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Health Insurance:

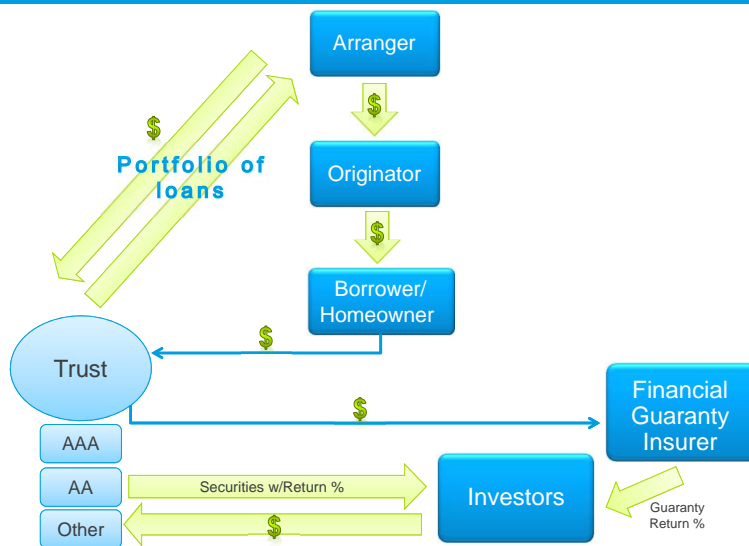
Reinsurance as an Alternative Capital Market Funding Solution in Health Insurance Securitizations

Steve Najjar, Executive Vice President
Hannover Life Reassurance Company of America

17th East Asian Actuarial Conference
Singapore, October 19, 2013

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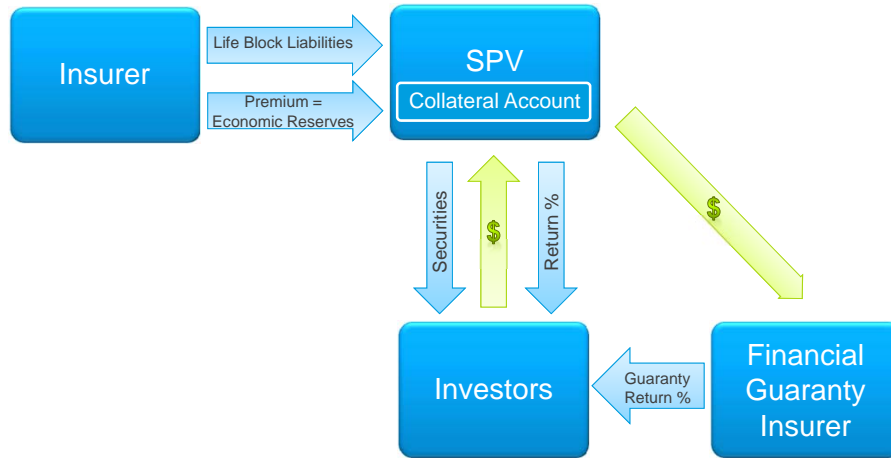
Typical Real Estate Securitization



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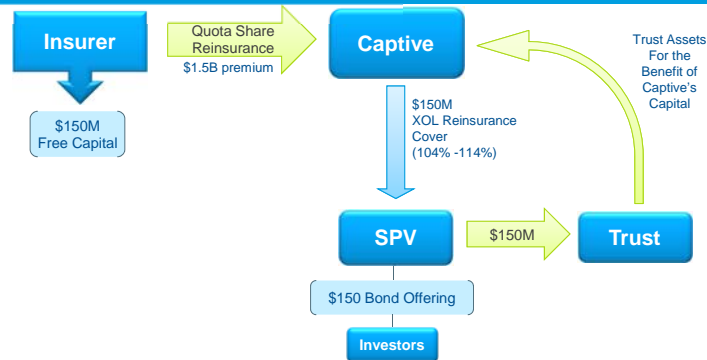
Typical Life Insurance Securitization



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Capital Markets Solution ILS Structure (Funded Solution – A Tranche)



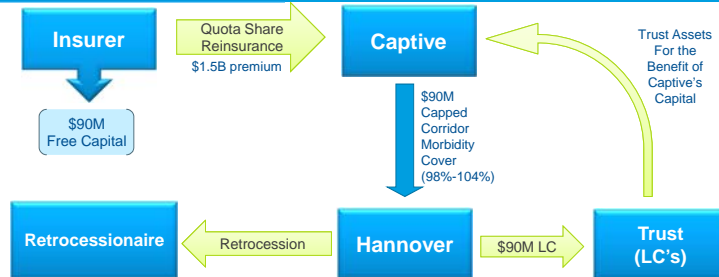
► A Tranche ILS Transaction

- Subject Business: Group commercial health
- Captive entered into excess of loss reinsurance cover (XOL) with Cayman Islands Special Purpose Vehicle (SPV)
- SPV bond issuance:
 - A Tranche: Losses within a MBR of 104% - 114% = \$150M (10 pts x \$1.5B)
 - Captive counts proceeds of bond offering as capital
- Insurer frees up \$150M of capital for redeployment

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Reinsurance Solution (Unfunded Solution - B Tranche)



- ▶ Hannover reinsurance arrangement replicates A Tranche offering, but with the B Tranche corridor, using reinsurance and letters of credit.
 - Capped Corridor Morbidity Cover reinsurance agreement provides reinsurance for Captive on the Subject Business within the B Tranche corridor of a MBR between 98% and 104%
 - 3-year agreement (2011, 2012, 2013)
 - Maximum losses capped at \$90M, which is based on \$1.5B premium and the 6-point exposure corridor
 - Hannover establishes security trust and deposits \$90M of assets (LC) for the benefit of Captive
 - LC is counted as capital of Captive

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Sources of Capital

- ▶ Retained Earnings
 - May not cover the extra capital needed (incr in NB, Large group, etc.)
 - Company may wish to deploy to higher yielding lines
- ▶ Equity
 - Issue additional stock but dilutes EPS and is expensive
- ▶ Debt
 - Increases debt to capital ratio and must be paid back regardless of earnings
 - Impacts the company's rating
- ▶ Reinsurance
 - Cost effective way to provide temporary funding
 - Paid from future profits of the ceded business
 - No negative financial leverage

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Sources of Capital



RBC Relief

- ▶ Products with High Capital Requirements
- ▶ Lower Cost
- ▶ Cedant Retains most of U/W Risk
- ▶ More Flexibility to Adjust Relief Provided each year
- ▶ Usually Shorter Duration

Conventional Coinsurance

- ▶ Parties share in Premiums, Claims, Expenses and Profit
- ▶ Products Where the Company is Uncomfortable Retaining Full Risk
- ▶ Less Regulatory Scrutiny
- ▶ Agreements are more Common and Usually Simpler

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RBC Relief

RBC Relief

- A reinsurance structure that allows a company the ability to reduce their capital requirements with minimal risk transfer

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RBC Relief

- ▶ The relief can be provided through a number of reinsurance structures including, YRT and coinsurance. For health insurance, we typically use a coinsurance structure where the coinsurance percentage is selected to provide the required RBC relief.
- ▶ There is a fee charged for the relief provided that varies based on the amount of risk transferred. The greater the risk, the larger the fee.
- ▶ Profits on the business (reinsurance premiums minus claims minus allowances) in excess of the reinsurer's fee are returned to the company by means of an experience refund
- ▶ Losses are carried forward and paid with future experience refunds

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Company ABC Pro Forma

Income Statement (millions)	Company ABC	% of Prem
Premium	\$1,000	100.0%
Net Investment Income	\$5	0.5%
Total Revenue	\$1,005	100.5%
Incurred Claims	\$840	84.0%
SG&A	\$110	11.0%
Total Benefits & SG&A	\$950	95.0%
Pre-tax Gain/Loss	\$55	5.5%
Balance Sheet		
Capital & Surplus	\$180	
100% Authorized Control Level RBC	\$36	
RBC Ratio	500%	

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Company ABC Pro Forma for a New Acquisition

Acquisition Cost = \$100 million

0% Reinsurance			
Income Statement	Hypothetical Acquisition Target	Combined Pro Forma	% of Prem
Premium	\$300	\$1,300	100.0%
Net Investment Income	\$2	\$7	0.5%
Total Revenue	\$302	\$1,307	100.5%
Incurred Claims	\$252	\$1,092	84.0%
SG&A	\$33	\$143	11.0%
Total Benefits & SG&A	\$285	\$1,235	95.0%
Pre-tax Gain/Loss	\$17	\$72	5.5%
Balance Sheet			
Capital & Surplus	\$54	\$134	
100% Authorized Control Level RBC	\$11	\$47	
RBC Ratio	500%	286%	

$\$180 + \$54 - \$100$

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Company ABC Pro Forma for a New Acquisition

with Reinsurance

43% Reinsurance			
Income Statement	Reinsurer's Pro Forma	Combined Pro Forma w/ Reinsurance	% of Prem
Premium	\$556	\$744	100.0%
Net Investment Income	\$0	\$7	0.9%
Total Revenue (TR)	\$556	\$751	100.9%
Incurred Claims	\$467	\$625	84.0%
SG&A	\$0	\$143	19.2%
Total Benefits & SG&A (TB)	\$467	\$768	103.2%
Experience Refund (EA)	-\$84	\$84	11.3%
Pre-tax Gain/Loss	\$5	\$67	9.0%
Balance Sheet			
Capital & Surplus		\$134	
100% Authorized Control Level RBC		\$27	
RBC Ratio		500%	

$ER = TR - TB - Fee$

$\$47 * (1 - .43)$

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Questions?

Thank you for your attention!

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