

Rent-a-captive sector reports drop in number of cells

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By Stuart Collins

The soft insurance market has not helped the rent-a-captive sector, with several domiciles reporting that the number of cells has decreased even as new formations continue, experts say.

Rent-a-captives, which enable companies to share the benefits and costs of captive ownership by forming a cell within a group captive to meet their insurance needs, have been around for about 40 years.

But within the past decade, several domiciles have improved on the concept, passing legislation that legally separates the liabilities and assets of participants in what is known as protected, sponsored or segregated cell companies from participants in other cells.

The number of captives with cells and the number of cells had grown steadily, but the financial crisis and the soft insurance market disrupted the trend, said Steven Chirico, associate vp at Oldwick, N.J.-based rating agency A.M. Best Co. Inc. Cell captives continue to be formed, but some cells have closed or are inactive because of the repercussions of the financial crisis on their owners, he said.

The development of sponsored cell captives in Vermont has been "modestly successful," said David F. Provost, deputy commissioner of captive insurance at the Montpelier-based Vermont Department of Banking, Insurance, Securities & Health Care Administration.

The domicile has 18 cell captives with 80 cells, down from the peaks of 19 companies in 2006 and 106 cells in 2005. Total premiums for sponsored cells in Vermont dropped to \$24 million in 2009 from \$98 million in 2007, Mr. Provost said.

A large part of the decline has been due to closing or shrinking cells that write mortgage guaranty insurance, but cell captives in general did not grow as much as sponsors once expected, Mr. Provost said. Some sponsored cell companies never wrote any business and eventually closed, he added.

While captive cell numbers have declined in the soft market, some domiciles say interest in new formations is increasing.

Guernsey, where the number of protected cell companies declined in recent years, now is seeing applications increase to form new insurance cells, said Mike Poulding, deputy director at the International Insurance Division of the Guernsey Financial Services Commission in St. Peter Port, Guernsey.

"We believe that this is due to increasing acceptance of the PCC structure and the greater ease of establishment of a new cell as compared to a stand-alone insurance company."

Guernsey has 64 insurance PCCs with 337 cells, down from 69 PCCs with 344 cells in 2008. The reduction was caused by fewer new PCCs and cells being licensed rather than an exceptional level of closures, Mr. Poulding said.

The Mediterranean island of Malta also has seen fresh interest in establishing cell companies, said Joe V. Bannister, the Attard, Malta-based chairman of the Malta Financial Services Authority. Malta, which first passed protected cell legislation in 2004, has four PCCs and 12 cells and is processing applications for another PCC and three more cells.

Soft insurance pricing makes retaining risk less attractive, so forming or joining a cell captive also becomes less appealing, said John Lochner, Weatogue, Conn.-based director of consulting services at Towers Watson & Co. "But companies continue to set up and join cell captives, so interest is still there even with the head winds of a soft market."

While cell captives may not have been the "tremendous success" some sponsors would have liked, they have proved "useful," Mr. Lochner said.

Cell captives enable a company to “rent a space” in a captive, which is particularly attractive for companies that are not of sufficient size or do not have sufficient time, capital and resources to set up a wholly owned captive. They also are attractive to entities that wish to separate liabilities, such as a hospital that wants to have its coverage for physicians held in separate cells, or real estate and construction companies involved in joint ventures, he said.

While a hard market drives captive activity overall, joining a cell company may be less costly for a company than establishing a single-parent captive in a soft market, said Rick Stasi, chief operating officer of Avizent Alternative Risk, a unit of Avizent, a Dublin, Ohio-based TPA and risk management service provider.

Avizent continues to add about five programs a year to its Bermuda-based captive cell company, Atlantic Gateway International Ltd., which typically sees 36 agency-owned cells offer insurance programs to more than 1,000 companies.

“The soft market has been prolonged, but we are seeing interest now pick up,” Mr. Stasi said. “The smart brokers and risk managers realize the market is primed to turn any time and are looking ahead to the next few years. We are already seeing some 10 or 12 new prospective programs.”

Even though there has been a general slowdown of captive formations, there still is plenty of interest from companies that want to form or join cell captives, said Everett Newman Jr., managing partner at Costa Mesa, Calif.-based United Alternative Risk Insurance Solutions L.L.C., a unit of Miller United Insurance Brokerage Inc.

Companies have been attracted to United's cell captive for restaurant franchisees because it gives them more control over claims and the potential to participate in underwriting profits. The Restaurant Franchise Captive Program—which has a cell in Atlantic Gateway International—has returned profits of \$9.1 million on premiums of \$33 million, while participants have enjoyed loss ratios of 16% on average through better loss and claims management, he said.

United this year plans to launch another cell company—Restaurant Franchise Captive Program II, which is expected to exceed its existing program in terms of member companies within a year, Mr. Newman said.

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