Loss Portfolio Transfers & Beyond - Runoff Insurance 101

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What is run off insurance?

Business that is no longer core to strategy

Business that is no longer underwritten and is being wound down

Any discontinued line of business

Companies in runoff want to release trapped capital and achieve finality

Active companies looking to better manage and reallocate capital

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The Global Run-off Market

- Total global non-life runoff reserves of $1.01 trillion:
  - US= $489bn
  - Europe= $344bn
  - Rest of World= $189bn
- Common exposures/risks (US market):
  - Asbestos & Pollution
  - Construction Defect
  - Medical Malpractice
  - Workers' Compensation
    - Black lung

"The legacy market has evolved from its focus on finality and removing underperforming business, to the current trend of facilitating capital relief solutions."

*** PWC Global Insurance Run-off Survey, March 2024**

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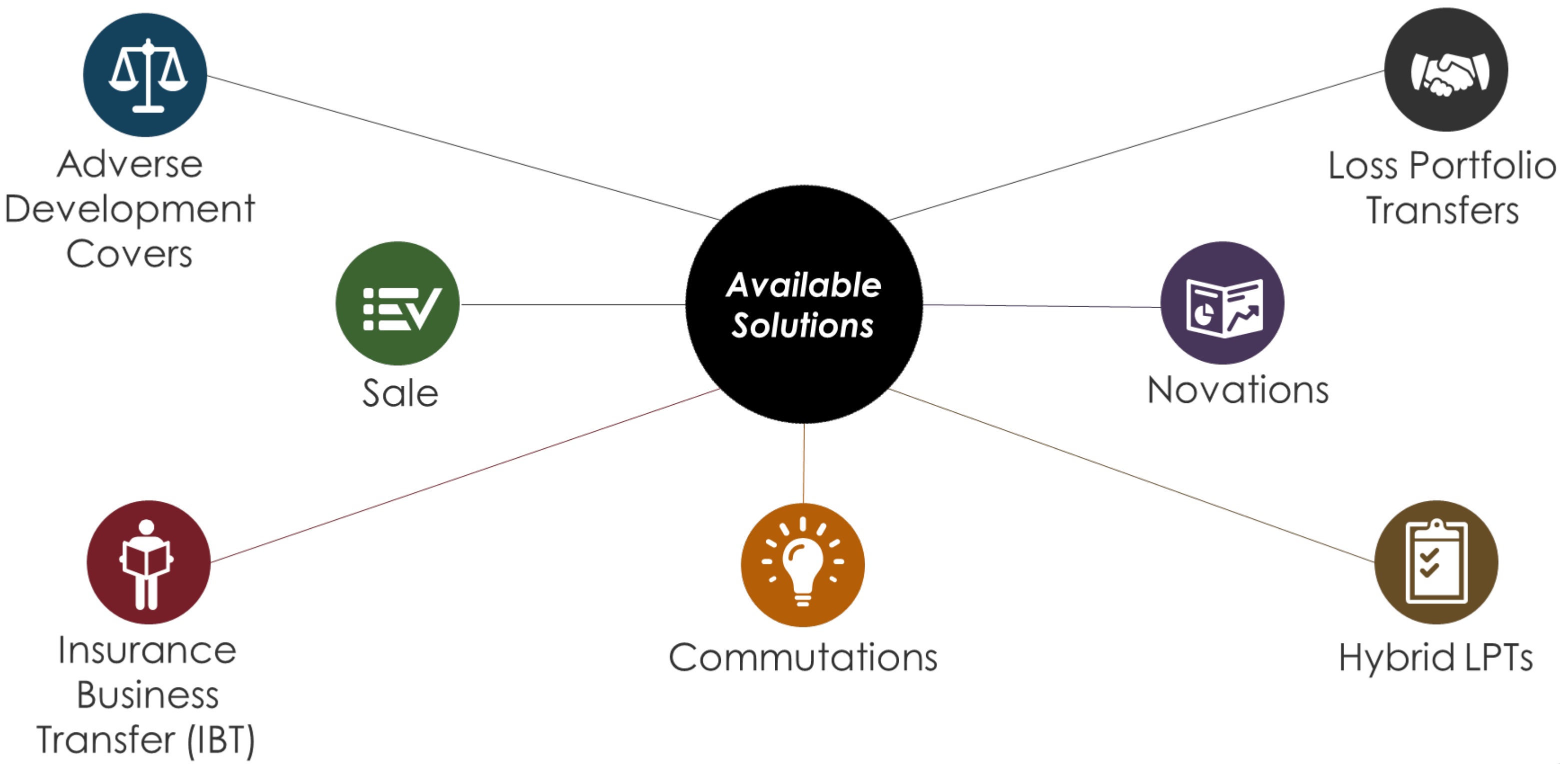
There are a number of types of runoff transactions



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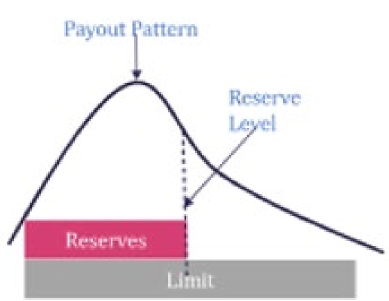
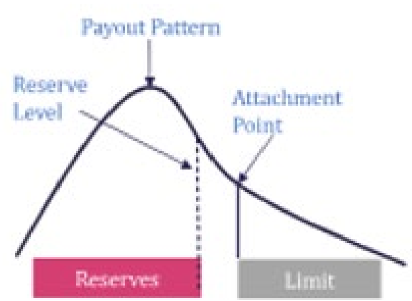
Two Most Popular Transactions

- Any transaction where the risk of existing reserves is transferred from one entity to another.

Loss Portfolio Transfer



Adverse Development Cover



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Deeper Dive into a Legacy Transaction

- Loss Portfolio Transfer: What is it?

  - Reinsurance transaction in which liabilities that are already incurred are ceded to a reinsurer
  - Reinsurance for all known and unknown claims at an agreed point in time
  - Original policy issuer still on risk if reinsurer fails its obligations
  - Transfer all covered case & IBNR reserves for cash and a risk premium
  - Reinsurer may provide collateral for reserves
  - Claims handling can be retained, especially if LPT is less than 100% of reserves
  - Treated as retrospective reinsurance under accounting rules

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Potential Benefits of a Legacy Transaction

- Provide legal or financial finality, depending on nature of transaction
- Provide capital relief
- Increase risk-based capital ratios
- Stabilize Balance Sheet
- Avoid unexpected adverse development on old years
- Allow management to focus on current underwriting and avoid financial and administrative distractions of legacy years
- Release any stacked collateral and restricted assets
- Accounting for retrospective contracts – if reserves improve then deferred gain in retrospective contract is recorded

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How do run off insurers provide all these benefits while still being profitable?

- Efficient claim handling
- Improved investment strategies
- Managing legal expenses
- Capital management

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There are a number of ways to perform a runoff transaction

- Reinsurance broker vs directly approaching known runoff carriers
- Single offer vs competitive bidding
- Offshore segregated cells for unlicensed entities and wealthy accredited investors

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Ethical & Business Considerations Abound

- Post transaction obligations of the ceding company
  - Financial reporting changes
  - IT & Systems
  - Maintaining collateral
  - Claims handling
- Potential legal issues
  - Data breach and/or misuse of customer data at runoff insurer
  - Consumers potentially challenging the legality of claims handling changes being made without their consent
- Ethical considerations
  - Is the existence of runoff insurers ethical if they can potentially profit by proactively lowering settlement amounts of claimants?

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We expect the runoff industry to evolve over time

- Anticipated changes include but are not limited to:
  - Increased use of AI and natural language processing in the due diligence process
  - Continuous transactions with ceding company
  - Partnering with multiple runoff carriers
  - Increasing requests from ceding companies for transactions covering more recent accident years
  - New and unconventional risk exposures

Questions/Contact

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