DISRUPTION IN THE CAPTIVE INSURANCE SPACE

Sandra Duncan and Nick Hentges, of Captive Resources, discuss the dramatic rate of growth in the group captive insurance marketplace, and the factors which have been informing its success

Captive Review (CR): Captive Resources' client group captives continue to grow significantly. Is the growth coming from new formations or expanding portfolios?

Nick Hentges (NH): We have seen growth in both of these areas, having successfully formed several new captives over the past 5-6 years. In addition, we're dramatically growing existing captives organically, by adding new members.

Sandra Duncan (SD): Also, we've helped some of the larger, more mature captives to manage growth by developing minimum size parameters for new members. Consequently, there was a need for new captives, to accept smaller new members.

NH: There's been a movement towards increasing the minimum premium of the mature captives. For example, a former minimum premium of $150,000 for all three lines is now being increased to $400-500,000; a second programme is then implemented and smaller members are placed into this.

We recommended this strategy because some of the mature captives were reaching a size of over 250 members. They still want to grow, but logistically, it becomes more difficult and begins to impose limits. This is more of a logistical than premium situation – a case of being able to effectively service and manage the members while offshore at Board meetings.

Sandra Duncan

Sandra Duncan, MBA, ARM is senior vice president at Captive Resources, LLC. Duncan has 30 years' experience, specialising in alternative risk structures, including captives. She has previously held senior reinsurance and management consulting positions at Alea North America and Willis Towers Watson. At Captive Resources, she has responsibility for captive operations quality review and oversees marketing communications.

Nick Hentges

Nick Hentges, MBA, CIC is president and principal of Captive Resources, LLC. Hentges has held management positions in underwriting and marketing with CIGNA, and specialised in association programmes for a large broker. He has general oversight for the day to day services provided by Captive Resources to its captive clients, and also oversees all production and administration representatives.

CR: What specific sectors do you believe remain untapped by the group captive concept, and if so why do you think that is?

SD: In the past, any business with very high risk and severity would typically not have been a good fit for our group captive model. Our model is frequency driven. This remains unchanged and we continue working to develop captive options for industries that we believe are going to be a good fit in this regard.

However, within the past 4-5 years, we've been working to form group captives in somewhat more difficult industries, seeking out the most well-managed, best-in-class entities. These include the temporary staffing industry for certain classes of business such as industrial, agriculture, construction, and energy; heavy construction; and oil drilling and related service operations – all of which come with heavier risks.

CR: Are there some classes not viable for the group captive concept?

NH: There are – completely severity – driven classes, as work-comp is usually the driver in these captives. If there isn't a frequency to it, that's not something we're going to be interested in.

Even for tough construction, for example, our newest captive for heavy construction – which includes steel erectors and bridge painters – we're looking for companies that are best in class and have well developed risk management programmes. Essentially, we're not interested in classes that we don't think we can help to mitigate

risk through risk control or claims management practices.

CR: What are the main reasons for domiciling all of your group captives in Cayman?

NH: The Cayman Islands offers all the necessary banking, accounting, legal and captive management services. The availability of qualified, experienced service providers is of the utmost importance. This, along with a knowledgeable, flexible and amenable regulatory body in CIMA, makes the domicile a great place to do business.

SD: Also, with particular regard to group captives, a domicile must be reasonably accessible. With hundreds of captive members attending Board meetings, you need accessibility and a hotel and tourism industry able to handle meetings of that size. Grand Cayman certainly meets the captives' needs in this respect.

CR: How has the group captive industry evolved in recent years?

SD: Fundamentally, the group captive industry doesn't change much. We view this as a positive because new problems or changes in regulation and legislature seldom arise.

As we work with such a large percentage of the group captive industry, we feel that Captive Resources has been a real disruptor in the insurance industry – not just the captive insurance industry. To date, nearly 4000 middle market companies that used to be in the traditional market have migrated to group captive insurance – and they're no longer being lured back by a soft market.

The captives have retained 98% of members every year, the remaining 2% are leaving mainly because of mergers and acquisitions. And we believe the current number of members represent only a fraction of the universe of middle market companies that could potentially be a good fit for a group captive.

We also see that this migration from traditional insurance continues at a much faster pace than previously. The total premium volume across all of our captive clients has doubled in the past 4.5 years. The middle market no longer views group captives as "alternative": they're a powerful, all-encompassing option in their own right, and 4,000 companies and $2bn in premium is significant market change.

NH: Allow me to put this into perspective: Captive Resources has been doing what we do for more than 30 years. It took 25 years to reach $1bn in premium, and just over another four years to reach $2bn. The pace of growth is increasing very rapidly. One of the key reasons for this is education. We see ourselves as educators. We educate brokers on why it makes sense to put their clients into a group captive; prospective clients as to why it makes sense for them to join one; and we educate our clients about how to run their own captive insurance company.

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Past barriers and concerns have been broken down and mid-size companies are now very comfortable with this concept.

CR: What are some of these misconceptions that have traditionally kept people away from the group captive structure?

NH: Originally there was the notion that if you got into a group captive, it would be difficult to get out; but that's not the case. We close policy years. Some captives close at around 4-5 years, but some between 7-8 years. There is a timeframe, but you can exit.

I've also heard it said that once you join a captive, you have no say, which is simply not true. As consultant to the captive, we provide assistance and support, and make recommendations, but the members run the captive and make the decisions as to how the captive will operate.

Another deterrent is around collateral. We use a formula-driven approach to building collateral, and after three years, collateral is well established and will not continue to mount as in some other captives.

SD: In the past, I think potential members were also concerned that they would somehow be putting their company at risk. However, the captives are protected by both specific and aggregate reinsurance. Posted collateral also serves to protect members.

Also, prospective members have been concerned that they couldn't retain a relationship with their agent or broker, but nothing could be further from the truth. We don't sell captive insurance – the group captive concept is introduced and conveyed by members' agents and brokers, who remain involved in essentially the same capacity as previously.

Specifically with regard to our group captive model, I think there's a further misconception that these captives are 'ours'; they are not. We have no ownership position in any of the captives, nor do we want any. Our relationship with the captives is primarily consultative.

NH: Now that the middle market is more fully aware of the value of group captives, we believe there is a tremendous opportunity for growth. We are going to have a further impact on not only the group captive insurance industry, but the insurance marketplace, because of the number of companies that are now hearing about the group captive option, embracing its many advantages, and choosing to become captive insurance company owners.