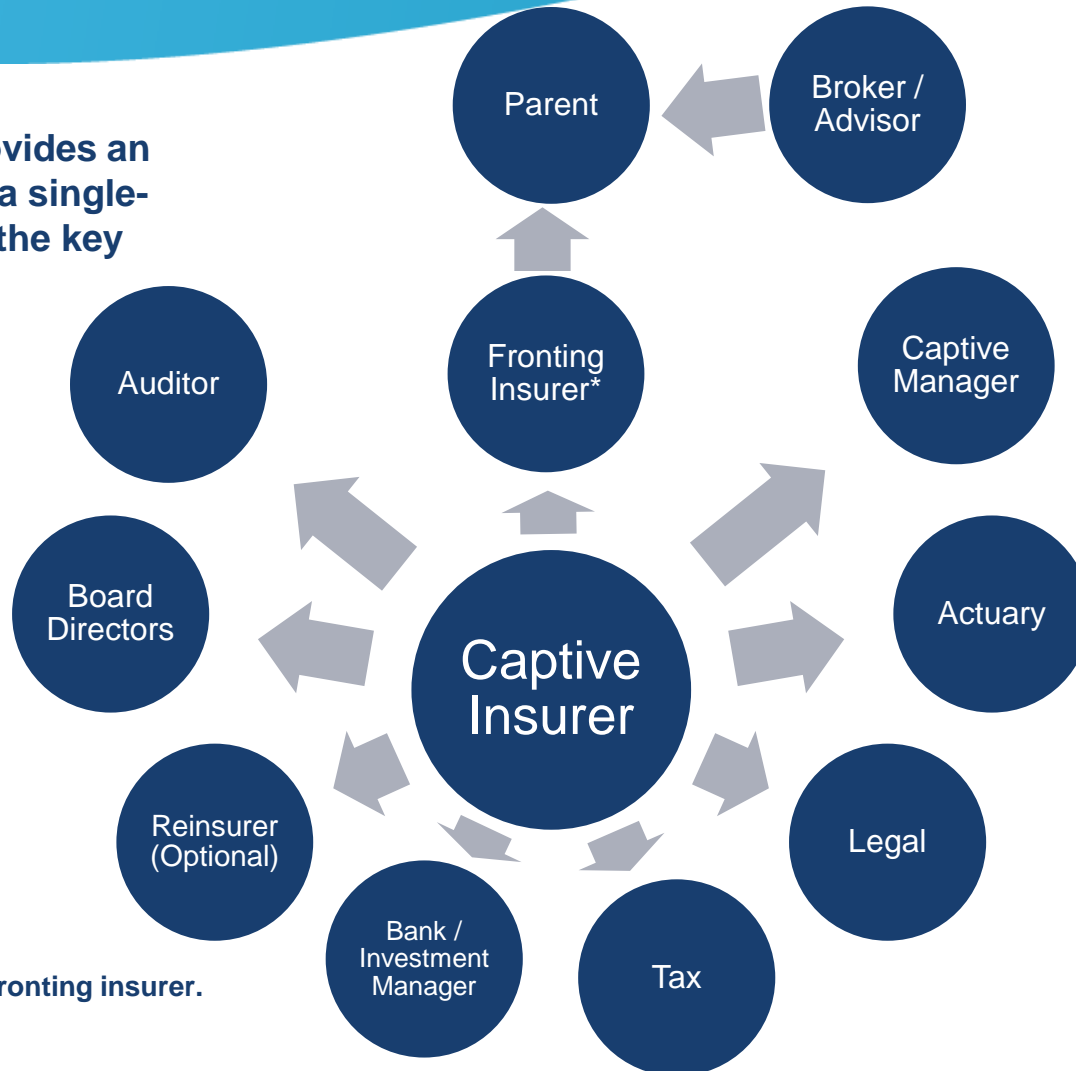
Laura Hurlston – Account Manager, Artex
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Vince Yezzi – Consulting Actuary, Willis Towers Watson



CAYMAN
CAPTIVE
FORUM
2018

THE CAPTIVE STRUCTURE

The following diagram provides an outline of the structure of a single-parent captive, indicating the key parties in the structure.



A comprehensive captive team can include:

- Insurance/captive manager
- Insurance broker/consultant
- Legal advisor with captive experience
- Tax advisor with captive experience
- Claims administrator
- Actuary
- Auditor
- Bank/Investment advisor
- Regulator

*Many captives do not require a fronting insurer.

ONGOING CAPTIVE MANAGEMENT

Once the captive is operational, the captive manager's role becomes focused on ensuring that the new captive delivers the full extent of the benefits possible and evolves over time to meet the owner's strategic and risk objectives. These services will include:

- Company and secretarial administration
- Regulatory liaison and compliance
- Corporate governance
- Accounting and financial reporting
- Coordination of any third-party service providers
- Strategic advice on the evolution of the captive

The captive manager's role is wider than the operational maintenance of the captive. It is critical that the manager also ensures that the captive continuously evolves to meet the parent organization's needs throughout its lifecycle. This involves working in partnership with senior management so that any changes to the risk profile or requirements to the parent, or variations in the commercial insurance market, are reflected in the operation of the captive.



OPERATIONS

Underwriting

- Policy issue and premium collection
- Evidence of insurance
- US legal & tax counsel review
- Actuarially determined funding

Claims management

- Normally the claims department of insured entity, but can be outsourced to a third-party administrator (TPA)
- Administer loss payments
- Loss run provided to captive manager & actuary
- Actuarially determined loss reserves

Treasury

- Investment of assets (within investment policy)
- Local bank account
- Monthly statements provided to captive manager
- Authorized Signatories
- Prepare annual budget

Management

- Account preparation
- Annual audit
- Schedule and attend board meetings and prepare minutes
- Ensure captive is run within policies set by BOD and regulators

Board of Directors (BOD)

- Nominated by Shareholder(s)
- Set governing policies for captive
- Approve engaging service providers, changes to corporate documents, previous minutes, and annual audited financial statements

Ongoing costs

- License renewal & regulatory fees
- Captive management fee
- Any necessary ongoing legal advice
- Actuarial fees
- Auditor fees
- Tax consultancy fees or expense
- Sundry expenses, including meeting costs, travel and accommodation



LOCAL REGULATIONS

Cayman Islands Monetary Authority (CIMA)

- Capitalization
- Solvency Provisions
- Obligations & Guidance
- Business Plan
- Corporate Governance Framework & Conflict of Interest Policy
- Risk Management Framework
- Record Keeping
- Beneficial Owner
- Local Meetings
- Fines & Penalties

Registrar of Companies (ROC)

- Directors
- Officers
- Registered Office
- Fines & Penalties

Summary

- Capitalization
 - B(i) \$100,000
 - B(ii) \$150,000
 - B(iii) \$200,000
- Solvency Provisions
 - B(i) \$100,000
 - B(ii) & (iii) Percentage Scale of Net Earned Premium
- Registration & Incorporation Expenses
- No Investment Restrictions (See CIMA guidance notes)
- Director Restrictions – 2 minimum
- 31 Tax Treaties
- Annual Audit Reporting Requirement - due 6 months after FYE



ANNUAL REVIEW

Annual Review

- Review captive participation, operations and coverages against ongoing objectives and regulatory requirements
- Continue working with client's professional advisors to evolve and add new lines of coverage where appropriate

Traditional captive lines

Expanded captive lines

Emerging captive lines

Captive Success

- Good risk management
- Favorable loss experience
- Sound underwriting and actuarial projections
- Consistent compliance with laws & regulations
- Disciplined application of retrospective premium mechanism (if utilized)
- Prudent release of surplus reserves
- Long-term commitment to this strategic initiative by the parent company



ROLE OF THE ATTORNEY

NOVEMBER 2018

MARK D. KLEINLEIN



IN A NUTSHELL

- **Serve as U.S. counsel/general counsel in captive operations**

CAPTIVE OPERATIONS

- Collaborate with insurance manager and other consultants, including Cayman counsel when necessary
 - Assist with Board education, strategic planning and best practices
- Attend Board and key committee meetings
- Prepare/review amendments to the business plan, governing documents and corporate resolutions
- Keep the Board apprised of legal and regulatory developments in Cayman and other domiciles
- Representation in captive mergers and consolidations

INSURANCE ACTIVITIES

- Review insurance policies, reinsurance arrangements and fronting arrangements, if any, to ensure the insurance program meets goals and expectations
- Provide advice regarding coverage and policy interpretation
- Protect the captive by appropriately reserving its rights in coverage disputes
- Prepare denial letters to protect the integrity of insurance policies
- Defend coverage and reinsurer disputes



REGULATORY MATTERS

- Provide advice regarding:
 - State insurance laws
 - Local regulatory requirements (e.g., onshore/offshore conduct) and related corporate governance policies
 - Hospital or physician regulatory and contractual requirements for insurance
 - Fraud and abuse, inurement and Stark laws, where applicable

TAX AND FINANCIAL MATTERS

- **Tax Compliance - work with shareholders and their tax advisors and auditors on:**
 - Shareholder and captive tax filings
 - Federal excise and state direct procurement taxes
 - FATCA and Common Reporting Standards
- **Tax controversies – assist with:**
 - Withholding tax issues
 - IRS disputes
 - Audit defense
- **Financial management**
 - Review draft audited financial statements and related notes
 - Ensure accuracy of Director’s Letter of Representations to the auditors
 - Draft custody and investment management agreements to ensure favorable terms



WHAT IS AN ACTUARY?

Someone not cool enough to be part of the Geek Squad at Best Buy.

A person who compiles and analyzes statistics, and uses them to calculate insurance risks and premiums.

ACTUARIES

Types of Actuaries

- Life
- Pension
- Property / Casualty

Employers of Actuaries

- Insurance Companies
- Government
- Consulting Firms



EDUCATION

Finance

Economics

Accounting

Computer
Science

Law

In addition to

Probability

Statistics

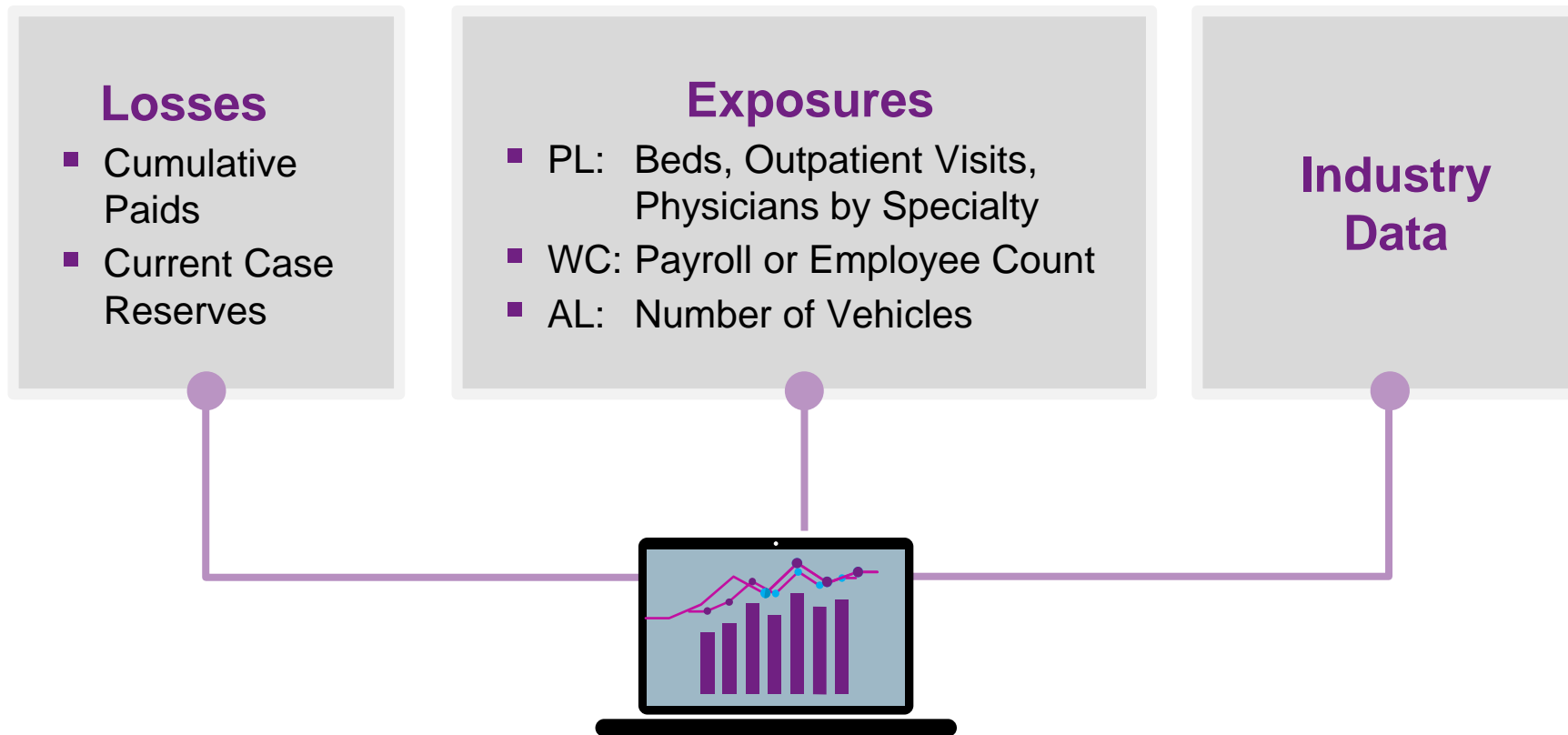
Calculus

Linear
Algebra

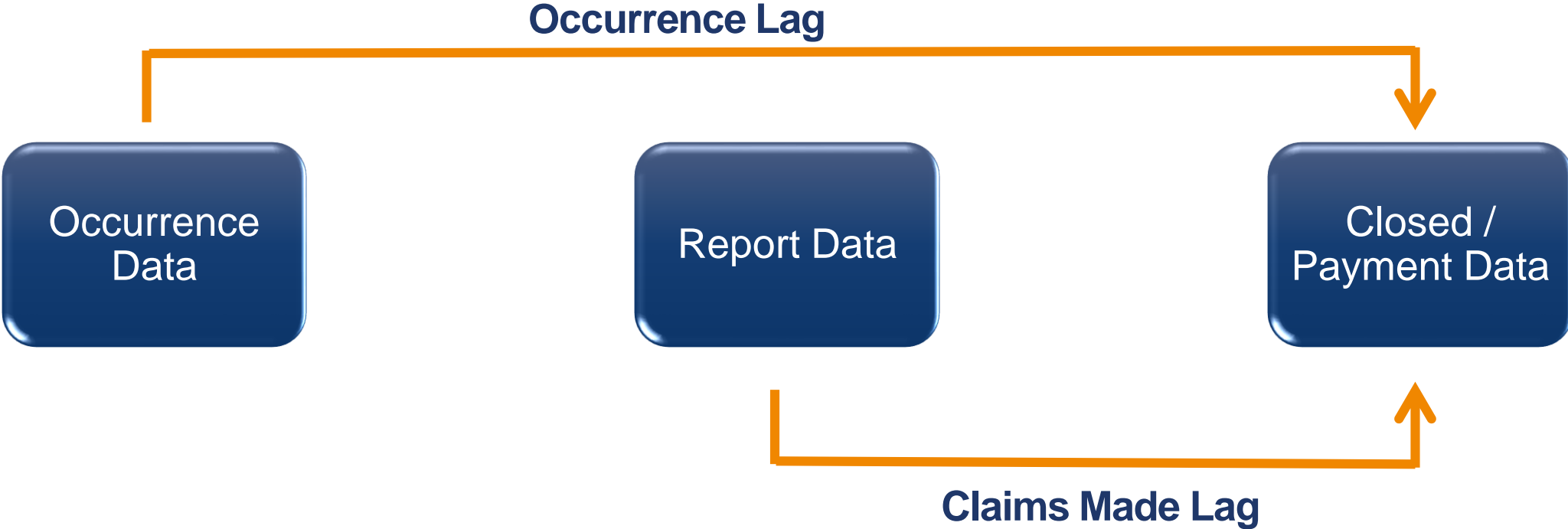
ACTUARIAL ROLES IN CAPTIVES

- **Feasibility Study**
 - Domicile
 - Lines of Business
 - Retentions
 - Proformas
 - Premium Indicators
- **Funding for Prospective Year**
- **Liabilities for Prior Years**
- **Allocation to individual member**

DATA USED



INSURANCE LAGS



ULTIMATE LOSS COMPONENTS

Ultimate Losses

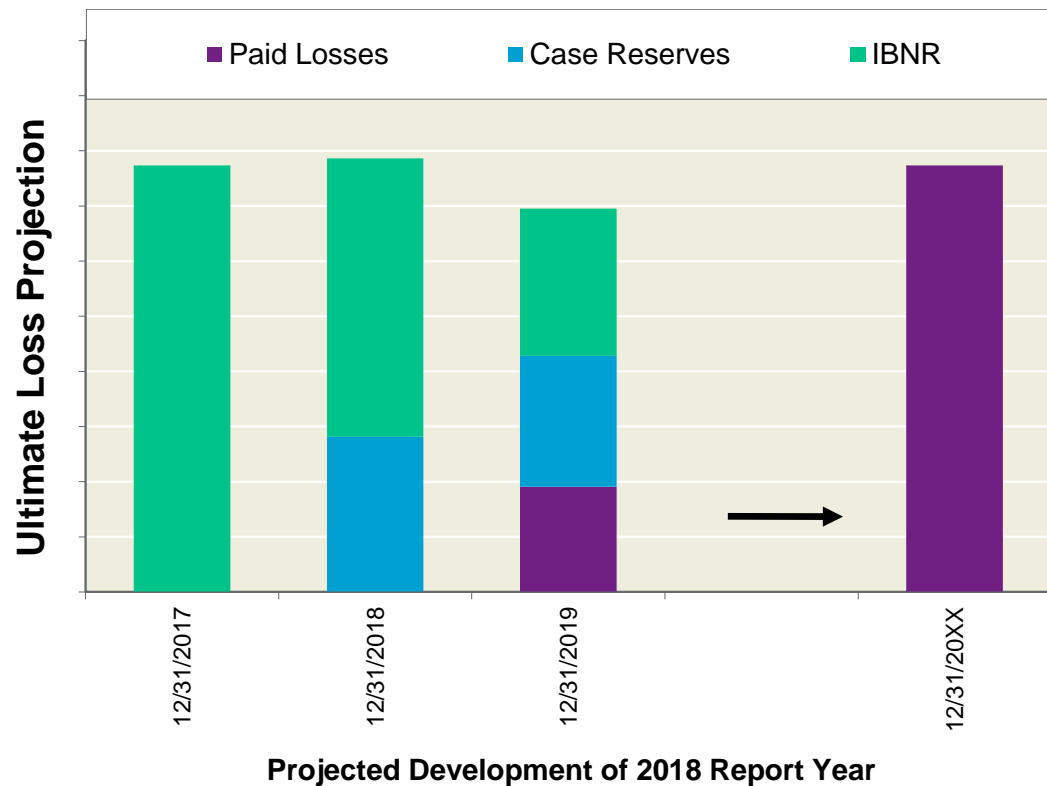
- Paid Losses
- Case Reserves
- IBNR

IBNR

(Incurred But Not Reported)

- Claims that have not yet been reported
- Additional development on case reserves of known claims

Sample Illustration



ADJUST PRIOR DATA FOR:

Exposure
Growth



Change
in Retentions



Trend



Loss
Development



QUESTIONS?

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THANK YOU



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