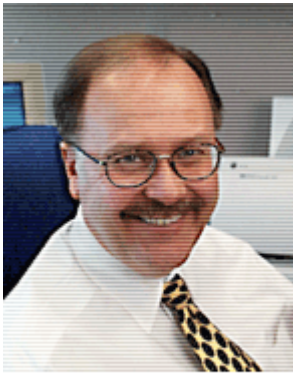


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Why A Life Reinsurance Intermediary?



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The life and annuity industry has changed significantly in the past 20 years. There have been dramatic changes in product, in technology, in process, and perhaps most evident, in distribution. In addition, there has been significant consolidation, and the re-identification of the industry from insurance to financial service entities.

One thing that has seen little change is the way in which life and annuity companies obtain one of their most important and, in many circumstances, most costly needs --reinsurance. Reinsurance plays a large part in a primary company's ability to write risk, and increasingly in their ability to manage capital efficiently and effectively. Reinsurance is the 'silent partner' that allows companies to effectively control risk exposure, while enabling them to write relatively large risks so as to better serve producers and policyholders.

Traditionally, in the life and annuity business, reinsurance selling has been accomplished through an employee of the reinsuring entity, while the buying decision has been made by a number of different disciplines. In today's environment, however, it is generally the actuary who has the buying responsibility. In past years, and in many organisations, the chief underwriting officer was usually the buyer, but that has not been the case in most circumstances for 20 years or so. One of the reasons why there has been a general consolidation of reinsurance buying to the actuary level has been the increasing attention to the cost of reinsurance. This cost factor has become critical in an environment where first dollar quota share and products designed using low-cost reinsurance have become essential benchmarks of competition.

Interestingly, while the price-sensitive competition on the primary side of the business has led to independent marketing to the consumer, reinsurance buying has not reacted in the same way. This is only true on the life side of the business, as perhaps 60% of the world's property and casualty reinsurance premiums are placed through this distribution method in a very efficient manner.

In the life reinsurance business, the intermediaries' involvement has been, for the most part, confined to the group, catastrophe, and to some degree the financial areas. Why has this been? Is there a reason in today's environment to consider the value an intermediary can bring to the individual life side as well? This article examines that premise and answers the question: "Why a life reinsurance intermediary?"

Those of us who have been in the business for many years remember the days of the captive agent. The captive agent was an individual who represented one company, who had one selection of products, and who served his customer within a narrowly defined scope of choice. They had only one company to offer and only one portfolio with which to satisfy the protection and asset accumulation

needs of their clients. This producer had to find a way to make the client's needs 'fit' into that narrow product offering line, or lose the sale.

In the 1970s, and accelerating in the 1980s, independent or 'brokerage' distribution grew rapidly in the US. It provided the producer with the opportunity to serve the client by providing the freedom and ability to offer a number of providers and portfolios to best suit the client's needs. The producer could provide a blend of products from different companies to satisfy the varied needs of the insured. In many ways, it cut the umbilical cord that had kept the agent completely tied to the 'mother' company.

This migration of distribution from 'captive' to 'independent' played a significant role in the growth and profitability of many entities during the 1980s and 1990s. In fact, many captive-only companies spent a great deal of their resources developing independent distribution systems. One of the major marketing challenges of the 1990s proved to be effective management of a multiple distribution system.

What has this change in distribution meant to the end consumer of insurance products -- the insured? From my perspective, it has meant wider choice, lower price, more analytical planning and advice, and better overall value for the consumer.

Lower cost implications

What has it meant to insurers? Again, from my perspective, it has meant lower costs, better spread of risk and the need to fine-tune products, services and compensation to meet the competition. What's more, the lower distribution costs have in many circumstances been used to enhance services and products -- all in all a win/win situation for those involved in the process from producer to company to insured.

Now that we have seen how effective independent distribution has become on the primary side of the business, let's reflect on the impact it can have on the decision-making and procurement process for reinsurance.

Traditionally, life reinsurance has been sold direct, with the reinsurer's employees selling and servicing the cedant's business. While it is accepted that the reinsurance marketer represents both the buyer and the seller of reinsurance, their compensation and career growth is dependent upon the seller only.

While this 'direct' distribution method has served the seller well for many years, there is a question mark as to whether it is the most effective means for a buyer to procure reinsurance. Does it provide the buyer with objective counsel on such issues as structure or the use of offshore entities? Does it provide the buyer with the broadest view with respect to capacity or potential risk concentration issues? In many instances, it does not.

Without a third-party representative in the transaction, buyers of reinsurance are left to negotiate and structure contracts that are not necessarily in their area of expertise. Why isn't there a buyer advocate acting as an independent third-party intermediary? The importance of this advocacy is recognized in many other commercial transactions, from real estate to stock brokerage to the attorney representing their clients.

Today's life insurance marketplace is becoming more complex, more sophisticated. The role of the actuary is expanding. New, more intricate mortality tables demand a great deal of time for modifying products and reserving methodologies, and with that there comes an increasing pressure industry-wide on reducing expenses. In light of all this, 'outsourcing' the reinsurance buying process makes good sense.

Buying made simple

For the ceding company, the process is simple. Rather than dealing with numerous marketing people and countless actuaries and underwriters from different companies during the quoting process, the buyer at the ceding company deals with one group of people, the account team at an intermediary.

These specialists work only for the buyer and can strategise, counsel, model and work closely with the primary company to create a reinsurance structure that is effective and economically advantageous -- to the buyer.

Many don't leverage the significant role an intermediary can play in the very beginning of the product development and reinsurance strategy-setting process. It is increasingly important in an environment where reinsurance structure and price play such a critical role in primary company pricing strategies and profit assumptions. With corporate and product pricing goals and objectives clearly defined, the intermediary can deliver appropriate product offerings from an entire industry in order to achieve those goals, rather than just the offerings of a single company.

The intermediary can be just as critical in the increasingly important discipline of capital management. It is said that the life industry is just now catching up with some of these techniques, many of which have been used in the property/casualty industry for a number of years. It is critical that life insurers pay close attention to their surplus and capital management strategies, particularly following the significant asset decline caused by market conditions of the past several years. Financial reinsurance can help attenuate the strain associated with new business writings or increase surplus levels to meet regulatory requirements. From techniques such as traditional surplus relief transactions to increasing risk based capital (RBC) levels, it can be an important ancillary tool in tax planning and in the financial support of significant corporate initiatives.

One of the newest of these techniques is 'securitisation'. Although securitisation is not popular as yet on the life side, it is, nonetheless, a technique that may increase in popularity if life reinsurance price and capacity change. Most intermediaries are intimately familiar with this and other alternative risk transfer (ART) methodologies, as they have been involved in them in the p/c sector for some time. With ART and financial reinsurance, reinsurance intermediaries provide two specific value-added services:

- the individual representing you in these transactions has your needs, your structural preferences, and above all, your organisation's strategic objectives uppermost in their mind in the market selection and negotiation process; and
- your representative has available a wide range of potential markets, both domestic and offshore with which to place your business.

One source insufficiency

One source is simply not going to do the job. In effect, the intermediary brings broad knowledge, intelligence, capabilities and resources to the table in order to create the best possible risk transfer mechanism and/or capital management program for the buying company.

Perhaps the best example of the value one can derive from the intermediary system has come about as a result of September 11. Life companies have traditionally used an intermediary in the procurement of life catastrophe protection. Never has the need for cat cover, nor the risk of concentrations, been more prevalent than at present. Unfortunately, after the losses of September 11, many of the traditional markets for life catastrophe reinsurance exited the business. It was only through the hard work of intermediaries that the market was put back together. Brokers worked diligently with life and non-life markets to create capacity where none existed before. Out of necessity, capacity has been reduced, restrictions have been added, and prices increased to reflect what have come to be the facts of life about concentration risk.

Intermediaries are focused, knowledgeable, and have the worldwide resources to get the job done. Just as this has become evident in the catastrophe reinsurance line, it will become evident in other areas of the life and annuity sector as well.

We have concentrated, so far, primarily on the value of reinsurance intermediaries to the ceding company. How about the benefits to the reinsurer? There are several, not least the fact that the truly

professional intermediary does a comprehensive job of selecting the appropriate market for a particular piece of business, and then diligently preparing a comprehensive submission so that the reinsurers have a well-prepared package of information with which to work. In addition, at a time when reinsurers are eliminating their marketing staff, the intermediary can bring them business from companies that they would otherwise not have time to call on. It is also worth mentioning that the reinsurer incurs no marketing cost unless they actually book the business. This variable marketing expense can be a very cost-effective method of distribution, particularly when reinsurance prices are soft and marketing budgets are being cut.

What is the message? Just as the face of life insurance and annuity distribution to the consumer has changed dramatically in the past 20 years, so will the face of life reinsurance distribution. Life reinsurance buyers have a partner in their professional life reinsurance intermediary, a partner who can put new tools in hand, help navigate the choices in today's reinsurance market, and maximise the effectiveness of negotiating customised reinsurance solutions.

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