WELCOME TO THE PRESENTATION ON

REINSURANCE

WHAT IS REINSURANCE AND WHY IS IT NEEDED?

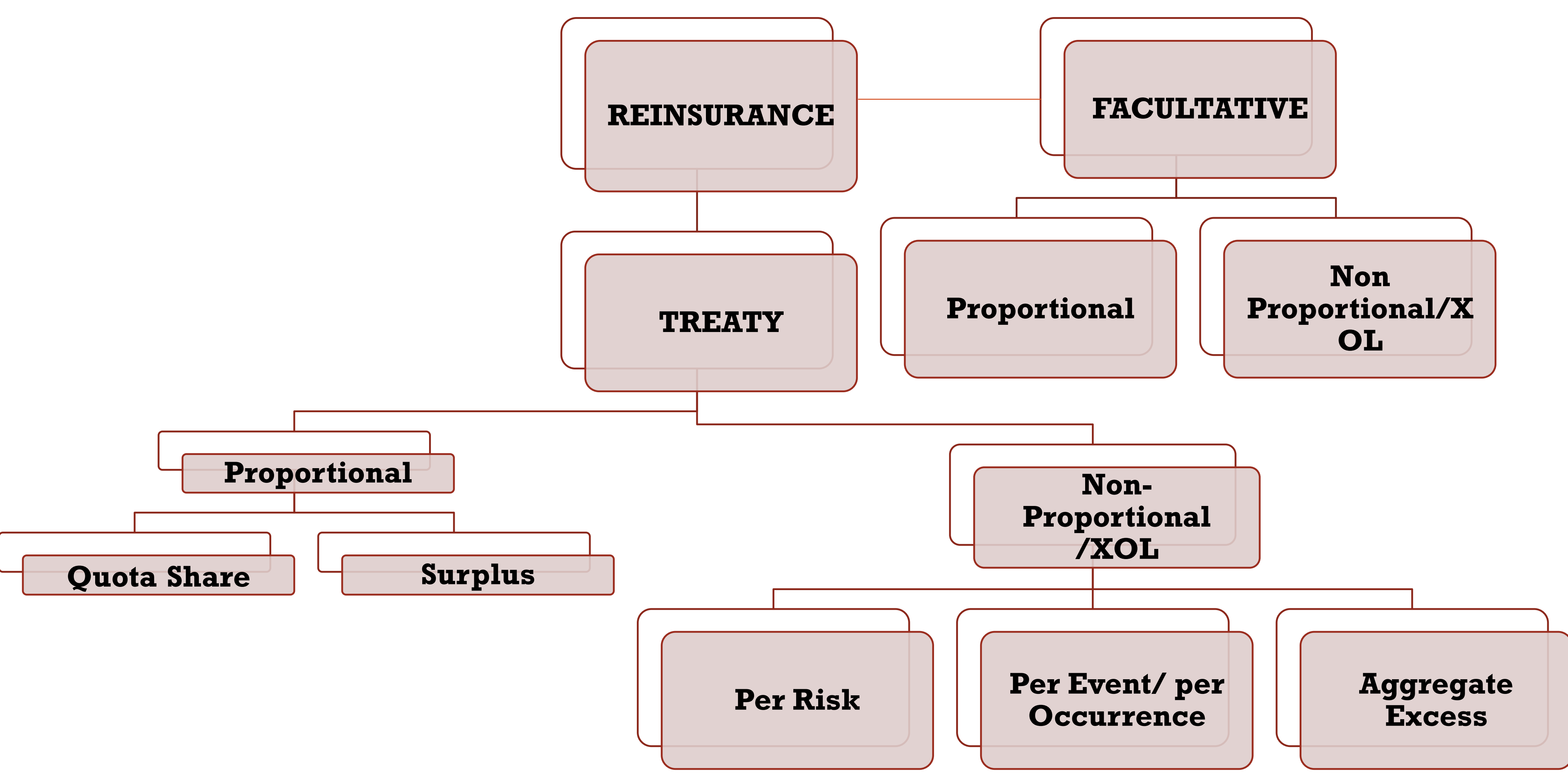
- Reinsurance is insurance of Insurance – Of the risks assumed by the Insurer.
- It is a contract of Indemnity and is independent of the contract with the insured.
- Based on Utmost Good Faith just as in case of Direct insurance.
- Needed to manage risks associated with

a. Catastrophes
b. Accumulation of many losses
c. Lack of Financial Capacity

HOW DOES REINSURANCE HELP AN INSURANCE COMPANY?

- Increases the underwriting capacity of the company thereby enabling the insurer to take the risks which would not have been normally taken.
- Gives financial stability to the insurance company by way of helping recover the major portion of the claims especially in case of catastrophic losses such as the Chennai floods/ Uttarakhand floods/Hudhud cyclone/ cyclone Vardah etc.
- Enables wider spread of risks in many countries enabling a good balance.
- Gives flexibility in the size and types of risks insurer can undertake and thereby increase the volume of business and have profitability.
- Helps accept new and untested risks.
- Gives the expertise on technical, rating, claims handling etc.

FORMS OF REINSURANCE



TREATY REINSURANCE

- Is based on an agreement which is called 'Treaty'.
- Agreement is between the Original Insurer and the Reinsurer.
- Treaty may be on Proportional or Non Proportional basis.
- In Proportional, the Reinsurer automatically accepts a fixed portion of liability for all the risks falling within the scope of the treaty. Under proportional reinsurance, the sum insured, premium and losses if any (irrespective of the size of the loss) are shared proportionately.
- For a treaty, formal wording is usually agreed upon describing the classes of business covered, the territorial scope, exclusions, monetary limits.
- Since this is an automatic cover, the insurance is guaranteed and administrative costs are much lower.
- Proportional treaties are of two types – Quota Share and Surplus treaties
- **Example of Quota Share treaty is obligatory** – where premium and Claims paid are shared in a predetermined Quota with GIC Re - which is now 4% of the Sum Insured (without Cap)

ADVANTAGES OF QUOTA SHARE TREATY

- Is more profitable to the reinsurer and hence he pays more ceding commission.
- Administratively easy to manage
- Very useful for new insurance companies with less capital and reserves since it helps to protect the business till the business grows to a reasonable extent.

EXAMPLES OF OBLIGATORY INSURANCE

Sum Insured Rs	50,000	5,00,000	10,00,00,000
Ceding insurer share Rs.	48,000	4,80,000	9,60,00,000
Reinsurer share 4% Rs.	2,000	20,000	40,00,000
Premium Rs.	500	75,000	25,00,000
Ceding Insurer share Rs.	480	72,000	24,00,000
Reinsurer share 4% Rs.	20	3,000	1,00,000
Claims paid Rs.	45,000	4,00,000	7,00,00,000
Ceding Insurer share Rs.	43,200	3,84,000	6,72,00,000
Reinsurer share 4% Rs.	1,800	16,000	28,00,000

TREATY REINSURANCE – CONTD.

- Another type of Proportional Treaty is the Surplus treaty.
- Here, the original Insurer decides how much of the risk he wants to retain to his own account and cedes the balance(surplus) over his retention.
- Hence the name "SURPLUS" Treaty.
- Premium and losses are shared in the proportion that the insurer's retention and the amount ceded bear to the sum insured of the original insurance.
- The limit of liability which one retains is different for different classes of risks.
- The surplus over and above this retention will be allotted to a set of reinsurers.

TREATY REINSURANCE – CONTD.

- The surplus is stated as either Sum Insured or PML – Probable Maximum Loss
- PML is assessed by the Insurer himself and by ceding on PML basis, more premium is retained by the insurer.
- The amount ceded to the reinsurer under surplus treaty is called "line". A "Line" is equal to the ceding company's retention
- Example: In Fire and Engineering, our surplus treaty is for one line whereas for Burglary, it is for five lines.
- The ceding company (Cedant) can have as many surplus treaties as required.
- Treaty document for surplus cession has all details as required for a treaty document including the method of cession.

EXAMPLE OF SURPLUS TREATY – BURGLARY – TREATY TAKEN FOR FIVE LINES- COMPANY RETENTION RS.5 CRORE PER RISK

Description	Sum Insured	Premium Apportionment	Loss apportionment
	30 crores	3,00,000	15,00,00,000
Retention of ceding insurer	5 crores	50,010	2,50,05,000
Ceded to Surplus treaty	25 crores	2,49,990	12,49,95,000
Percentage ceded (25/30)	83.33%		
Percentage Retained (5/30)	16.67%		

TREATY REINSURANCE – CONTD.

- In some surplus treaties, a 'Bordereaux' is submitted to the reinsurers giving all details of the risks ceded. This is submitted monthly or quarterly.
- The insurer gets a ceding commission on a pre agreed rate from the Reinsurer.
- Ceding commission is given for compensating the insurer for the original commissions and brokerages, Acquisition cost and other expenses.
- Ceding commission rate also depends on whether the treaty is profitable for the Reinsurer. If it is very profitable, profit commission is also given.
- Profit to the treaty = Earned premium – Incurred claims – Ceding commission.

INCEPTION AND TERMINATION OF TREATIES

- Usually Fire and Miscellaneous treaties are on clean cut basis viz. they start and end on a particular pre agreed date. Premium is paid for all the policies underwritten during that period.
- Engineering Treaties are based on Underwriting year and are for a long period.
- Since the treaty comes to an end on a pre agreed date, there may be policies whose period is not yet over, there may be claims which occur just before the period is over.
- To have continued protection, a portion of premium is withdrawn from the existing group of reinsurers and given to the new set. Similarly a portion of the outstanding claims are removed and given to the new set of insurers. This is called Portfolio Entry and Portfolio withdrawal.
- This does not apply to Marine and Aviation insurances.

TREATY REINSURANCE- NON PROPORTIONAL

- In Non Proportional, liability is not in proportion to the premium paid but on loss limits.
- Under these contracts the reinsurer agrees to indemnify the reinsured for losses exceeding a particular monetary limit. Such a limit is called 'Deductible' or 'Excess'
- The reinsured (cedant) has to bear the losses upto the deductible stated
- XL is the short form of Excess of Loss and Xs is the short form of Excess.
- So an arrangement for an agreed limit of 200 crores with a deductible of 50 crores is expressed as 2000000000 Xs 500000000
- The arrangement is made in layers and the participation of the various reinsurers may be on all or chosen layers.

TREATY REINSURANCE- NON PROPORTIONAL

- Here a proportion of premium is not ceded. In contrast, a price is paid as premium, to mitigate a loss beyond the chosen amount of retention/ excess/deductible.
- Hence the name Excess of Loss Insurance or XOL
- Examples of XL – Catastrophic (CAT) XL – covers the losses arising from one event (per event basis) – eg. Chennai Floods, J&K Floods, Hudhud, Mumbai Rains 2005 etc.
- Risk XOL – Covers the loss arising from one single risk – eg. HPCL refinery
- Motor XL – For covering the liability arising out of motor claims exceeding a particular amount.
- Stop Loss – For portfolios like crop- The loss ratio of the ceding company is stopped at an agreed percentage and if in any one calendar accounting year the loss ratio exceeds that percentage, then the reinsurers pay the difference
- Top and Drop Cover – Is a cover which sits on top of all the covers and comes into play when the cover limit is exhausted under any XL cover.

LAYERING IN XOL COVERS

- Layering is a term used to describe the division of XOL protection sought in a number of layers which usually operate consecutively one on top of the other in the event of a heavy loss.
- The first layer is in excess of the deductible and for the subsequent layers, the previous layer is the deductible
- Example – Cover Limit Rs.700 crores – Deductible Rs.50 crores
- Layer 1 – 100 Xs 50, Layer 2 – 200 Xs 150, Layer 3 – 200 Xs 350, Layer 4 -200 Xs 550. Total cover limit is 700 crores. Rate is charged for each layer.

NON-PRPORTIONAL REINSURANCE

200 crs xs 500 crs	IV Layer
200 crs xs 350 crs	III Layer
200 crs xs 150 crs	II Layer
100 crs xs 50 crs	I Layer

50 crs

TOTAL LIMIT 700 crs xs 50 crs

FACULTATIVE REINSURANCE

- The system by which each offer of reinsurance is considered individually by the Reinsurer and either accepted or declined is called Facultative Reinsurance.
- This is usually Policy Specific
- Rates and terms are indicated by the Reinsurer and are to be strictly followed.
- Premium is paid based on the fac support percentage and claims recovered in same percentage.
- This may be on Proportional basis or Non Proportional Basis.
- Advantages of fac:

a. To reinsure Hazardous risks not protected by treaty

b. To reduce the liability of the insurers in certain risks

c. To provide extra capacity

COMMISSION IN REINSURANCE

- Flat rate of Commission:- A flat agreed percentage of commission payable.
- Sliding scale Commission: The rate of commission is based on the loss ratio of the treaty during one treaty year. The loss ratio is calculated as the percentage that incurred claims bear to Earned premium. The table of commission rate corresponding to the loss ratio band is given.
- Overriding Commission- Usually paid in Retrocession inward.
- Profit Commission – It is an additional percentage payable to a ceding insurer on profitable treaties in accordance with an agreed formula.

POOLS AS A MEANS OF REINSURANCE

- A pool is a form of reinsurance arrangement between member companies by which one or more classes of business is pooled and then retroceded to members in an agreed proportion of volume of business ceded.
- Examples – Terrorism Pool, FAIR (Federation of Afro Asian Insurers and Reinsurers)Pool

INWARD REINSURANCE

OBJECTIVES ::

- To increase the gross premium and net retained Premium.
- To achieve a lower expense ratio by the maintenance of volume of premium income.
- To obtain a better and wider spread of business by writing business from overseas.
- To counteract the drain of foreign exchange on account of reinsurance ceded abroad.
- To earn an investment income which may be derived from the cash flow resulting from inward acceptances.
- To act as a window on international reinsurance markets.

TYPES OF INWARD

DIRECT INWARD

- INDIAN INWARD
- FOREIGN INWARD
- ON FAC
- ON TREATY
- ON RETRO

IRDAI REGULATIONS IN RESPECT OF REINSURANE

- Governed by the IRDAI (General Insurance- Reinsurance) Regulations 2016.
- The objectives of Reinsurance as stated in the Regulations are:

a. Maximise retention within the country.
b. Develop adequate capacity
c. Secure the best possible protection for the reinsurance cost incurred
d. Simplify the administration procedures

REGULATIONS – CONTD…

What is contained in the Regulations?

1. Obligatory Cession
2. Reinsurance Programme:

   - Shall commence at the beginning of the year

   - Board Approved Programme will be submitted 45 days before commencement of year to IRDAI

   -Any amendment in RI programme subsequent to filing shall be filed with IRDAI within 30 days of commencement of Financial year
3. RI arrangements in respect of Catastrophe accumulations are adequate.
4. File within 30 days of commencement of financial year copies of all the Lead slips and list of all reinsurers with their shares and ratings
5. Cession Limits

REGULATIONS – CONTD…

6. Order of Preference for cessions
7. Inward Reinsurance Business

The Amendment issued on January 28th 2016 specifies the order in which terms are to be obtained for Reinsurance:

a. Indian Reinsurers
b. Branch offices of Foreign Reinsurers
c. Overseas Reinsurers and Indian Insurers.

COMMON TERMS

- Cede: to give away or transfer all or part of risk to another company or companies.
- Cession: the amount given off by way of reinsurance and therefore accepted by the reinsurers.
- Cedant / ceding company: the original insurer who places reinsurance
- Facultative reinsurance: the system by which each offer of reinsurance is considered individually by the reinsurer and either accepted or declined
- Line: the amount of retention of the direct insurer.
- Reinsurance treaty: an agreement made between the ceding company and the reinsurer under which the former agrees to cede obligatorily a portion of risk upto an agreed limit to the reinsurer, who in turn agrees to accept such cessions.

COMMON TERMS

- Slip: a document showing details of reinsurance proposed to be offered which is circulated to the reinsurers
- Cover limit: the maximum amount for which the reinsurer is liable to the ceding company in the event of loss in excess of the deductible.
- Claims co-operation clause: where the reassured agrees to consult and co-operate with reinsurers on claims handling and settlement.
- Bordereaux: advices of cessions to a treaty, giving details of each cession.
- Pure burning cost: the cost of claims to an excess of loss cover expressed as a percentage of original premium income.
- Loaded burning cost: pure b.C. Is loaded by 100/70 to take care of worsening loss experience, acquisition costs and profit margin.

COMMON TERMS

- Follow the Fortunes: A concept which actually means that the Reinsurer shall "follow the fortunes of the Ceding Insurer in all matters falling under this agreement"
- Hours Clause: The term which limits the time period during which claims resulting from a given occurrence may be included as part of the loss subject to the cover.
- Retrocession: The reinsuring of Reinsurance. It is a separate contract and document from the original Reinsurance agreement.
- Cut through Clause : Any event of insolvent of the Insurer, as per this clause the Reinsurers settle the claim directly to the Insured.
- Ultimate Net Loss : The total liability to the insured less all recoveries under Proportional Insurance.

SURPLUS TREATY STATEMENT OF ACCOUNT

Expenses of Management		Premium due to Reinsurers	
RI Commission		Portfolio Premium Entry	
Claims Paid due from Reinsurers		Portfolio Claims Entry	
Portfolio Premium Withdrawal		Premium Release	
Portfolio Claims Withdrawal			
Premium reserve			

SURPLUS TREATY STATEMENT OF ACCOUNTS

Expenses of Management		Ceded Premium	
Ceding Commission		Cash Call Credit	
Claims Paid		Premium Release	
Premium Reserve		Portfolio Premium Entry	
Portfolio Premium Withdrawal		Portfolio Premium Withdrawal	
Portfolio Claims Withdrawal			
Balance Due to/from			

THANK YOU. ALL THE BEST. QUESTIONS?