Swiss Re
Corporate Solutions

Virtual Captive Solutions

A traditional captive is set up as a (re)insurance company within a corporation. A virtual captive is a multiyear agreement with a licensed insurance company.

Our virtual captive product is a multi-year insurance agreement that emulates the mechanics of a traditional captive with a simplified setup, leveraging our strongly rated and broadly licensed insurer balance sheet. Quite simply, you can take advantage of the popular captive approach for risk financing but use our balance sheet instead.

How does it work?

A traditional captive's main goal is to fully or partially self-insure its parent's risk. The captive collects premiums from the various business units of the organization to finance losses. The captive's capital serves as the "buffer" in case the sum of the accumulated premiums is not enough. The parent establishes a (re)insurer – injecting the capital and holding the captive against its balance sheet. The mechanics of a traditional captive make sense if:

- Your expected loss is lower than what the commercial insurers imply in the market premium
- A hard market demands higher premiums and limits coverage capacity
- You are interested in purchasing reinsurance, i.e. interested in accessing the wholesale risk transfer market

However, the cost and the complexity of setting up a captive can take a toll on the organization and its financials. The initial need to inject capital in the captive can also have an impact on the overall financial flexibility.

A **virtual captive** can retain the mechanics of a traditional captive with one major difference: Swiss Re Corporate Solutions (SRCS) handles the set-up and the administration of the supporting balance sheet, virtually taking it off your balance sheet. A virtual captive makes sense if:

- You want to avoid **the cost behind the set-up,** the need to inject capital and the regulatory complexities
- You want the insurer to bear the cost of running a (re)insurance legal entity and the related **related governance**
- The **traditional captive reasons** above also apply to you

Within a virtual captive, the capital of a captive is replaced by the risk transfer to the insurer – the insurer‘s capital at stake.

A virtual captive is, effectively, a multi-year insurance agreement between a customer (i.e. a parent) and an insurer. The agreement replaces the legal entity of a traditional captive but retains much of its characteristics.

- **Can cover** the same risks as a traditional captive
- **Considers the funds needed** to finance the expected losses within the agreement period (e.g. 3 or 5 years with an option to extend)
- **Accounts** for the calculated risk (potential deviation from the expected)

The insurer carries the remaining risk of any additional deviations from the expected losses. Since most risk will be self-financed over time by the customer itself, the remaining risk to the insurer is kept at relatively low levels. The insurer, in turn, collects a risk premium and a fee to cover the cost of providing the balance sheet and running the program. Both are deducted from the annual premium.

Once the programme finishes (virtual captive ceases to be active,) the remaining funds are returned to the parent by way of a **"low claims bonus."**

Both, a captive as well as a virtual captive structure require a minimum scale to justify their setup and administration.

If the premium for the programme is too low, the expense of running any of them is simply too high.

Virtual captive: does it work for you?

Clear advantages

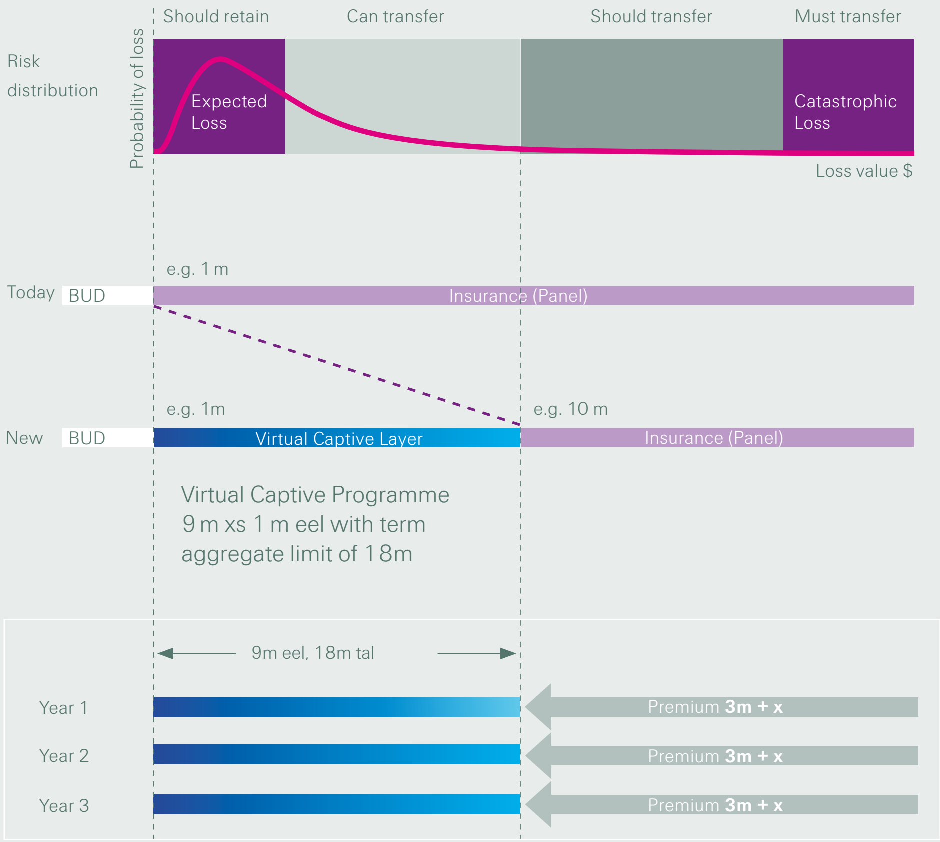
- No set-up cost and no need to navigate the regulatory complexities
- No expenses for captive management services, actuarial, audit and other fees
- Speedy implementation; Simple, clean exit options; Swiss Re Group financial strength

Things to consider

- Types of risks are limited to those that reflect the insurer's license, capabilities and risk appetite
- Flexibility of the virtual captive structure is reduced for the term of the agreement. Once the virtual captive insurance agreement is signed, parties are bound for the entire term, and any changes require mutual agreement

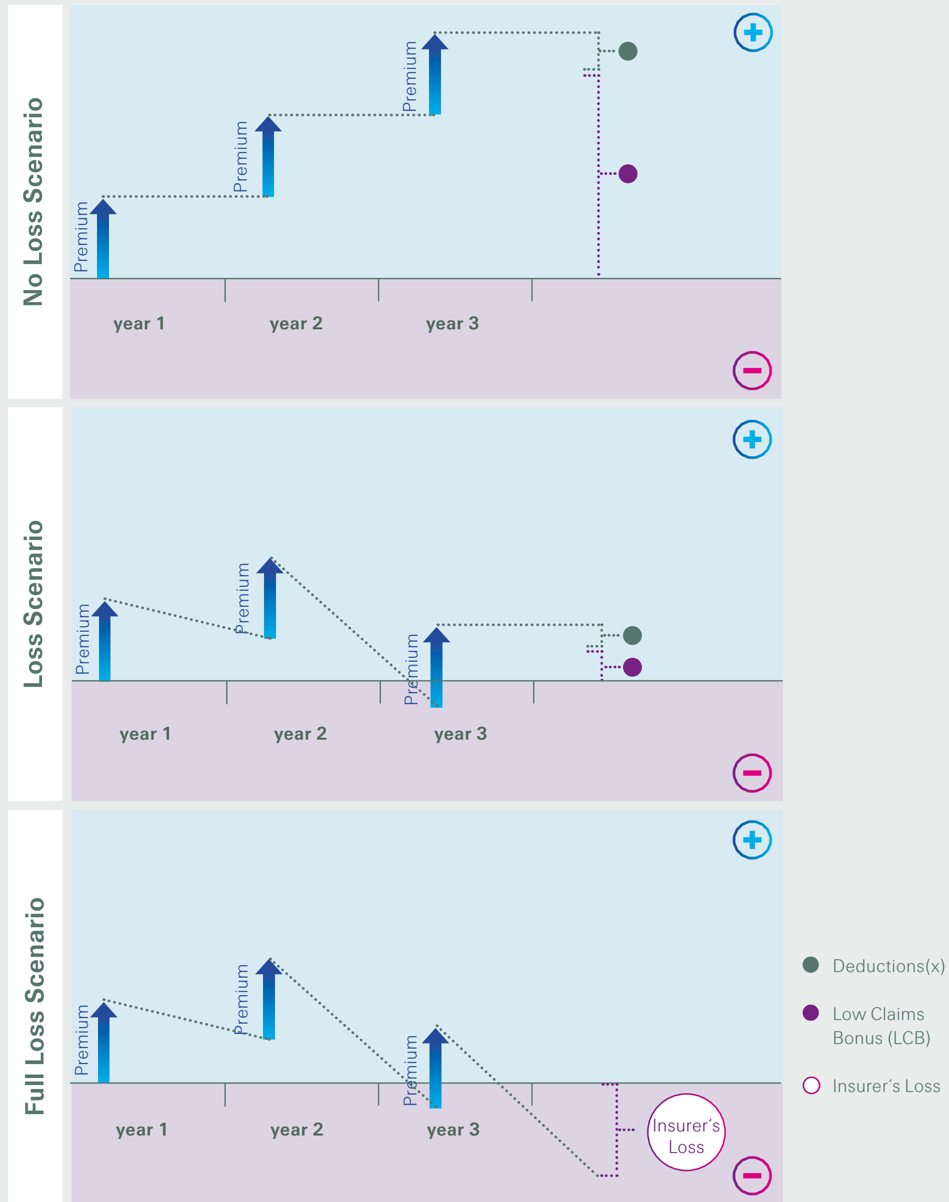
Virtual captive	Traditional captive
The **insurance agreement** is between the customer (you) and the insurer (us)	The insurance coverage is agreed upon by the insured and the captive
Covers a **multi-year period**; finances risks over time	Set up to exist for many years or indefinitely, finances risks over time
We (the insurer) provide coverage through the agreement and **handle all regulatory aspects** (license, solvency, tax, etc) through our already efficient and existing infrastructure	All regulatory aspects are handled by the captive management and contracted third parties (registration, substance, arm's length pricing, solvency, governance, etc.).
The agreement considers the risk appetite of the insurer, (i.e. the amount of **risk transfer** capacity provided in the insurance agreement)	The captive's capital is carrying the risk
Remaining funds are paid through: Low Claims Bonus **(LCB)** to the customer	Remaining funds are paid through: A dividend to the parent
Additional funds: Additional Premium **(AP)** feature	Additional funds: A call for capital injection by parent
The call for AP likely extends the insurance agreement period	A call for additional capital means the intent to continue operating the captive

Situation: a corporate client is looking to take more risk in response to the market conditions. To minimize the administrative and regulatory expense, they opt for the SRCS virtual captive. The structure is simple, transparent and cost-effective, allowing the client to finance a first (full) loss over 3 years and transfer any second loss risk to the insurer.



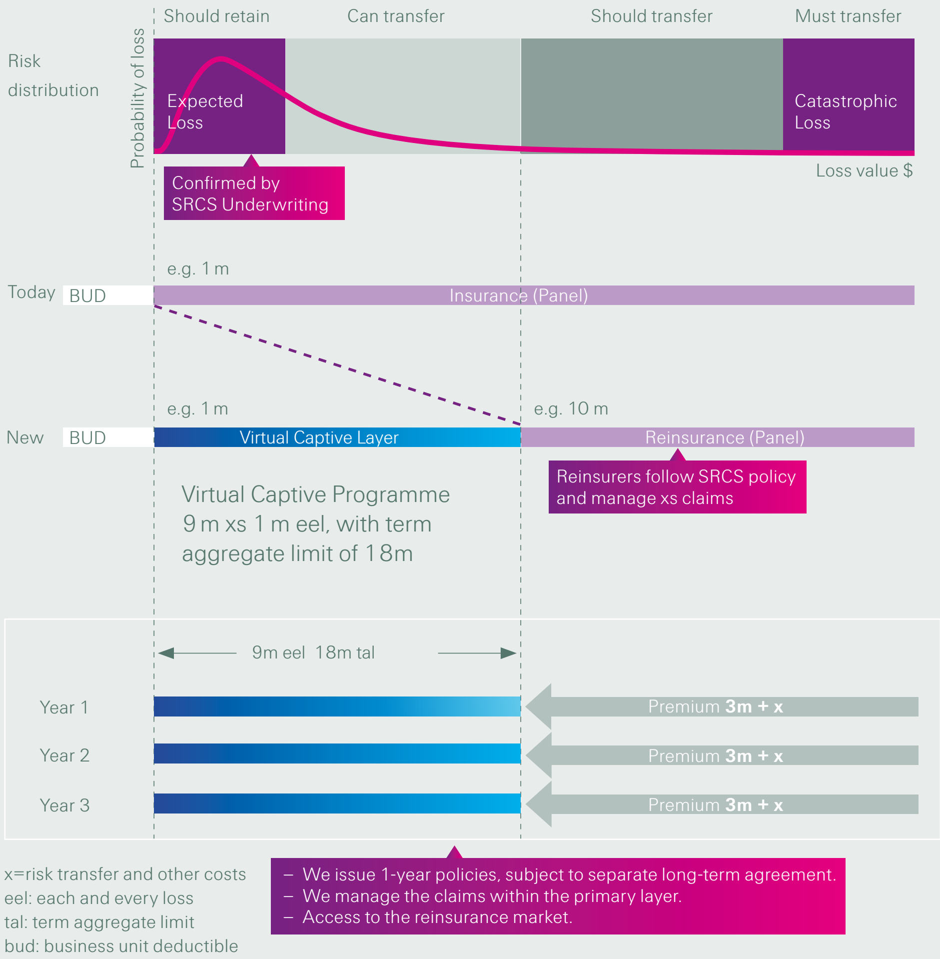
x=risk transfer and other costs
eel: each and every loss
tal: term aggregate limit
bud: business unit deductible

Cumulative premium minus Losses

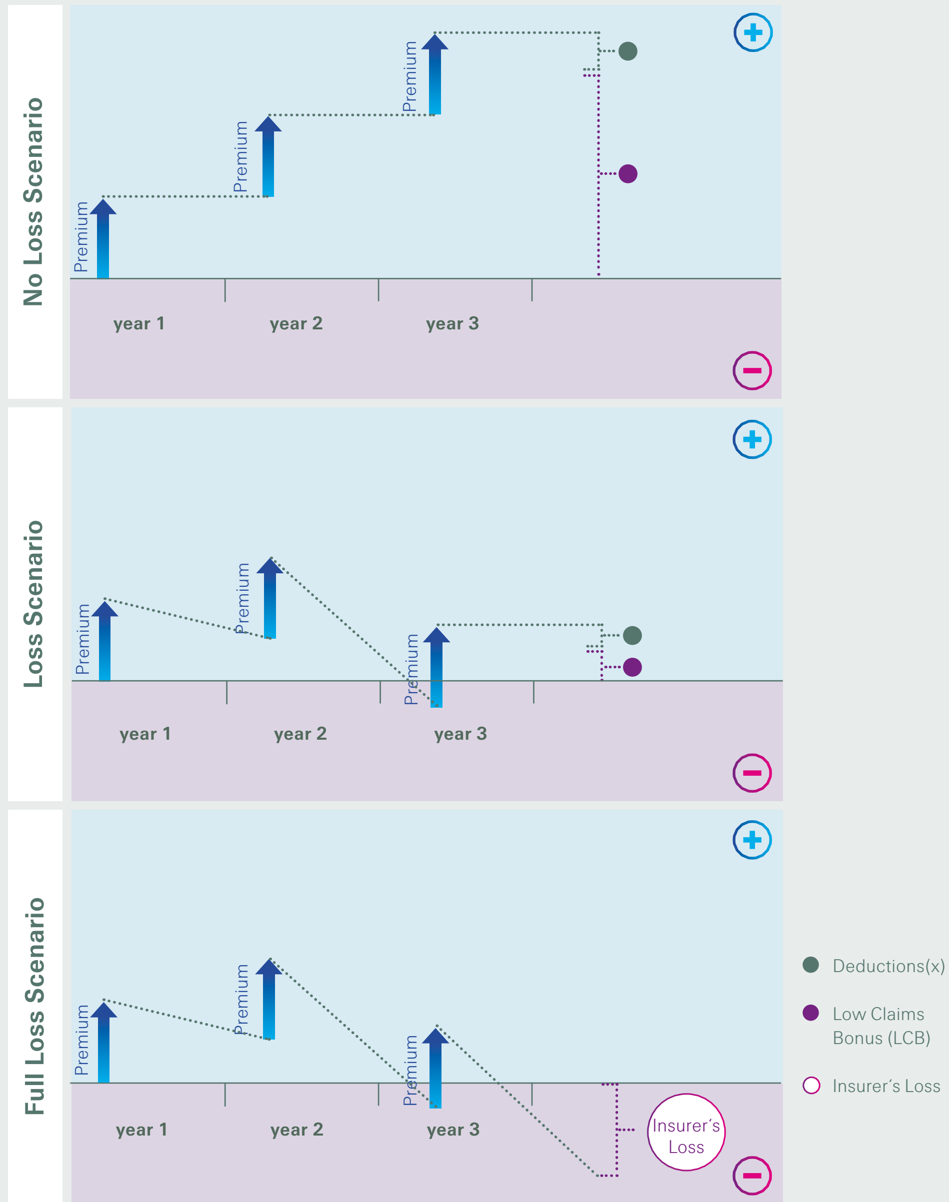


Virtual Captive Example Two

Situation: a corporate client is looking to outsource all of a captive's functions entirely. They select SRCS direct virtual captive. The new insurance agreement with SRCS becomes the primary direct insurance program to the corporate client. Coverage limits above a certain point (the maximum limit intended to be financed through the virtual captive) are reinsured by SRCS (the insurer) in the reinsurance market.



Cumulative premium minus Losses



In a hardening insurance market, understanding alternative ways of transferring risk can help protect your business.

Next Steps

1. Confirm the motivation for setting up a virtual captive. Are you prepared to self-finance a larger part of your insurance coverage? A virtual captive does not mean a reduced premium spend on a single year basis. The reduced cost of risk plays over multiple years, essentially by way of Low Claims Bonus at the end of the agreement.
2. Assess self-financing risk appetite for a 1-, 3-, or 5-year agreement. How much loss are you ready to finance?
3. Evaluate the optimal retention on the relevant lines of business within current insurance market
4. Involve Accounting/Tax to ensure understanding and support
5. Discuss the appropriate structure with Swiss Re Corporate Solutions, evaluate value of the program and make a buying decision
6. Implement with Swiss Re Corporate Solutions

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