



RM-7 LOSS PORTFOLIO TRANSFERS AND ADVERSE DEVELOPMENT COVERS AS RISK MANAGEMENT TOOLS

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KEY CONSIDERATIONS OF LPT/ADC

- View of required reserve
- Reserve range
- Scenarios
- Payment pattern
- Booked impact vs economic impact
- Value to communicate to outside parties
- Unique setup
- Commutation provision
- Profit share provision
- Claims handling
- Benefit/Cost
- Monitoring/Reporting requirements

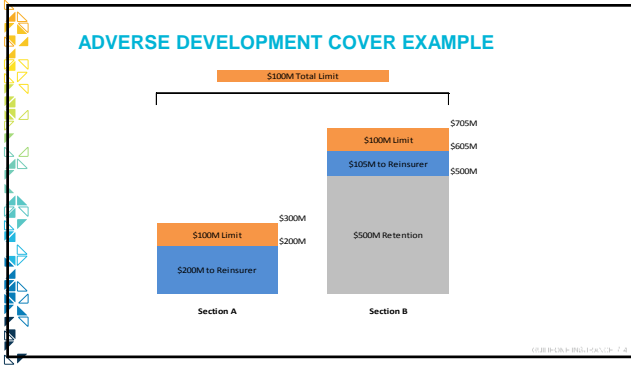
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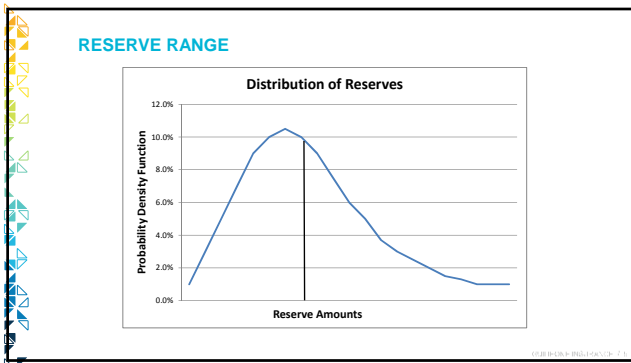


REQUIRED RESERVE

- Assumptions underlying reserve estimate
- Varying reserve estimates
- Review of paid and incurred patterns
- Review of case reserves
- View of claims management
- View of settlement pattern
- View of detailed characteristics of underlying open claims

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SCENARIOS - ASSUMING MAX SECTION A RECOVERY AND SECTION B RECOVERY VARIES

	1 (Section B - Dev 10% Fav)	2 (Section B - No Dev)	3 (Section B - Dev 10% Adv)
Upfront Cost	200+105+305M	200+105+305M	200+105+305M
Section A Recovery	200+100+300M	200+100+300M	200+100+300M
Section A NPV Recovery	280M	280M	280M
Section B Recovery	45M	105M	105M
Section B Loss Investment Income	-22M	-42M	-30M
Section B NPV Recovery	23M	63M	75M
Total Recovery	300+45+145M	300+105+405M	300+105+405M
Total NPV	-2M	38M	50M

SCENARIOS - ASSUMING SECTION A \$30M ADVERSE AND SECTION B RECOVERY VARIES

	1 (Section B - Dev 10% Fav)	2 (Section B - No Dev)	3 (Section B - Dev 10% Adv)
Upfront Cost	200+105=305M	200+105=305M	200+105=305M
Section A Recovery	200+30=230M	200+30=230M	200+30=230M
Section A NPV Recovery	215M	215M	215M
Section B Recovery	45M	105M	166M
Section B Loss Investment Income	-22M	-42M	-57M
Section B NPV Recovery	23M	63M	109M
Total Recovery	230+45=275M	230+105=335M	230+166=396M
Total NPV	-67M	-27M	19M

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SCENARIOS - ASSUMING SECTION A \$30M FAVORABLE AND SECTION B RECOVERY VARIES

	1 (Section B - Dev 10% Fav)	2 (Section B - No Dev)	3 (Section B - Dev 10% Adv)
Upfront Cost	200+105=305M	200+105=305M	200+105=305M
Section A Recovery	200+30=170M	200+30=170M	200+30=170M
Section A NPV Recovery	160M	160M	160M
Section B Recovery	45M	105M	166M
Section B Loss Investment Income	-22M	-42M	-57M
Section B NPV Recovery	23M	63M	109M
Total Recovery	170+45=215M	170+105=275M	170+166=336M
Total NPV	-122M	-82M	-36M

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INVESTMENT INCOME

- Difference in investment yield
- Difference in investment assets
- Difference in risk tolerance on investments

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PAYMENT PATTERN

- Sensitive to the total reserve
- Varies significantly due to mix of business

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BOOKED IMPACT VS ECONOMIC IMPACT

- Possible to setup a revenue neutral adverse development cover
- Paid for through future investment income

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OUTSIDE COMMUNICATION

- Value in communication to outside parties such as AM Best
- Value from a management or board perspective
- Perception that the company has fully exited

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UNIQUE SETUP

- Adverse development cover can be tailor made to individual company
- Modifications can be made to protect certain lines of business or accident years
- Flexibility can be included in how the cost of risk transfer is paid

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COMMUTATION PROVISION

- A commutation provision can be included
- Can give the option to commute the contract at specified times with certain provisions
- Depending on the contract the adverse development cover may be in place for a long period of time without a commutation.

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PROFIT SHARE PROVISION

- A profit share provision can be included
- Can be included to allow a portion of potential favorable development to be retained

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CLAIMS HANDLING

- Who handles the claims?
- Monitoring change in case reserves, paid loss, open claims
- Pending open claims per adjuster
- Incentive to close claims?
- Oversight of claims handling

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BENEFITS/COST

- Benefit – Transfer adverse development risk up to limit
- Cost – No longer receive investment income on transferred reserves
- Cost – No longer retain benefit of favorable development before a limit
- Cost – Recovery subject to credit risk of the reinsurer

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MONITORING/REPORTING REQUIREMENT

- Reinsurer will likely require various levels of reporting
- Transfer of funds as payments are made
- Does LPT/ADC correspond with reserve review splits

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