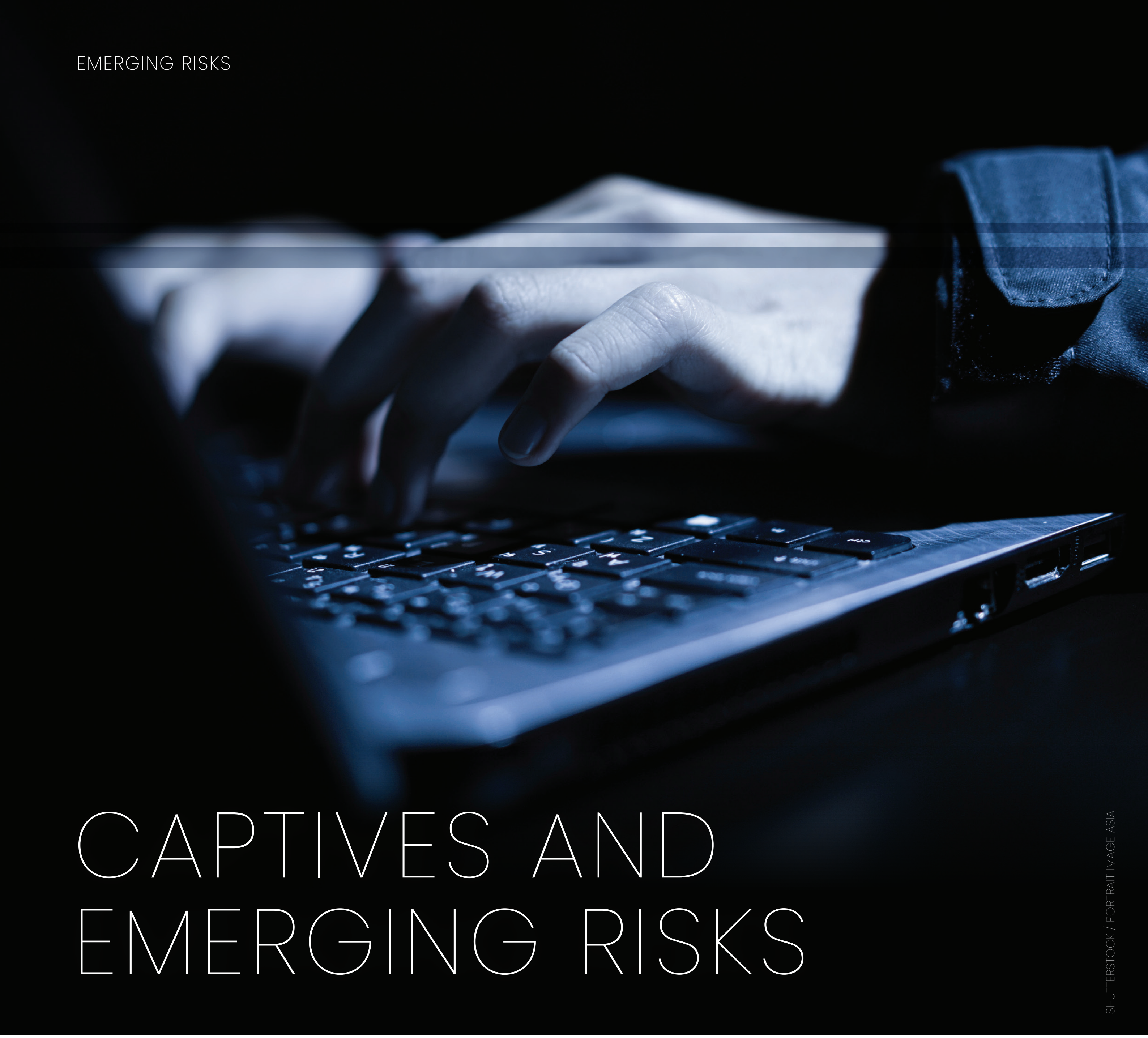

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CAPTIVES AND EMERGING RISKS

A growing number of emerging risks are being written into captives. Four industry leaders discuss how the sector is responding—and what the future will look like.

From marijuana to cryptocurrency, organizations face a rapidly evolving range of emerging risks, and these pose significant insurance and risk management challenges. In many cases, the risks are not yet fully mapped and understood, yet they could have far-reaching consequences for any organization hit with them. That's why many organizations are seeking to address them through their captives.

"If you rewind the clock 15 or 20 years, people entering the captives market were more likely to take a 'dip a toe in the water' approach when forming a captive," says Mike Meehan, principal at Milliman. "They would typically include a single or maybe up to a few traditional lines of coverage, including workers' compensation, general liability, auto liability, etc.

"Today, prospective owners often take a different approach. They tend to come to the market looking to form a captive with more lines of coverage. Many of the captive feasibility analyses that I am involved in consider five or 10 lines of coverage.

"In addition to the more traditional lines of coverage, these analyses will often include cyber liability, medical stop loss, as well as other lines of coverage."

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>
> **STEVE MCELHINEY, ARTEX**

One of the hottest topics is cyber. Lance Abbott, president and chief executive officer of BevCap Management, says this is an evolving and increasingly ominous risk to all business owners.

"We are seeing more and more captives take on cyber," he says. "This allows them to craft the terms and conditions of the policy to respond to the particular cyber risks to which they are exposed."

Meehan agrees that cyber liability, while not necessary an emerging risk, is certainly an evolving risk. "I expect that pandemic-related risks will be a hot topic for the foreseeable future," he adds. "I also envision that cannabis and blockchain related issues will continue to gain more attention."

Abbott predicts developments on the excess auto liability front. He notes that this market has firmed up and many of the reinsurers or fronting companies have become more willing to collaborate with captive owners on increasing the auto layer due to trends in the market.

"Captives that currently have auto liability in their program are looking to increase their retentions since many umbrella markets are no longer willing to attach at a $1 million limit," he says. "Those companies may now consider offering $2 million on the primary policy. This makes them a more favorable risk for the excess markets."

Captives have some distinct advantages over the commercial market when it comes to addressing emerging risks.

"Essentially, a captive can be flexible to fit the specific needs of its owner," says Meehan. "It provides the owner with a risk financing alternative in cases where the traditional market is not willing to provide a solution at a price which is considered cost-effective to the insured.

"As the traditional market experienced a hardening over the past few years, many organizations turned to a captive solution to meet their risk financing needs."

Mikhail Raybshteyn, financial services partner at professional services firm Ernst & Young, says innovation will play an increasingly important role in the future as captives address emerging risks.

"We expect continued innovation in the captive space, especially in the area where insurtechs are getting into the captive space to further their brands and market position," he says.

Steve McElhiney, senior vice president and director of reinsurance at Artex, agrees. He has been a panelist at two CICA events speaking on the application of captives to various emerging risk applications and has been involved with some parametric cat product solutions in recent years with a particular focus on various hurricane events.

"A single parent captive (SPC) is a natural insurance platform to access such products so the recoveries can dovetail into traditional indemnity solutions and fill some gaps that may exist due to reinsurance sub-limits or specific cat retentions," he says.

"In CICA panels we have explored the application of blockchain technology to captives, particularly around issues such as perishables where this new technology will allow global intermodal shipments to be tracked for more efficient risk management and insurance risk transfer.

"Most recently, a CICA panel explored the use of parametric solutions to ensure intangible assets through the use of a captive. Finally, there is a global need for new event cancellation-type solutions given that traditional markets are exiting various communicable disease triggered policies. One global reinsurer is working on such a product that would be a natural fit for a SPC."

CICA closely monitors trends, emerging risks and business needs and addresses these through education sessions at its annual international conference and other educational programs.

"Our education is constantly evolving to help our members prepare to address challenges and leverage new opportunities to strengthen their risk management programs through their captives," Abbott says.

"The CICA conference provides a convenient way for captive owners to meet and interview many service providers in one place to find the resources they need for their captive. My company did this when we started our captive and it worked out very well for us."

As more risks emerge and evolve, Raybshteyn says understanding will be key to addressing them successfully.

"The risks need to be well understood so that appropriate underwriting can take place," he cautions. "Having a risk and such risk being an insurable risk are not one and the same." ●