
CAPTIVES Unleashed
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WRCIC
WESTERN REGION CAPTIVE
INSURANCE CONFERENCE, LLC
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# Captive Finance & Collateral Complexities

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WRCIC 2024
WESTERN REGION CAPTIVE INSURANCE CONFERENCE, LLC

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# Presenters

01 What is Collateralization

02 Why is collateralization important in reinsurance

03 How much Collateralization is needed

04 Types of Collateral

05 Advantages & Disadvantages of each type of Collateral

06 Accounting Practices for Collateralization

07 Draw down process

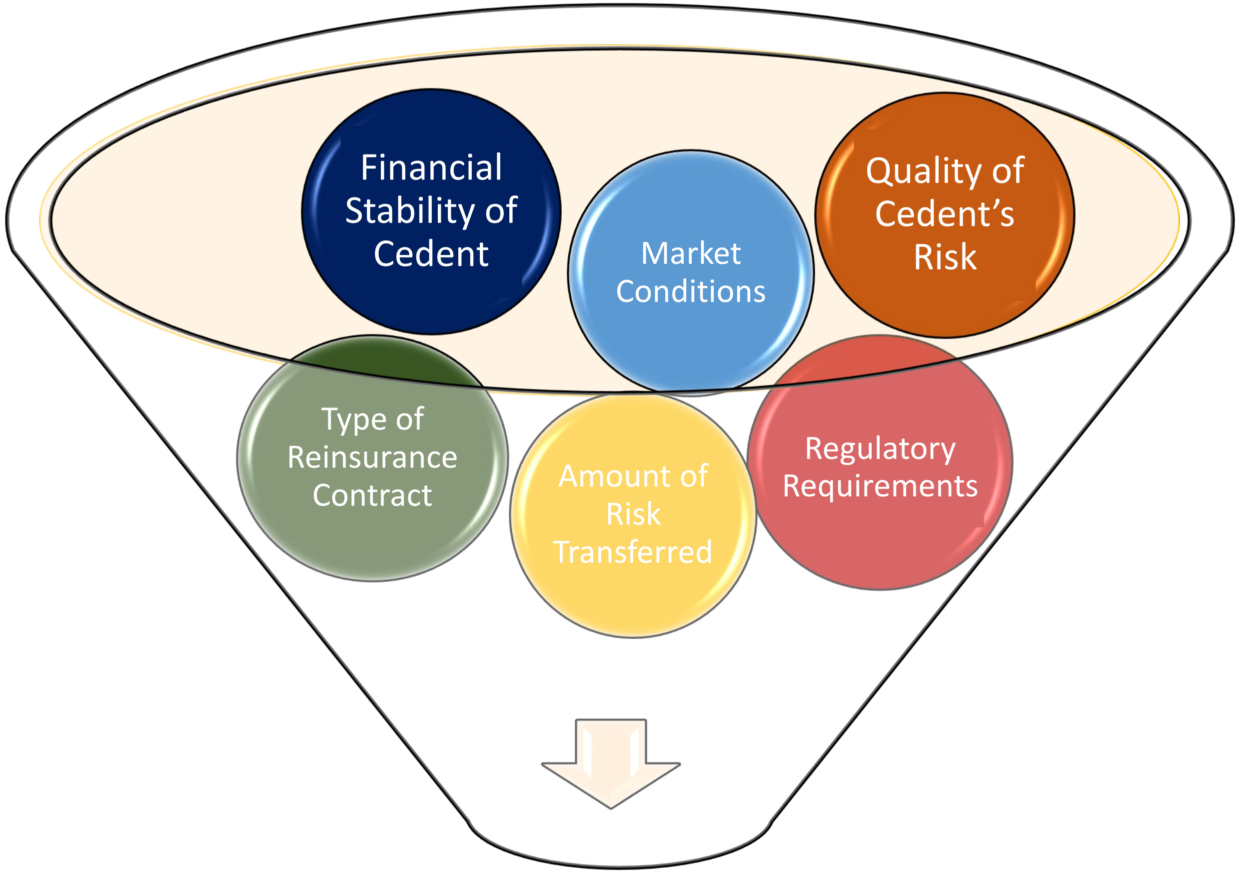
08 Impact of Vestoo on Collateralization

# Why is Collateral Needed?

# Schedule F: Credit for Reinsurance

Section in an annual insurance statement in which reinsurance transactions are disclosed. It is used by regulators to identify the different reinsurance arrangements that an insurer may be taking part in and as an indicator of the ability to collect reinsurance recoverables if losses are incurred.

1. Shows assumed and ceded reinsurance by reinsured and reinsurer, as well as premiums on portfolio insurance.
2. Shows the provisions for reinsurance recoverables from reinsurers who are slow in making payments.
3. Restates the insurer’s balance sheet to be gross of ceded reinsurance.
4. Schedule F is a Statutory Concept but there are components of credit for reinsurance in GAAP and IFRS




To take credit for reinsurance ceded to a non-admitted carrier, the insurer must be provided collateral in an amount equal to at least the amount of reinsurance reserves the insurer recorded in its financial statements

There is an exception technically if the cedant and reinsurer share the same US domicile (RARELY used)

# Amount of Collateralization Needed

- Cash
- LOCs
- Securities
- Funds Withheld
- Trust Agreement
- Third-Party Sureties

# Types of Collateralization: Pros & Cons

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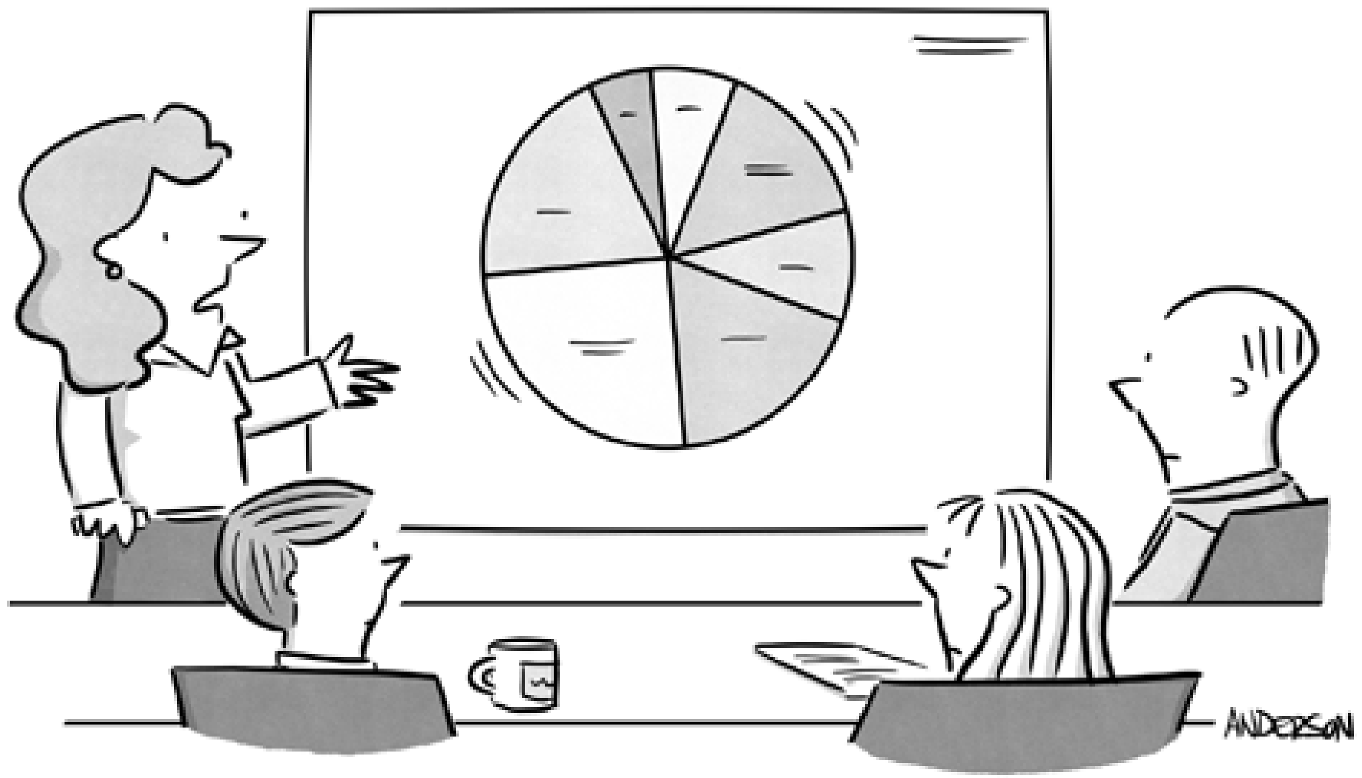


"I can make it bounce, I can make it spin...
But you understand that it doesn't change
the numbers, right?"

# Collateralization Accounting Practices & The Draw Down Process

# Collateralization Accounting Generalizations

## Cash

- Asset on the balance sheet in the amount of restricted cash held
- Liability is booked at the amount of reserves provided by the reinsurer
- Changes in the fair value of cash collateral may impact the financial statements through profit or loss or other comprehensive income.

## LOCs

- Until the LOC is utilized for a business transaction, an LOC is an off-balance sheet disclosure.
- Most jurisdictions will recognize a LOC as an asset and capital contribution, but expect a modified audit opinion
- The disclosure included the type of LOC, the maximum of the LOC, and any terms or conditions attached to the LOC
- Most of the time the reinsurer, cannot alone support it so accounting must follow, the LOC "sponsor".

## Securities

- Asset on the balance sheet
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# Collateralization Accounting Generalizations

## Funds Withheld

- Asset on the balance sheet
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## Trust Agreement

- Just a trust held for the benefit of the cedant
- The trustee controls disbursements

## Third Party Sureties

- The accounting treatment for third-party sureties, such as bonds or guarantees provided by external parties, depends on the nature of the surety and the underlying transaction.
- Companies typically disclose information about third-party sureties in the notes to the financial statements. This includes details about the nature of the surety, the maximum amount covered, and any terms or conditions attached to the surety

# Typical Draw Down Process

1. **Loss Fund/Trust**
   Claims are paid from the captive's loss fund/trust account
2. **Captive Surplus**
   Excess losses are paid out of captive surplus
3. **Capital Contribution**
   Shareholders post additional capital to rectify any shortfall
4. **Collateral Draw Down**
   Collateral draw down is triggered

# Vestoo Implications
# Presented by Doug

witty commentary provided by Leon, Nate & Kirsten