



**2010 Insurance Economic Summit:  
Navigating the Era of Reform**

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**2010 Insurance Economic Summit:  
Navigating the Era of Reform**

**Minimizing Exposure in a  
Down Economy**

**John G. Aquino**, Executive Vice President, Willis Re, Inc.  
**Laura M. Johnson**, Managing Director, LECG  
**Eric A. Haab, Partner**, Foley & Lardner LLP

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**Agenda**

**Practical advice regarding strategic and tactical steps  
your organization can take to:**

- Protect your reinsurance program from external pressure
- Identify financially strong reinsurance partners
- Negotiate contract terms to protect against downside risks
- Minimize risk and effectively deal with business partners that are financially troubled or in receivership
- Ensure timely identification and collection of all inuring protections

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## Protect Your Reinsurance Program

**Reinsurance Broker Perspective**

- Macro-economic Environment Is Weak Growth
- Implications For Insurers
  - Product demand is off
  - Rate levels are down
  - Revenue pressure is up
  - Insurers are dressing up revenue by cutting reinsurance
- Implication For Reinsurers
  - Same as insurers
  - Hence, cost of reinsurance is currently low
- Is Now The Smart Time To Cut Reinsurance Protection?

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## Identifying Financially Strong Reinsurers

**Reinsurance Broker Perspective**

- Credit Risk Is Real
- Broker Role
  - Does not act as guarantor of carrier solvency
  - Has a duty to use skill, care and diligence in reinsurance placement
- Willis Vision Of The Broker Role
  - Protection of clients
    - Application of prudent standards
    - Rating agency information
    - Internal assessments
  - Added value: information and updates on reinsurers
  - Management of Willis relationships with reinsurers
- Reinsurance Buyer Makes The Reinsurer Decision

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## Identifying Financially Strong Reinsurers

**Reinsurance Broker Perspective**

- Willis Approach To Market Security In Practice
  - Market Security Committee led by the Chairman of Willis Ltd
  - Dedicated market security team of 35 personnel
  - Independent evaluation of 2,000 insurers and reinsurers globally
  - Carrier financial data captured and maintained for online access
- Practical support to Willis Re clients
  - Financial results for last three years on every carrier
  - Factual reports on key groups and Lloyd's syndicates
  - Rating agency ratings and rationales
  - Advice and updates on distressed carriers
  - All available via Willis Online extranet

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## Identifying Financially Strong Reinsurers

**Consultant Perspective**

- Building Tools to Support Timely, Informed Decision Making
  - Automation of analysis and reporting based on corporate criteria
  - Evaluation of IRIS tests results and profitability/ liquidity/ leverage/ loss reserve adequacy/ RBC and growth criteria ratios
  - Data integration of third party data sources including A.M. Best, S&P, Moody's, Fitch and IRIS ratios;
  - Evaluation of reinsurance recoverable exposures
- Tracking
  - Approved reinsurers
  - Approval limits, current and historical
  - Current events including press releases & articles

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## Negotiate Contract Terms and Conditions

**Reinsurance Broker Perspective**

- Contract Clauses Related To Reinsurer Financial Distress
  - Special termination
  - Reserves and funding
  - Sunset and commutation
  - Service of suit
  - Arbitration
- Collateral Considerations
  - Collateral forms
    - Funds held
    - LOC
    - Trust account
  - Reinsurer categories
    - Admitted
    - Rated non-admitted
    - Unrated non-admitted

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## Negotiating Contract Terms and Conditions

**Legal Perspective**

- GOAL: Find as stable a business partner as possible, and obtain contract terms that provide the greatest protection possible
- Careful review is critical
- Beware of treaties pieced together using standard clauses from a variety of sources
- Consistency with slips and cover notes must be confirmed

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## Negotiating Contract Terms and Conditions

**Legal Perspective**

Contract provisions relevant to the risk that business partners will become financially troubled in the future

- Insolvency clause (mandatory for reinsurance financial statement credit)
- Collateral requirements
- Cut-through clauses
- Commutation/sunset clauses
- Downgrade clauses
- Change in control clauses

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## Minimize Risk – Troubled Reinsurers

**Reinsurance Broker Perspective**

- Evaluate Special Termination Options
  - Cutoff prior to expiration
  - Treatment of outstanding liabilities
    - Funding
    - Commutation
- Reconsider Reinsurance Costs And Benefits
  - Net capital benefit
  - Expected recoveries
    - Amounts due under contract terms
    - Revised expected value given potential current reinsurer condition

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## Minimize Risk – Troubled Business Partners

**Legal Perspective**

- Key considerations and issues to address the risk of insolvency
- Act swiftly and decisively – once a party is in receivership, a resolution may be years away. Opportunities may arise to assist regulators in avoiding or delaying an insolvency
- Fully and properly assert and take advantage of set off rights
  - Enforceable in receivership
  - Possibly enforceable against affiliates of an insolvent company
  - Language can be important, as can prior course of dealing

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## Minimize Risk – Troubled Reinsurers (cont.)

**Legal Perspective**

- Cut-through clauses
  - Not common, utilizing them properly is critical
  - Can be implied in circumstances
  - Take steps to ensure against double liability
- Enforcement of collateral for ceding companies / protection of collateral for reinsurers
- Downgrade and change in control clauses – enforcement or at least avenue to renegotiation

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## Minimize Risk – Troubled TPAs

**Consultant Perspective**

- Define and employ a process to identify at risk parties
- Ensure audit process considers operational and financial risks
  - Transactional review
  - Claim handling
    - Loss Reporting
    - Loss reserve development and adequacy
  - Loss payments (funding TPA)
  - Financial statement review
  - Governance and compliance
- Perform regular audits to evaluate controls and identify emerging risks
- Tailor audits to specific risk factors

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## Identification of Reinsurance Recoveries

**Consultant Perspective**

- Loss reporting from TPAs
  - Regulatory restraint to pay claims timely
  - TPA late and inaccurate reporting impact on cashflow
- Facultative
  - Multiple data sources
  - Certificates covering multiple policies
  - Low cost technology solutions to find potential hits
- Bordereaux reporting
  - Review processes and controls used in identifying ceded losses
  - Assign risk factor based on manual nature of process

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## Disputes... When to Involve a Lawyer

### **Legal Perspective**

- Know and assert rights in advance of receivership
- Opportunities for early resolution may be available, or steps may be taken to improve a position in advance of insolvency
- Following proper procedures once insolvency proceedings are initiated is critical
- Find counsel with experience in the area
  - Bankruptcy is frequently not a guide
  - Applicable decisions may be scarce in a given jurisdiction
  - Knowledge of how receiverships operate in practice is key

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