

# Alternative Risk Transfer in a Challenging Market

## Efficient solutions in a less efficient market

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**TOOLS FOR RISK MANAGERS**

# Agenda

What Is Alternative Risk?

Why Now?

What Key Alternative Risk Transfer Tools Are in the Risk Manager's Toolbox?

- Integrated Risk (IRP)
- Structured Risk
- Parametric Insurance
- Loss Portfolio Transfer (LPT)

Discussion: The Risk Manager's Perspective

- Alyson Buchanan and David Ingram (Lumen Technologies)

# Alternative Risk Essentials in a Challenging Market

## What is alternative risk?

- Nontraditional techniques and products that often involve leveraging an organization's ability to take on risk.
- Typically requires an organization to approach its insurance purchase in a different way, including multiyear purchases, shared aggregate limits, new basis risk, etc.
- Often uses specialized underwriters, "structurers," "deal architects," etc. at specialized insurers.
  - Some insurers may consider alternative risk as a strategic channel for deepening or broadening their relationships with key clients.
  - Some insurers consider alternative risk an attractive means of diversifying their business.
- Surge in demand, primarily driven by dislocation in property and casualty markets, creating opportunity both for insureds and new market entrants.
  - Several MGUs/MGAs have entered the market over the past year, allowing insurers that do not otherwise have the modeling and underwriting skills to access this growing market.

# Alternative Risk Essentials in a Challenging Market

## Why now?

- Challenging pricing and capacity environment means creative solutions can help mitigate pricing increases and capacity limitations.
- Streamline administrative tasks associated with insurance claims and renewals.
- Allow corporates (with or without captives) to share in their risk experience.
  - Take on a controlled amount of risk, while limiting downside.
  - Broaden coverage to traditionally uninsurable risk using parametric products.
- Taking on more risk gives insureds more leverage in negotiation or can allow them to round out programs without being reliant on a challenging market.
- Moving insurers further away from risk can be rewarded with premium savings, creating sustainable solutions for both insurer and insured.

# Alternative Risk Essentials in a Challenging Market

What key alternative risk transfer tools are in the risk manager's toolbox?

- Integrated risk programs (IRP).
- Structured property or structured casualty.
- Parametric.
- Runoff and loss portfolio transfer solutions.
- Captives and RRGs may be considered alternative risk tools, but will not be discussed.

# Integrated Risk Program Concept — Including Basket Aggregate

Annual monoline excess layers	Excess Liability	Excess Property	Excess Cyber	Excess EPL	Excess Professional/E&O	Excess Fiduciary	Excess Crime
Three-year integrated layer	<b>Sublimits</b>						
	Excess liability	\$25M					
	Property	\$25M					
	Cyber	\$25M					
	EPL	\$25M					
	Professional/E&O	\$25M					
	Fiduciary	\$25M					
	Crime	\$25M					
Primary program/SIR	<b>Integrated Program Limits</b>						
	\$25M per occurrence						
	\$50M annual aggregate						
	\$100M three-year term aggregate						
	\$1M GL	\$1M Auto Liability	\$500k Property	\$1M Cyber	\$1M Professional/E&O	\$250k Fiduciary	\$250k Crime
							Optional Basket Aggregate

## Advantages

- Multiple lines of noncancellable coverage with guaranteed rates and terms for three years.
- Potential premium savings of 5% to 20+%; rate guaranteed for three years irrespective of market conditions or losses.
- Coverage for unique or hard to place risks.

## Considerations

- Additional risk retention in the form of shared aggregate eroded by multiple lines of coverage.
- Capacity for these programs limited.

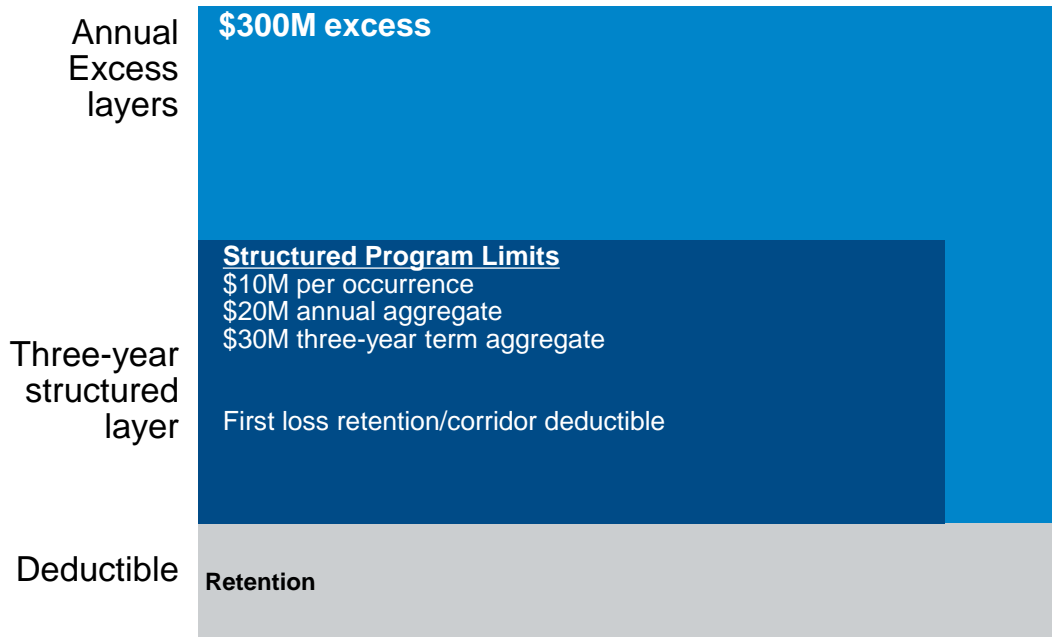
# Structured Risk Concept — Second/Third Loss Cover

## Advantages

- Multiyear capacity guarantees terms/conditions/pricing of structured layer.
- Insured takes on a controlled portion of its exposure (a first loss), while guaranteeing sideways protection against multiple losses.
- Additional features may include return premium/no or low claims bonus.

## Considerations

- Insured retains more risk relative to traditional program.
- Capacity for these programs limited.
- Term aggregate may be insufficient for multiple losses, meaning insured may be “on the hook” upon erosion of policy aggregate.



# Parametric Essentials in a Challenging Market

## What is parametric?

- Coverage triggering from an event or threshold, rather than associated physical damage or losses.
- Traditional insurance focuses on *impact* of event, whereas parametric focuses on *the event* itself.
  - Earthquakes, hurricanes, etc. often result in greater losses to the insured than the simple physical damage and business interruption that most policies indemnify.
- Allows clients to insure exposures where they have an economic interest, but do not have “insurable interest.”
  - Critical nonowned infrastructure, BI/CBI, etc.

## Why are organizations choosing parametric?

- Post-event **claims certainty** — many clients will know the exact value of their parametric payout within hours or days of a major event.
- **Clearly defined coverage** without deductibles or exclusions.
- No claims adjusting process = **claims are paid faster** and with less frustration.
- Event- or index-based triggers allow for **far broader coverage**.
  - No need for physical damage or waiting periods to trigger BI coverage.
  - No need for complex forensic accounting to determine extra expense, lost revenue, etc.
- **Cost** is less speculative, so market forces less determinant.



# Parametric Insurance Comparison

	Traditional Insurance	Parametric	
Trigger	Physical damage or loss	Event occurs or threshold met	A parametric trigger defines the payout scenario
Recovery	Actual losses post-assessment	Pre-agreed amount	Pre-determined recovery for post-event certainty
Basis risk	Exclusions, deductibles, T&Cs	Calculated loss < actual loss	"Basis risk" differs, but is not necessarily greater
Claims process	Long — months to years	Quick — days to weeks	Pays in days; limited or no post-event adjustment
Tenor	Typically one year	Up to 10 years*	Three-year terms for pricing and capacity certainty
Exclusions	Extensive	Limited to none	Simple coverage without deductibles or exclusions
Structure and wording	Standard and rigid	Custom and flexible	Marsh and insurer jointly develop solution
Form	Insurance	Insurance or derivative*	Typically on insurance form, but can be derivative

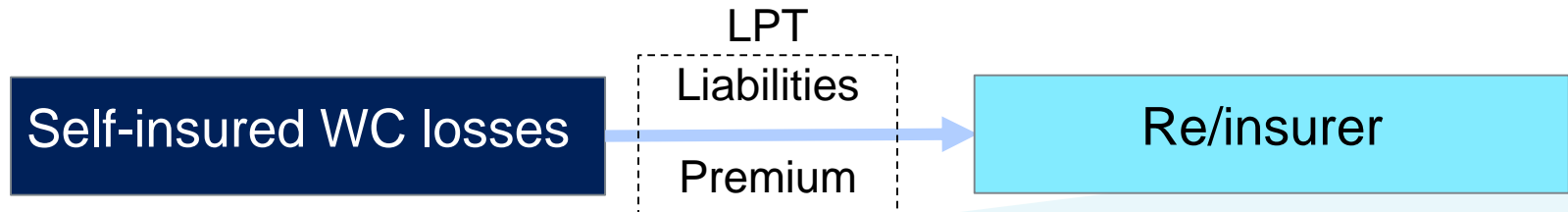
\* Certain terms, such as tenor and form, may be more limited in some jurisdictions.

# Loss Portfolio Transfers

## What is an LPT?

- Package and “sell off” outstanding liabilities; a third party assumes, for a premium, the obligations of historical losses, including projected ultimate net losses and IBNR.
  - Often used to transfer a company’s obligation for long-tailed programs (e.g. deductibles, SIRs, etc.).
  - Typically used for workers’ compensation, general, product, and hospital professional liability.
  - Remove long-tailed liabilities from the balance sheet.
  - Release collateral.
- Example: An organization with self-insured workers’ compensation losses seeks to transfer the risk of this long-tailed liability by ceding the loss portfolio to a re/insurer in exchange for a single premium.

## Sample Program: Large Deductible Program Closeout



# Thank You