BEECHER CARLSON

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OPPORTUNITIES TO FINANCE RISK IN A HARDENING MARKET

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SPEAKER INTRODUCTION

Pete is the leader of Beecher Carlson's Captive Practice, an integral part of the Risk Optimization Group, operating across 20 jurisdictions throughout North America and the Caribbean. Beecher Carlson is among the world's largest captive managers by entities managed and premium volume and is one of the most awarded captive managers in the industry as recognized by Risk & Insurance, Captive International and Captive Review's Annual US Captive Service Awards.

Pete has over 16 years of experience in the captive insurance industry, preceded by 10 years in public accounting. He began his career in public accounting, gaining significant experience in auditing, tax and business consulting and advisory services. In early-2005, Pete joined Beecher Carlson's Vermont office, managing several of the largest Vermont clients. Since 2019, Pete has been leading all of Beecher Carlson's captive operations, consisting of over 135 risk bearing entities, $4.8 billion in annual premiums and nearly $20 billion in total assets.

Pete is a graduate of Champlain College in Burlington, Vermont, where he earned a Bachelor of Science degree in Accounting. He is a Certified Public Accountant, licensed in the state of Vermont. Pete is a frequent speaker at conferences, contributor on podcasts and webinars, and writer for industry publications.

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- *2018 – Captive Review's "Ones to Watch"*
- *2019 – Captive Review's Captive Service Professional of the Year [Shortlist]*
- *2020 – Risk & Insurance Power Broker – Captives (1 of only 6)*
- *2020 – Captive Review's Captive Service Professional of the Year [Winner]*
- *2020 – Captive International's Feasibility Study (Individual) – [Highly Commended]*
- *2020 – Captive International's Captive Manager (Individual) – [Winner]*

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WHAT GOT US HERE

Soft Insurance Market	Bad CAT loss years	Hardening Insurance Market
early-2000s	mid- to late- 2010s	2018-2020
After the events of September 11, 2001, the insurance market started to soften based on a number of different factors - focus on unknown and unexpected risks and risk management, continually improving technology and access to data to better mitigate claims, risk being pulled from the traditional markets and utilization of captives for risk financing as a result of the premium increases resulting from the events of September 11, 2001.	There was a series of years with bad wind and fire CAT losses. In the first year, the carriers were able to release some redundant reserves (as they should) and turn to the capital markets to replenish their surplus. After the second year, there wasn't quite as much redundancy and the capital markets were growing more hesitant which started some pricing increases. In the third bad year in a row, the reserve releases weren't really there and the capital markets were retreating in their support resulting in significant pricing increases.	This hard market has been different than others due to the carriers fundamentally changing, some would say correcting, their underwriting philosophy. Historically, there had always been a push to "fill capacity" which even in an increasing premium environment would be a counter-balance the increase - the insured still had some leverage. Today, carriers are focused on getting "rate" - pricing the transactions to make money and not be nearly as concerned with filling capacity.

WHAT DOES IT ALL MEAN?

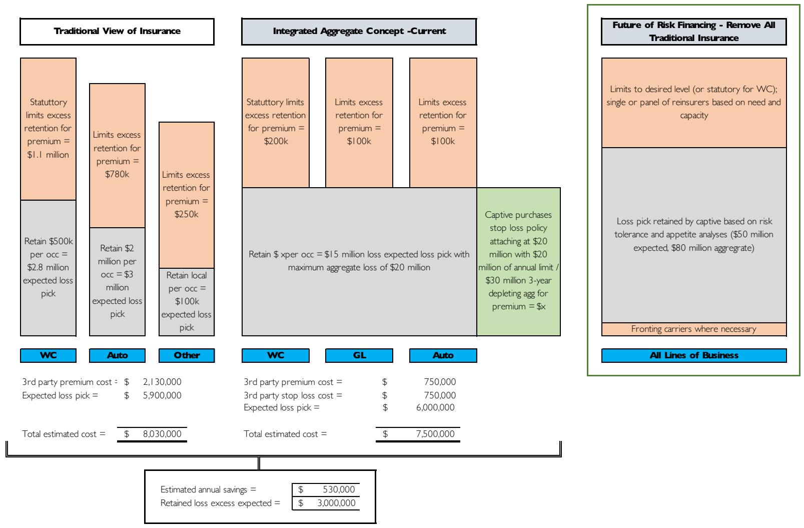
Risk financing is changing. This was already happening. Carriers and reinsurers are changing how they underwrite, which is becoming a greater impetus to the overall change in risk financing.

Improved technology, greater access to data and the continually improving ability to analyze that data has been leading larger, more complex organizations to not only retain greater amounts of risk but to rethink how they deploy their total cost of risk (TCOR) in the most efficient way.

The premium increases hitting insureds today is happening at all levels. As small and middle market organizations are experiencing these pricing increases, they, too, are needing to look at how they finance their TCOR.

Carriers, through their pricing increases and inflexible approach to underwriting, are causing for a faster advancement of risk financing than was already occurring.

EVOLUTION OF RISK FINANCING



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RISK TOLERANCE AND APPETITE

As risk financing continues to evolve, with more organizations accepting, or being forced to accept, more risk retention, the evaluation needs to begin with what an organization's risk tolerance and appetite are. Below is an example of a premium credit versus risk retention:

Potential Prem. Savings **	Layer	Loss Amount in Layer 1,000,000	2,000,000	3,000,000	4,000,000	5,000,000
1,250,000	$5M xs $10M	0.80	1.60	2.40	3.20	4.00
1,000,000	$5M xs $15M	1.00	2.00	3.00	4.00	5.00
750,000	$5M xs $20M	1.33	2.67	4.00	5.33	6.67
500,000	$5M xs $25M	2.00	4.00	6.00	8.00	10.00

Decreasing Likelihood of Event

** Payback years calculated as loss amount (unlimited, ground up) divided by annual premium savings*
*** Market premium would be captive premium amount (additional expenses would 3.4% DPT and est. $20,000 in captive OpEx)*

Tolerable assuming a 1 in 5 year event
Tolerable assuming a 1 in 10 year event

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RISKS COMMONLY INSURED BY CAPTIVES

Nearly any risk that is self-insured, carries large deductibles / retentions, is commercially unavailable, or cost prohibitive can be insured in a captive:

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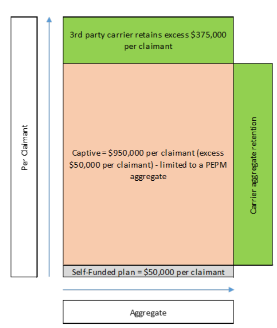
MEDICAL STOP LOSS

Fully insured medical programs, depending on loss experience of the enrollees, may hold an opportunity to capture profit from a carrier. In addition, a fully self-insured program may find itself significantly exposed to the risk of adverse loss experience and / or a single high cost claimant. Because of these factors, there has been an increased utilization of medical stop loss policies – both in and out of captives. However, many of these structures only address risk on an aggregating specific deductible ("ASD") basis attaching at, say, $250,000 per claimant per year. Many structures place the attachment point too low, resulting in capturing a dollar-trading layer – a point at which you know there will be claims but you still pay premiums to a carrier. In response to that, Beecher Carlson has led the market in developing a stop loss structure to address this having a ASD attachment point (higher than typical structures) along with an aggregate stop loss around the insureds retention, creating a pre-defined "worst case scenario" on a per employee per month ("PEPM") basis. The following is an illustrative example of such a structure:

- Self-funded plan retention = $50,000 ASD
- Captive writes reimbursement policy to self-funded plan for risks excess $50,000 ASD
- Captive purchases stop loss excess $1 million ASD and a PEPM aggregate around the $950,000 excess $50,000 ASD layer



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SURETY (REINSURED)

In a surety transaction, your organization pays a fee to the surety who provides a promise to the beneficiary to make them whole in the event you fail to perform. In addition to the fees you pay, you also provide an indemnification and / or a letter of credit to the surety. If you fail to perform, the surety makes the beneficiary whole and turns to you to collect on the letter of credit and / or indemnification – the surety fees do not cover claims.

ILLUSTRATON

	Current	Captive
Surety bond fees	($500,000)	$0
Fronting fee	0	(200,000)
Captive operating expenses	0	(125,000)
Net cost	($500,000)	($325,000)
Payment to surety (rated paper)		$500,000
Carrier retained "fronting" fee		(150,000)
Captive operating expenses		(125,000)
Captive reinsurance premium		$225,000

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