THE PROACTIVE PIVOT

Paul Corver of R&Q identifies the changes the firm has witnessed over the last decade in the run-off space

Captive Review (CR): R&Q has been actively providing solutions to captives for their discontinued business for over 10 years. What has changed in that time?

Paul Cover (PC): R&Q has been actively acquiring liabilities from insurers and reinsurers for almost 30 years and has been the lead run-off acquirer in the captive space for the past 10 years. Early captive deals were generally acquisitions or transfers of business from captives that were no longer utilised. However, over time and as the captive sector has become more aware of the benefits of proactive run-off management, we are undertaking more deals with captives and other self-insurance structures that are actively underwriting: clearing out the 'dead wood' of old years, discontinued classes or perhaps disposed operations and recycling capital to be used for fresh underwriting.

While we still see opportunities to acquire captives that are no longer utilised, there is a clear move to a more proactive state, which mirrors what has been happening in the wider insurance and reinsurance commercial market.

CR: How many transactions has R&Q completed in the past 10 years?

PC: R&Q has completed 95 transactions in all since 2009, 40 of these were with captives and 26 with other self-insurance structures such as RRGs or workers compensation self-insurance trusts. The captive and self-insurance sector is a key market for R&Q.

These transactions have been across 34 different legal or regulatory jurisdictions covering the US, Bermuda & the Caribbean, the UK & Europe as depicted in the charts on page 7.

Paul Corver

Paul Corver is the group head of Legacy M&A at R&Q and has been active in the run-off space for almost 30 years. Aside from managing both solvent and insolvent run-off companies, for the past 10 years he has been actively acquiring portfolios of legacy liabilities for R&Q. These have included acquisitions, LPT's, Part VII and business transfers, novations, mergers and assumptions. Transactions have been concluded in numerous territories and with companies such as Unilever, John Laing, Virgin Atlantic, Clariant, Astra Zeneca, Chubb and Axa LM.

CR: How important is execution risk and reputation of the counterparty for captives disposing of run-off liabilities?

PC: Execution risk and reputation are as important as price in our experience. A track record of closing deals in the relevant jurisdiction in a timely basis and having access to financing are important to sellers. A great price does not mean much if the funding is not there.

For disposals, a seller must be confident that the regulator of their captive will approve a change of control to a buyer. It may be the case that a seller wants a transaction completed within a certain time frame and does not have confidence that a buyer can meet the deadline.

Another key consideration is having the licensing and platforms required for novations, transfers and reinsurance deals.

Reputation and demonstrating a knowledge and operational capability to handle the liabilities being disposed of is important. The liabilities can often relate to the seller's past or present employees or customers and the seller must be confident that the liabilities will be managed appropriately.

CR: R&Q has rated carriers in the US and EU. How important are these for providing the appropriate solution?

PC: R&Q has two A-rated, fully licensed carriers in the EU and US and we have found the ratings to be very impactful to our legacy solutions offerings. There are very few legacy consolidators with rated paper and many corporates and insurers security committees need rated paper in order to transact (re)insurance transactions. We have found that our ratings open up markets that were not previously available to us.

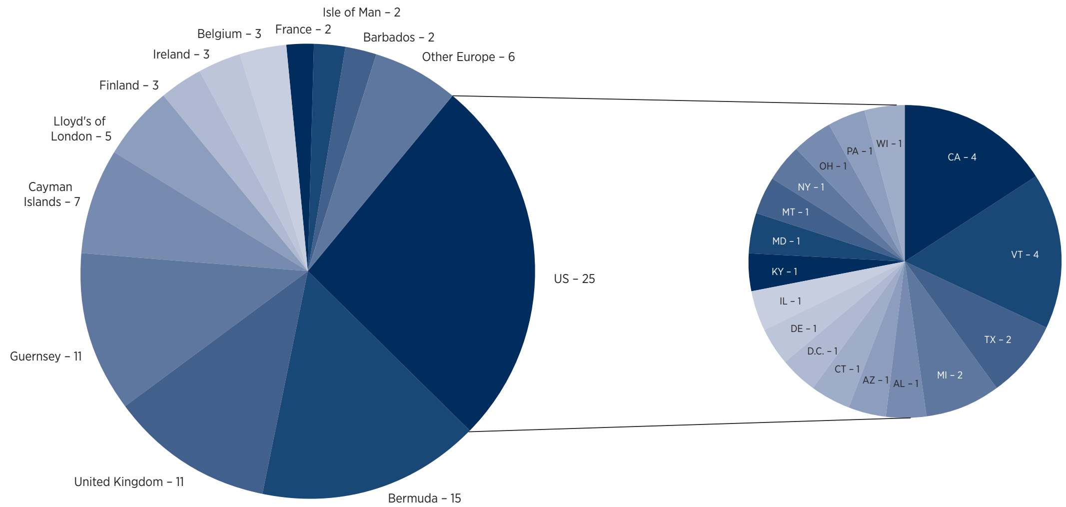
The rating provides an additional market standard that gives potential counterparties greater comfort around the financial strength, leverage, growth, transparency and capital management than unrated consolidators. R&Q have seen that having rated entities can reduce collateral requirements and benefits the cedant with reinsurance credit that comes from transacting with a rated run-off partner.

The ratings are particularly favourable for reinsurance transactions where removing discontinued books, old years or corporate deductibles will give an immediate capital benefit to sellers in addition to removing the cost and associated administrative burden associated with retaining these liabilities.

CR: What type of structures does R&Q now utilise?

PC: A wide variety of structures are utilised to provide the contracting party with the most suitable solution for their requirements. Outright acquisition has been the

CLOSED DEALS BY JURISDICTION, 2009 TO SEPT 30, 2019



Other Europe

Cyprus	1
Denmark	1
Gibraltar	1
Liechtenstein	1
Malta	1
Norway	1

most prevalent and that gives full finality to the captive owner. However, we are now seeing an increase in novations, LPTs and other transfers especially where the contracting party is an active and ongoing entity.

More bespoke structures have been used where rated paper is needed, such as assumption agreements for workers compensation liabilities from a self-insurance trust.

Whether discontinued liabilities are on licensed balance sheets or corporates, R&Q has the breadth of licensing and expertise to deliver legacy solutions that fit its clients' needs, as summarised in the chart below.

CR: Is effective use of run-off restructuring widely recognised in the captive space? If not what are the barriers?

PC: R&Q have completed 66 run-off restructuring transactions with captive insurance companies or other self-insurance vehicles in the past 10 years. The captive sector is becoming far more aware of the benefits of proactive run-off management and disposal.

Captives can be used to retain risk from the corporate parent enabling the group to retain premiums and underwriting profits, receive enhanced insurance terms and gain better access to the global reinsurance markets.

If there are changes in the market conditions and corporate structure or management, this can result in captives seeking run-off solutions as the demand or need for the captive reduces. Additionally, high claims volatility and long-term exposures can also drive desire for run-off solutions.

However, there are challenges in some jurisdictions due to regulatory or market conditions, for example in Luxembourg, captives with large equalisation reserves can be hard to restructure using traditional run-off solutions due to the high levels of tax applied should they be released. This is often an unattractive option for captive owners.

However, the run-off sector has always been innovative, and solutions will be found to address most challenging situations.

CR: With a reported hardening of insurance rates, what can captives do to expand their portfolios?

PC: As rates harden for certain classes, or rates for new exposures such as cyber risk are deemed expensive, there will be attractions for companies to put more of the risk in their captive, especially if they feel they have far stronger risk controls than the sector's average. In order to help finance the addition of new exposures, the captive should review its legacy as disposal of older, maybe long-tail liabilities should free up capital that can be used to support the new generation of underwriting activity. There is little benefit for a captive carrying trapped capital supporting old liabilities when it can use that capital to place more risk into the captive.

CLOSED DEALS BY TYPE, 2009 TO SEPT 30, 2019