Cell captives are the right move

Cell companies simplify captive market entry and exit, says Roundstone Management president **Mike Schroeder**

Briefing

- Cell captives

Insurance is a significant expense for most, and managing its growth and benefit can provide your enterprise with a number of strategic advantages. A captive insurance company is one approach for controlling your insurance costs.

These licensed and regulated insurance companies that are owned by the insured are critical components of most risk management strategies. The reason is the cost and coverage control that captives offer their owners. Whether a captive insurance company is right for you depends upon your particular risk or exposure, the size of your business and the activity or inactivity of the traditional insurance market. Fortunately, the ability to enter or exit the captive market has become a lot easier through cell or segregated account captive companies.

Best providers

Cell or segregated account captive facilities offer the opportunity to quickly and cost-effectively enter the captive market. Captive cell companies provide ready-made management services at a level equal or above the world's most sophisticated insurance enterprises.

The audit, loss reserving, accounting, regulatory and investment management services are established with proven best-of-breed service providers. Efficiency is realised when you are not forced to spend months and thousands on the vendor selection process, and there is no guesswork as to how well or how much an auditor will cost. The numbers and performance are available for your review, with quick and easy reference to the other cell account experience.

Investment management fees and targeted returns are not a surprise, but a recognisable benchmark. Common sense tells us that results improve when you do things more than once. Speak with any captive owner and a common experience is the length of time and difficulty they encounter in finding the right service providers for their captive facility. A cell captive offers performance by service providers who have prevailed in a selection process many times over. The burden and risk of error is assumed by the cell company. Customer satisfaction is not a distant suggestion or hope, it is a repeated fact within the cell company.

Adaptability

Insurance is a regulated business. Like any such business, flexibility and creativity can suffer unless regulation and marketplace ingenuity can find common ground. Cell companies provide the best opportunity for this common ground. Whether it is investment authority, capital and surplus requirements or loss reserve certification, a cell company is able to more quickly adopt the market's latest innovation and still satisfy its regulatory mandate.

It should come as no surprise that the latest insurance capacity crisis in coastal property coverage was met by the creative use of cell companies in what has commonly become known as "sidecars."

Maintaining the solvency of one's insurance programme is everyone's primary objective when entering the self insurance marketplace. This fact does not change with cell captive programmes. It is only managed more effectively through a regulatory scheme that recognises both the capital commitment and experience of the general account or cell company owner.

Because the cell company owner has satisfied a significant capital commitment in order to be licensed as a cell company, the cell owners are able to bootstrap or leverage their business plans to achieve maximum flexibility and creativity with regard to capital and surplus requirements. For example, the cell captive may be fully funded with assets and reinsurance support or, alternatively, traditional tests of insolvency can be applied to meet the regulatory capital and surplus requirements. Both are available capital and surplus strategies and either may prove to be the most effective approach for a cell owner to efficiently manage its risk while maintaining solvency.

The cell company also offers its cell owners financial and administrative advantages through economies of scale. As a regulated insurance company, a captive must satisfy audit, actuarial and regulatory restrictions on investments. These requirements can drive the cost of operating a captive company to a level that contradicts the objective of controlling insurance costs.

A cell company, however, can spread the costs over many cells or captive programmes, providing an economy of scale other captives cannot. Some regulatory schemes provide further cost reduction opportunities for cell captives by relaxing burdensome regulations concerning actuary and auditor reports, in favour of more practical and cost-effective certifications.

In short, the creativity and flexibility applied to your risk management strategy is enhanced in the cell captive environment, where the response to overhead is focused on retaining best-of-breed service providers without concern for runaway expense.

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Cell captives are insurance companies that can respond to your need to establish a risk-bearing facility. The cell captive submits its business plan to the proper regulatory authority prior to the cell owner opening its cell captive programme.

Regulatory authority is not wishful thinking, but pre-approved licence. Speed to market and implementation of the captive solution is unmatched with the cell company. Time is days, not months. Many a grand idea is lost waiting for the wheels of regulation to move in today's marketplace, where change and viable solutions shift 24/7. The cell captive offers you the chance to quickly implement a solution that is structured properly from a capital and insurance management perspective.

Ease of movement

Insurance exposures do not evaporate overnight. Self insurance commitments remain and continue with both expense and loss for many years after an insurance programme is terminated. Cell captives enable their owners to more quickly exit from these legacy costs. This is accomplished by the cell company owner having a very good perspective to quickly make arrangements for the assumption of legacy costs arising from a captive programme it managed over the preceding years.

The cell captive structure is uniquely positioned to facilitate the assumption of legacy expenses such as audit, actuarial and regulatory, as they can be efficiently transferred to the cell owner's general account through expense management for the overall cell company. One less captive programme's audit expense allocation is not a significant assumption of a legacy cost for a cell company to overcome.

Legacy costs related to insurance losses are also best managed by the cell company structure. As mentioned, the sidecar facilities recognise this fact. New investment and risk capital are attracted and accommodated by the ease in which a cell can be opened and closed. Once again, the cell company structure allows the discussion to be about days and weeks, compared with months and years under a standalone captive.

● Mike Schroeder is president of the Roundstone organisation. He has 17 years of insurance industry management experience with responsibilities in the captive market, self-insurance pools and trusts, publicly held insurance companies and the regulatory environment.

Who is Roundstone?

Roundstone Management ("Roundstone"), based in Westlake, Ohio, is an insurance organisation focused on the development, underwriting and servicing of alternative risk products, including captives, rent-a-captives and specialty insurance programmes. Roundstone uses the facilities of Roundstone Insurance, a class 3 Bermuda reinsurer registered as a segregated account company, and Companion Captive Insurance Company, a South Carolina protected cell-sponsored captive insurance company. Roundstone claims to be the only company offering cell company solutions onshore and offshore for both P&C and L&H captive programmes.