

GROUP CAPTIVES: INTRODUCTION & OVERVIEW



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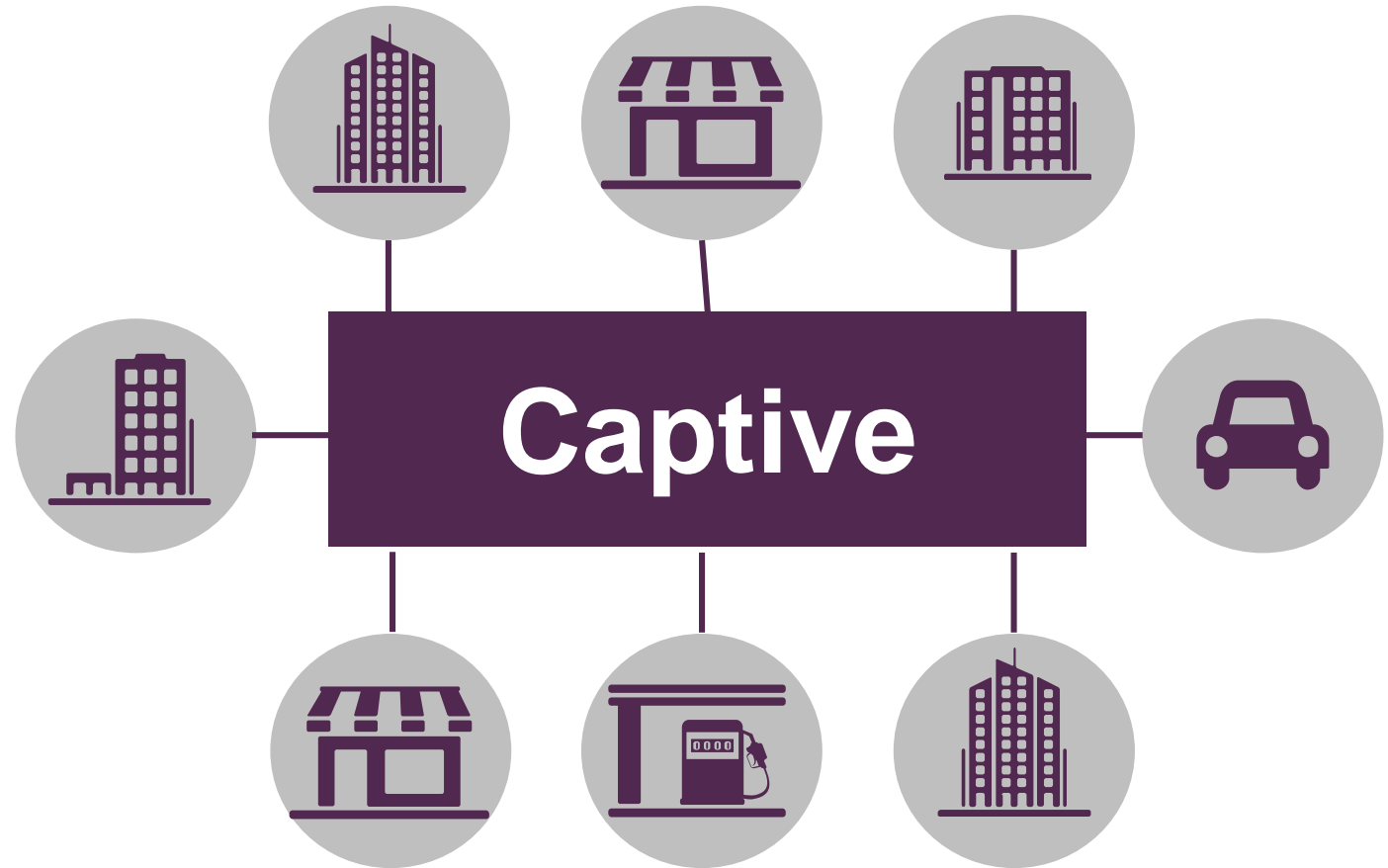
CAYMAN
CAPTIVE
FORUM
2018

GROUP CAPTIVE 101



WHAT IS A GROUP CAPTIVE?

A group of companies that come together to form their own insurance company.



WHY FORM A CAPTIVE?

Words commonly used to describe Insured's current insurance program.



WHY FORM A CAPTIVE?

Control

Control premium costs and improve risk management.

Stability

Find long-term financial stability.

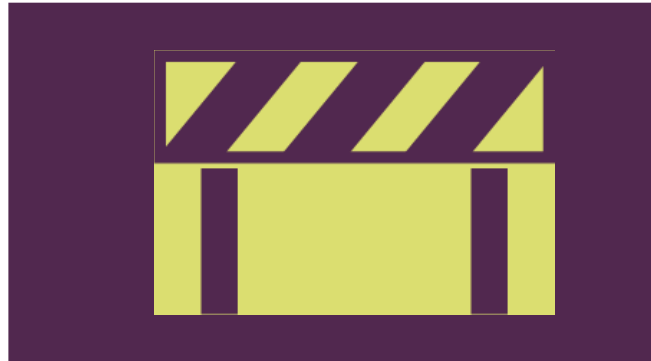
Opportunity

Reap the benefits of premium return and increase safety in workplace.

LINES OF COVERAGE



Workers Compensation

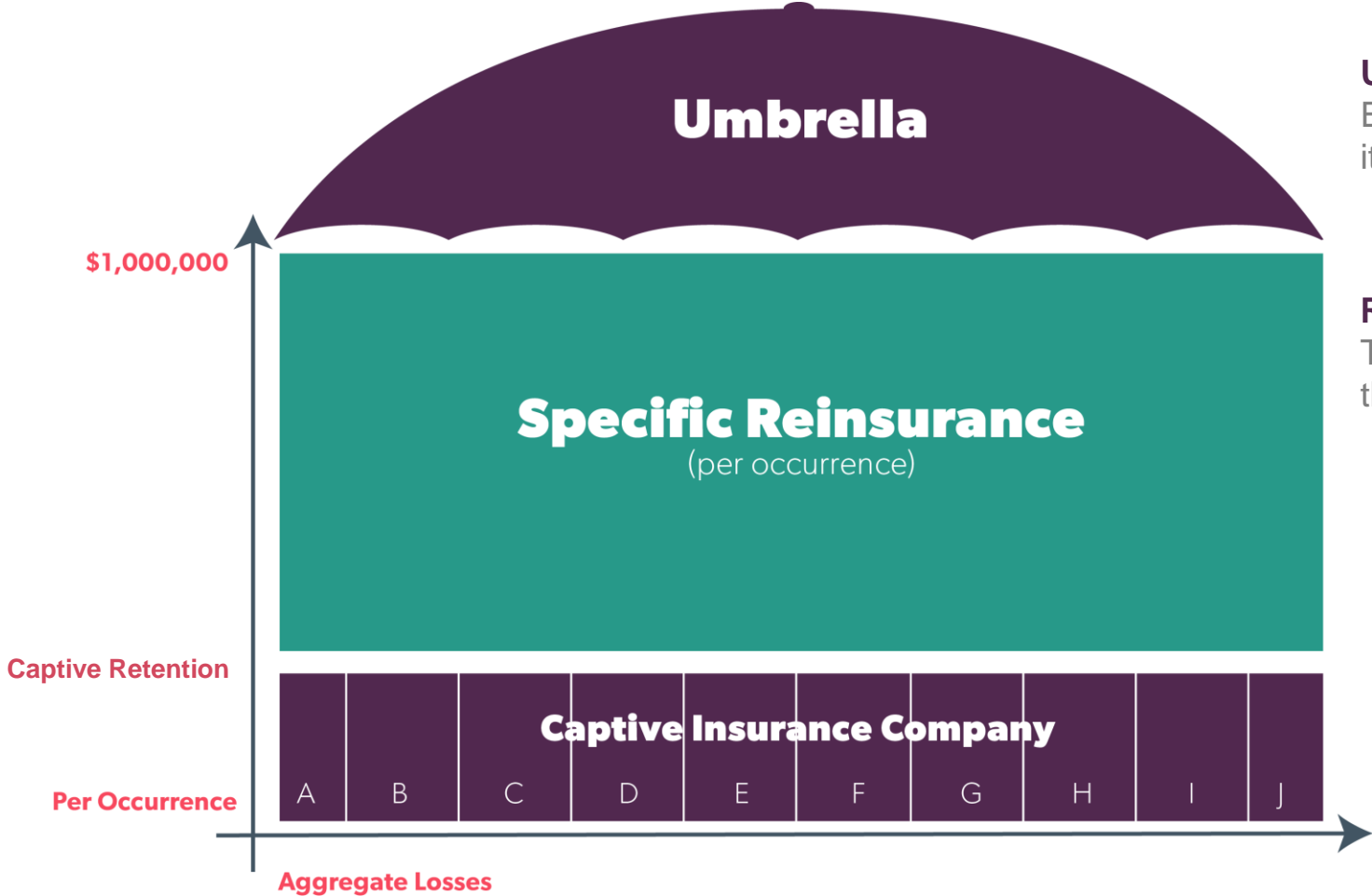


General Liability



**Auto Liability
Auto Physical Damage**

GROUP CAPTIVE PROGRAM STRUCTURE



Umbrella

Each company purchases its own umbrella policy based on its needs outside the captive.

Reinsurance Layer






The captive purchases reinsurance coverage to pass off the catastrophic loss potential.

Captive Layer

Each company has a loss fund to pay its claims. Their premium to the fund is determined by their loss experience and exposures. Money not spent in the loss fund is returned in the future.



THE CONSULTANT'S ROLE - FORMATION

-  Shareholder Insureds/Members
-  Program Insurer (i.e. Fronting Carrier)
-  Domicile Selection
-  Professional Partners
-  Proformas

THE CONSULTANT'S ROLE - ONGOING

Education

- New Members
- Captive Meetings
- Risk Management/
Safety

Partner Liaison

- Program Insurer
- Captive Manager
- Brokers
- Other

Consultant

- Formation
- Ongoing Operations
- Growth
- Strategic Planning



A CAPTIVE STORY

Captive Quick Facts



Founded 2000



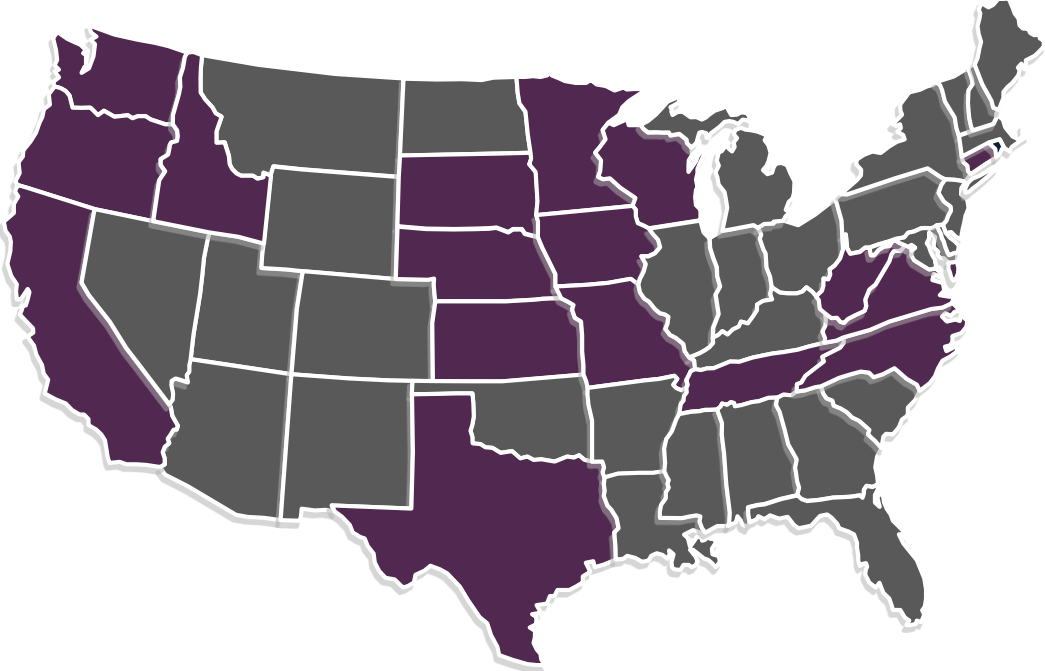
56 Members



\$500k Retention



37% Loss Ratio



Member HQ Locations: 18 States
Exposures: 46 States

Industries Represented



General Contracting



Mechanical



Street & Road



Heavy Construction



Masonry

A MEMBER STORY

Electrical contractor firm with multiple locations throughout the U.S. that joined a heterogeneous ICS captive in 2007.

52%

**WC Premium
Rate Reduction**



32% Growth

**In Payroll From:
2006 - 2016**

35%

**Return on
Premium**



\$1.38 MM

Returned to Date

A MEMBER STORY



Job Pre-Qualification Requirements



Extensive New and Ongoing Training



Risk Planning - Project Managers Analyze Jobs Potential Risk



Management Involvement in Captive and Claims Process



Safety Director Accompanies Employee to Doctor Visits



GROUP CAPTIVE STRUCTURE & OPERATIONS

BASIC REGULATORY REQUIREMENTS

- Cayman captive must be licensed under the Cayman Islands Insurance Law, 2010 and is regulated by the Cayman Islands Monetary Authority (CIMA)
- Typical License category will be a Class B(i) where 95% or more of the insurance program is “related business” by reference to net premiums
- Minimum capital requirement (MCR) and Prescribed Capital requirement (PCR) = \$100,000 for Class B(i) insurer, but CIMA may prescribe higher MCR and PCR



BASIC REGULATORY REQUIREMENTS

- Cayman captive must appoint a local insurance manager who will assist with:
 - The initial license application including the drafting of the business plan and submission to CIMA
 - Continue to act as the liaison between client and CIMA on regulatory matters
 - Assist with the day to day management of the insurance program which must be conducted in accordance with the captive's business plan, the Insurance Law and applicable regulations
- Cayman captive must also appoint a local auditor.



SO HOW DOES A TYPICAL HETEROGENEOUS GROUP CAPTIVE PROGRAM WORK?

- Requirements for admission to Program
- Each member typically issued 1 voting ordinary share and 1 non-voting preference share of the same class
- Voting ordinary share allows for control (vote on appointment and removal of the board) and non-voting preference share allows for economic participation (distribution of profits from successful underwriting and investment income)
- Issue of a different class of shares to each group member allows for separate tracking of financial performance of each member for purposes of calculating dividends, assessments and value of shares on redemption or liquidation.



SO HOW DOES A TYPICAL HETEROGENEOUS GROUP CAPTIVE PROGRAM WORK?

- Issue of a different class of shares to each group member allows for separate tracking of financial performance of each member for purposes of calculating dividends, assessments and value of shares on redemption or liquidation
- Separate “funds” usually created for purposes of the insurance program and tracking of each members performance:
 - Frequency Fund
 - Severity Fund
 - Expense Fund



SO HOW DOES A TYPICAL HETEROGENEOUS GROUP CAPTIVE PROGRAM WORK?

- Bad loss experience may result in an assessment if insufficient funds are available to cover losses
- Collateral in the form of an LOC or cash typically required from each group member
- Good loss experience should result in underwriting profits and increased investment income making distributions of profits possible in accordance with the group's dividend methodology and policies



SO HOW DOES A TYPICAL HETEROGENEOUS GROUP CAPTIVE PROGRAM WORK?

- Control of the Company – who appoints the board?
- Admission of new members
- Voluntary or compulsory redemption
- Calculation of NAV per share on redemption or liquidation
- Annual board and shareholder meetings?



DOCUMENTARY OVERVIEW

- Business Plan
- Memorandum and Articles of Association
- Shareholders Agreement
- Subscription Agreement
- Offering Circular/Disclosure Document



US TAX LAW AND ONSHORE CONSIDERATIONS



ONSHORE CONSIDERATIONS

Group programs typically use a fronting company

- Captive is not licensed as an insurer in any state
- Avoids doing insurance business onshore

GROUP MEMBER INSURED

- Placement/paper looks like an ordinary commercial policy transaction
- Member's constituencies are reassured/not aware of captive relationship



TAX ELECTIONS

- None – Captive can operate offshore and not be a US-income taxpayer
 - Captive is a CFC
 - Members have RPII
 - Captive avoids any US trade or business

or

- Captive may make §953(d) Onshore Election

DISCLOSURE DOCUMENT

- Captive shares may not be securities - - return doesn't arise from the “significant managerial effects of others”
 - Loss Experience
 - Participation in Governance



DISCLOSURE DOCUMENT

- If particular terms of a Program's structure make the ownership interests in the captive securities, they will typically be exempt from registration provided the accredited investor test is met
- Whether exempt securities or not securities, disclosure document is provided

DISCLOSURE DOCUMENT

- Explains Complex Program
- Forces up-front decisions on program parameters
- Puts everything in writing
- Provides tax, risk and other disclosures to protect the group

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THANK YOU



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