BENEFITS POOLING & CAPTIVES

American Benefits Council

Benefits Passport Webinar

March 7th, 2013

Introductions

- Lynn Dudley
  - American Benefits Council
- Sabina Marotta
  - L-3 Communications Corporation
- Kathleen Waslov
  - Willis Global Solutions

Agenda

- Global Employee Benefit Liabilities
- Managing Risk Exposure
- Financing the Plans
  - The Value of Pooling
  - Captive Reinsurance
- Information Utopia

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Background

- Many multinationals are seeking new options to finance their employee benefit liabilities, including coverage for death, disability, accident, medical and pensions for both active and retired employees.
- Like any risk exposure, employee benefit risks need to be managed and financed efficiently.
- Financing options include traditional insurance, self-insurance, and increasingly in recent years, pooling and captive reinsurance.
- This session is a brief overview of benefit risk financing techniques with examples.

Global Benefit Costs

Benefits range from 15% to 50% of total compensation costs

Typical plans include financial support and services to employees for events of:

- Death
- Disability
- Accident
- Sickness
- Retirement


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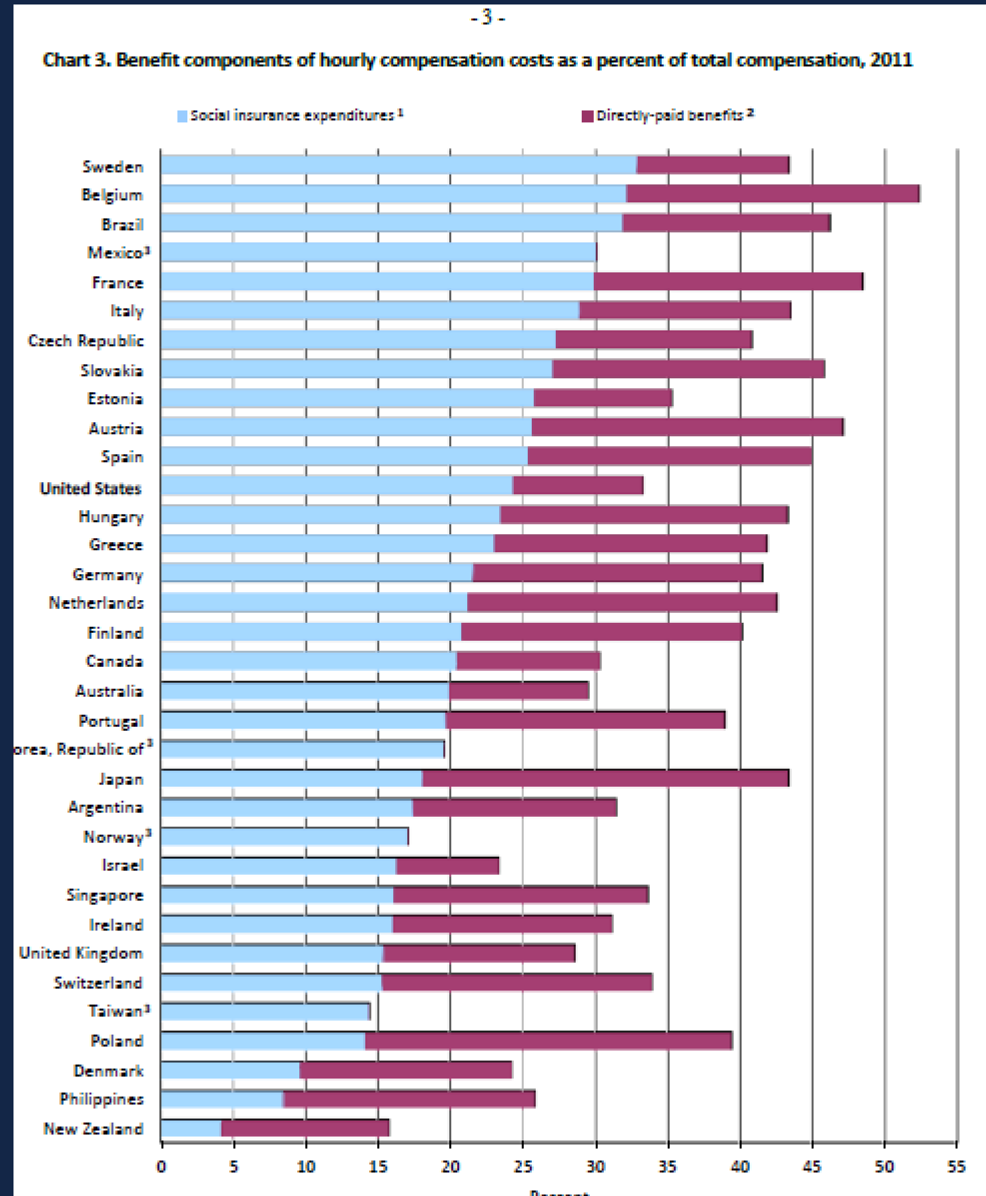
INTERNATIONAL COMPARISONS OF HOURLY COMPENSATION COSTS IN MANUFACTURING, 2011



Global Benefit Landscape

"Centralization of operations and governance of employee benefit plans is expected to increase significantly in the short term."

-- American Benefits Institute, 2012 Study*

- *"…organisations struggle to know what benefits they offer, …, how much they cost, and what types of risks they pose…"*
- *"Financial costs and risks due to employee benefits are driving corporate involvement in local benefits decision more than other factors…"*

* 2012 Corporate Governance of Global Benefits Study, American Benefits Institute and Aon Hewitt

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L-3 Global Benefit Landscape

- *L-3 grew by acquisition*
- *Multiple businesses with multiple locations operating independently*
  - *Keep ownership of financial bottom line*
  - *Do not want corporate headquarters interference*
  - *Fear of losing decision making control*
- *Different plan coverage and structure*
  - *Business Culture*
  - *Group size*
  - *Country regulations*
  - *Country best practice*

"No Economies of Scale"

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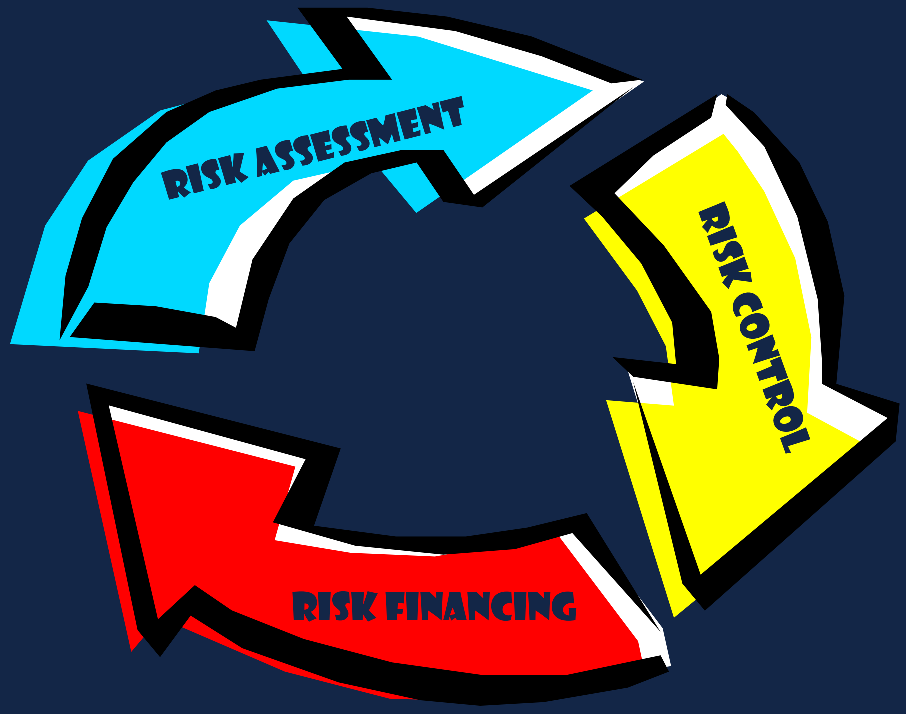
Risk Fundamentals

Benefit risk liabilities can be managed

- Identify the risk exposures
- Prevent and control losses
- Finance efficiently

Economies of scale derive from aggregation of volume

- Pool common risks across jurisdictions
- Coordinate with other enterprise risks in a strategic framework



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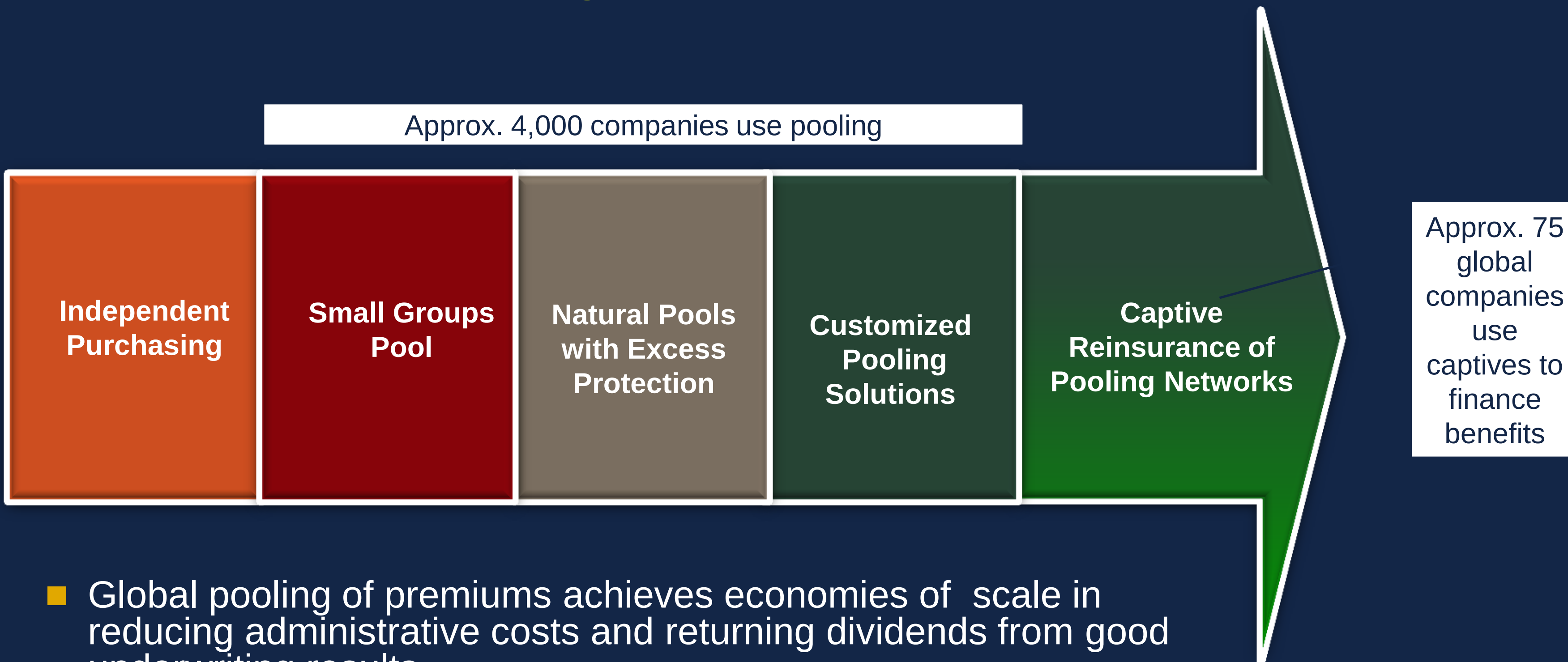
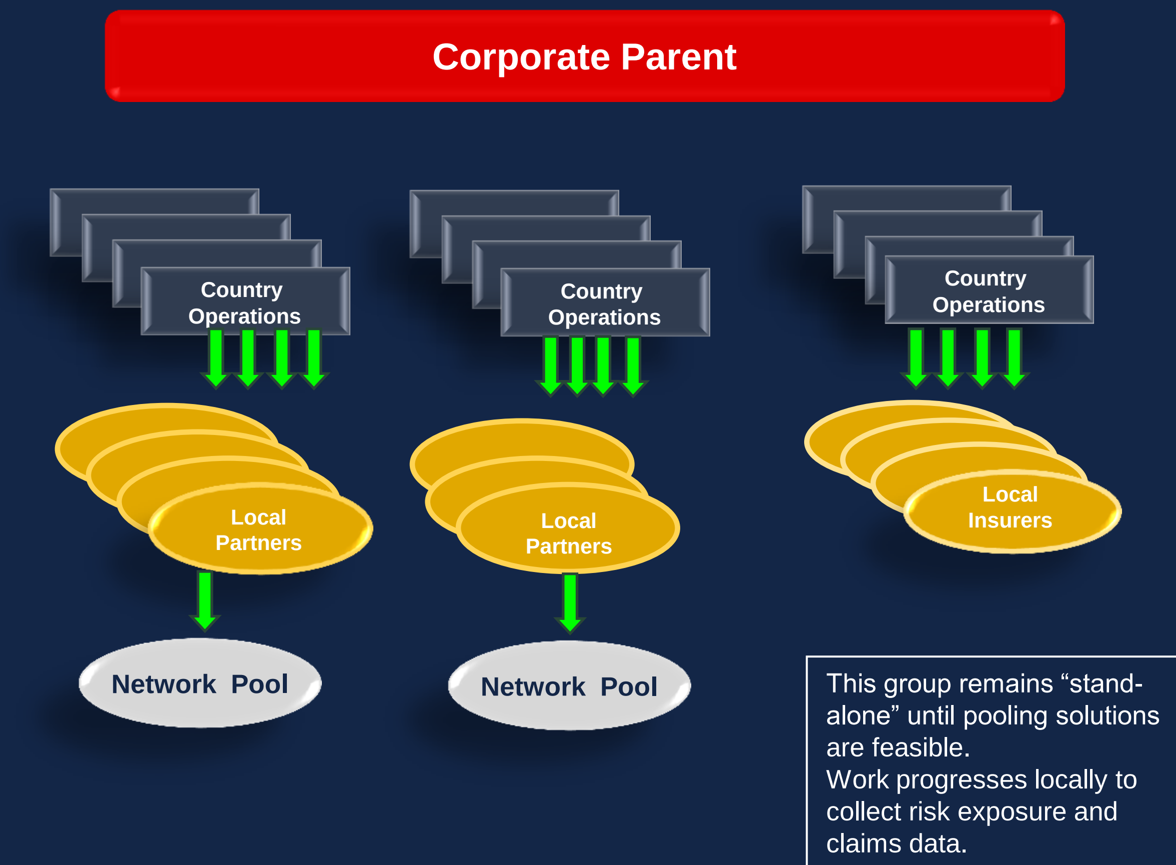
Financial Efficiency

Continuum of Savings and Control



- Global pooling of premiums achieves economies of scale in reducing administrative costs and returning dividends from good underwriting results
- Captive reinsurance of the pooled premiums gives control of information and assets and creates opportunities for custom coverage and underwriting and investment income

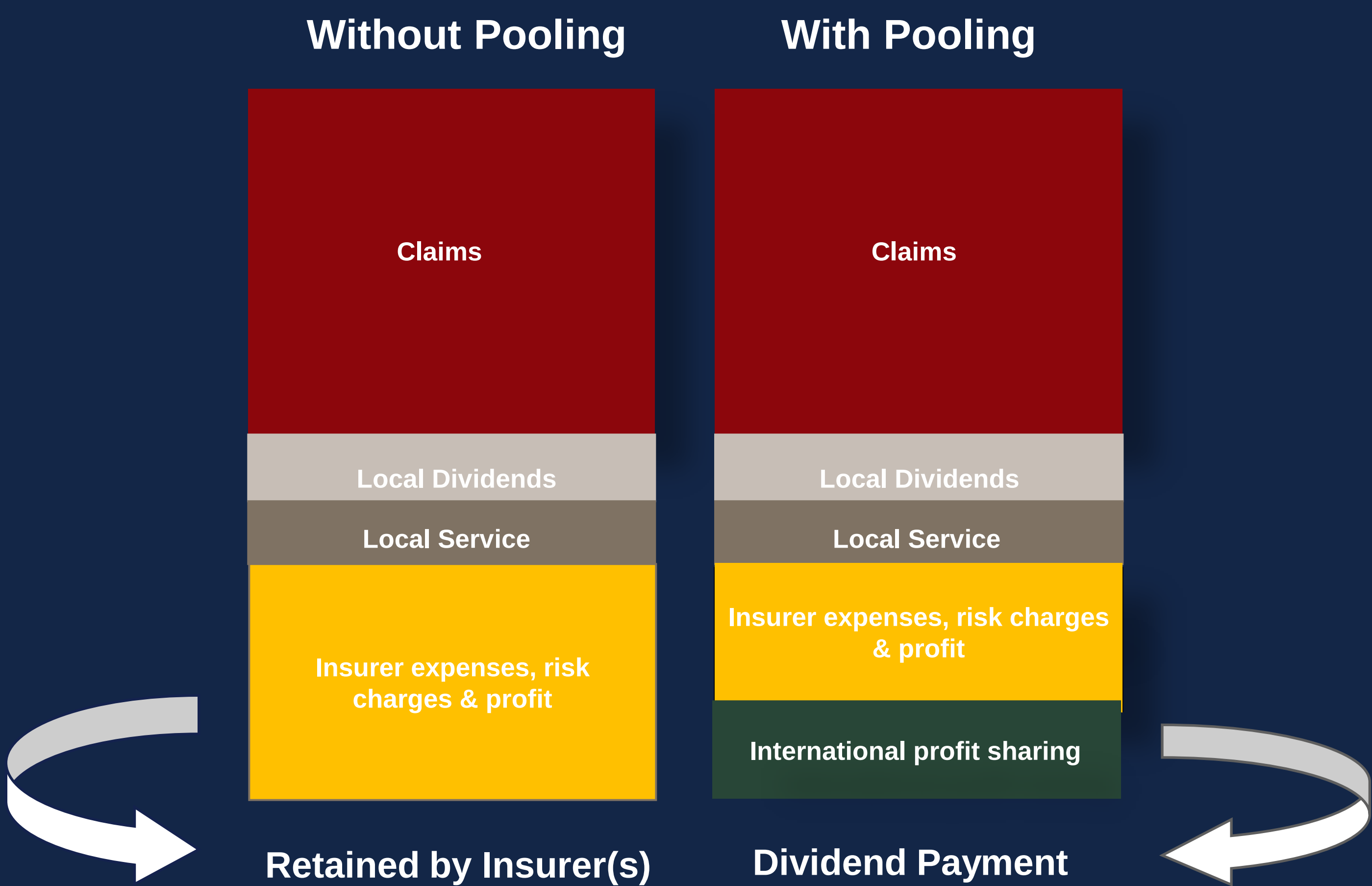
Pooling



Pooling Advantages

- Claim costs are more predictable (actuarially "credible")
- Insurers are more confident in their loss picks and charge less for volatility and solvency capital
- Fixed costs are spread wider, resulting in lower per unit expenses
- Underwriting dividends are paid
- Underwriting experience is understood by cost components

Financial Benefits of Pooling

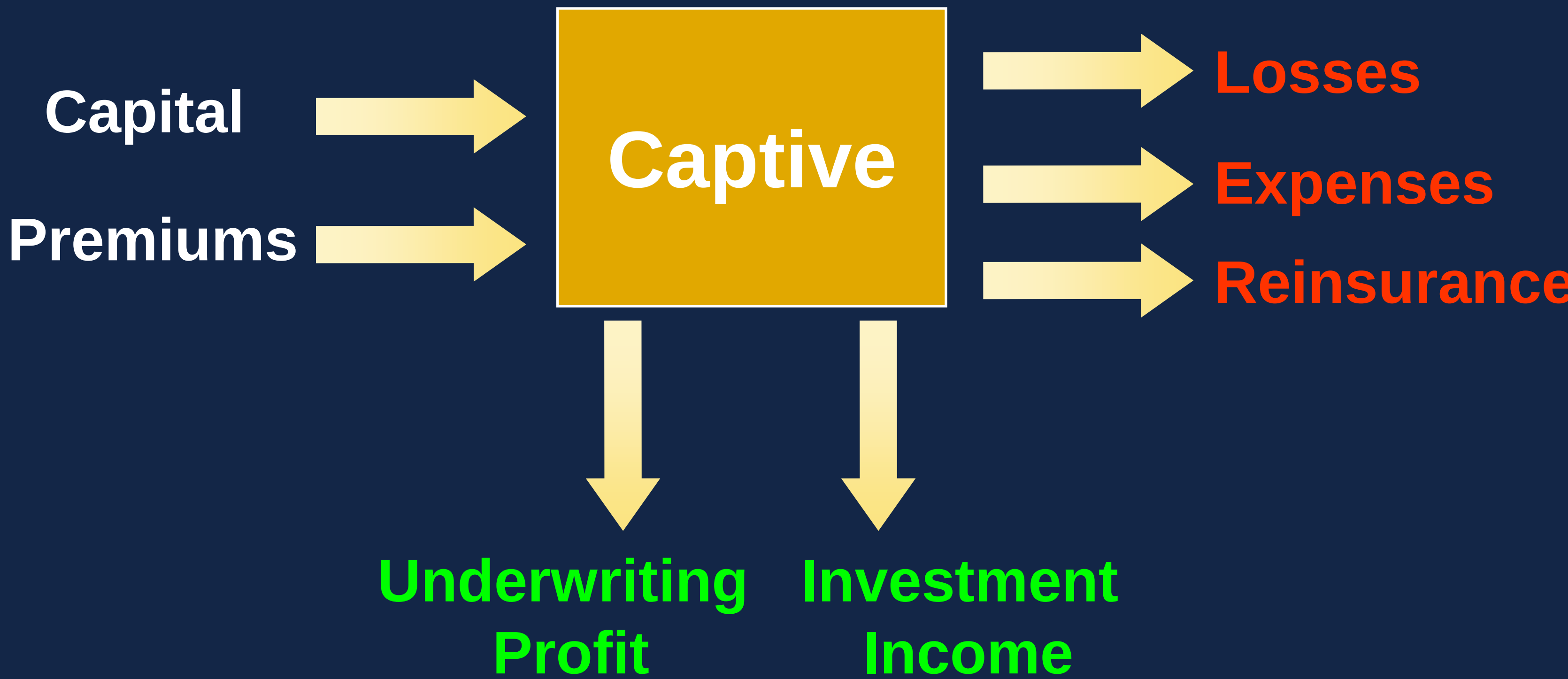


L-3 experience with pooling

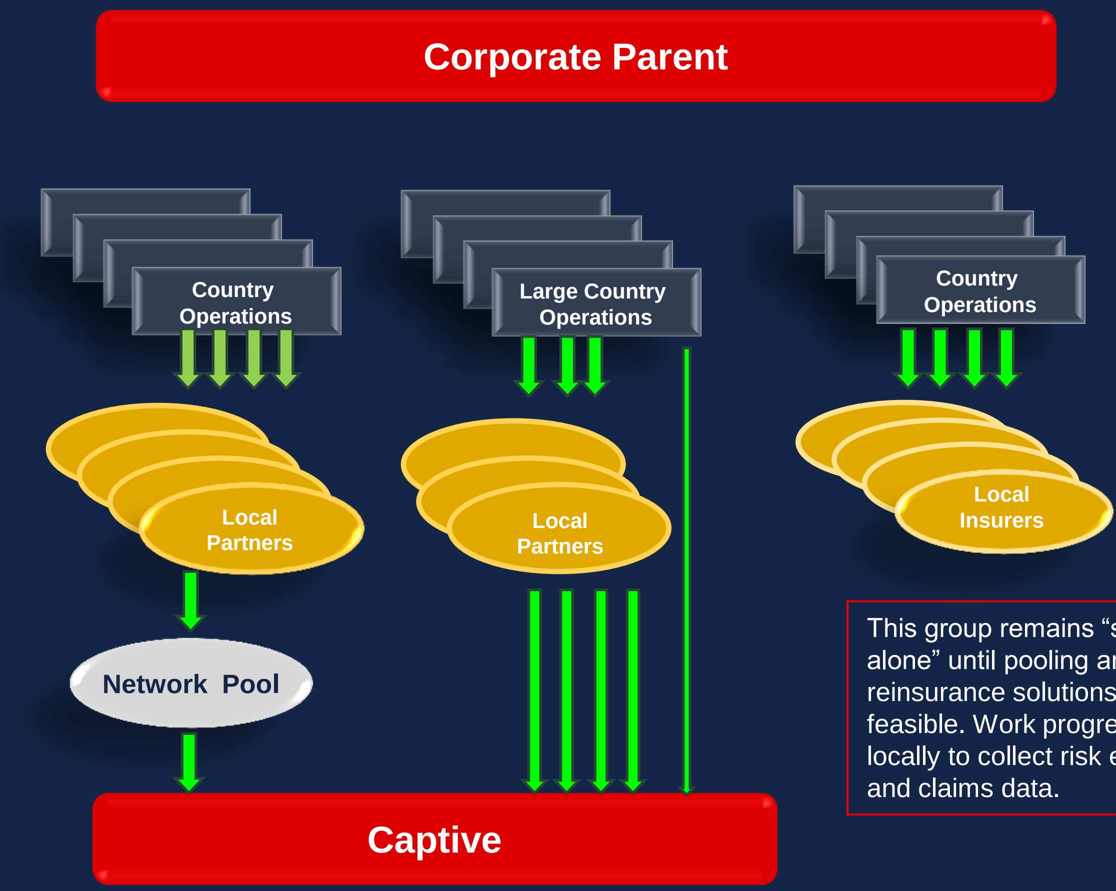
- L-3 entered into first “pooling” arrangement for insured life product in the United Kingdom in 2006
  - Reduce annual benefit cost
  - Insurance carrier must be willing to participate (our U.S. carrier does not want to participate)
  - No cost increase if “pool” sustains excessive claim experience

- Expanded to Hong Kong and Germany in 2009
- Thus far, participating business units have realized a 15% premium savings each year through dividend payments
- Business and country culture create difficulties for pooling expansion but……..
  - Expand to include insured income replacement product and capture other countries (e.g. Canada, Italy, Norway, Costa Rica)

How captives work



Captive Reinsurance



This group remains "stand-alone" until pooling and reinsurance solutions are feasible. Work progresses locally to collect risk exposure and claims data.

Captive Advantage

- Premiums flow to captive
- Captive sets reserves
- Assets are invested
- Earnings accrue to Group
- Risk exposure and claims information is centralized
- Decisions about plan design and loss control are informed

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Benefit Captive Evolution

1982-2000	2000-2002	2002-2013
▪ Large P&C captives add EB risks, reinsured from Pooling Networks: • 1982 - ALICO (Maxis) • 1984 - Generali ▪ Attempts to gain Labor agency approval to reinsure ERISA regulated plans, e.g. CSX	▪ Growth in number of Global EB captives ▪ Columbia Energy exemption for U.S. disability ▪ ADM exemption ▪ “ExPro” expedited process is allowed	▪ Other global pooling networks introduce captive reinsurance capability (All Net, IGP, Insurope, and Zurich) ▪ 25 more U.S. DOL approvals, including post-retirement medical ▪ First pension captives ▪ Changes at DOL; new team “suspends” expedited process for comprehensive review

Operational Value

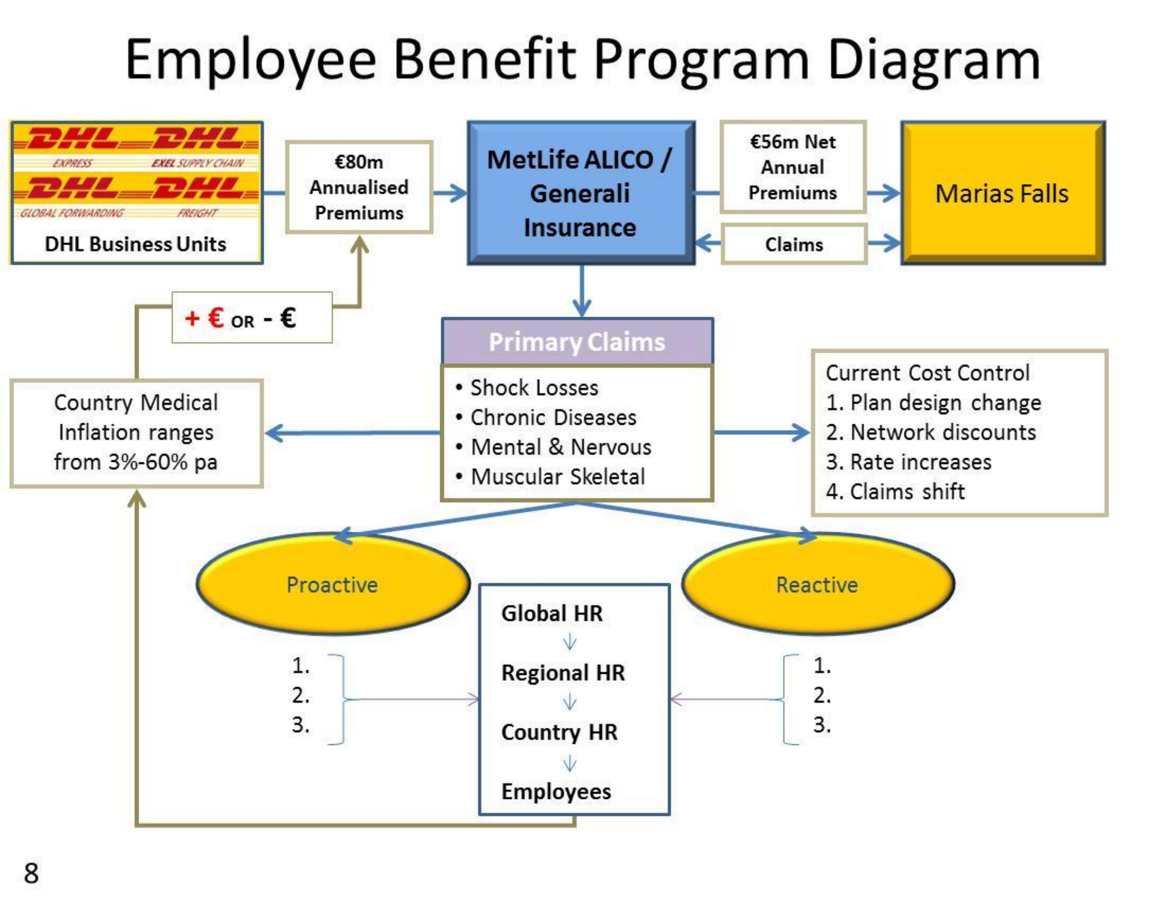
Captive insurance can improve risk management governance

- Pooling risks of individual business units
  - Smoothens results
  - Permits risk sharing and allocation methodologies
- Insurance company structure with accountant, auditor and actuary oversight improves regulatory compliance of self insured plans
- Assets that support enterprise risks are consolidated
- Captive can add customized coverage not otherwise available in the market, e.g. certain perils, limits, plan provisions

Perhaps the most significant advantage is transparency

- Timely access to claims data and focus on trends creates “feedback loop” that ultimately reduces costs

Global EB Captive
Feedback Loop



Source:
2012 World Captive Forum
Presentation by Bill Fitzpatrick,
Deutsche Post DHL

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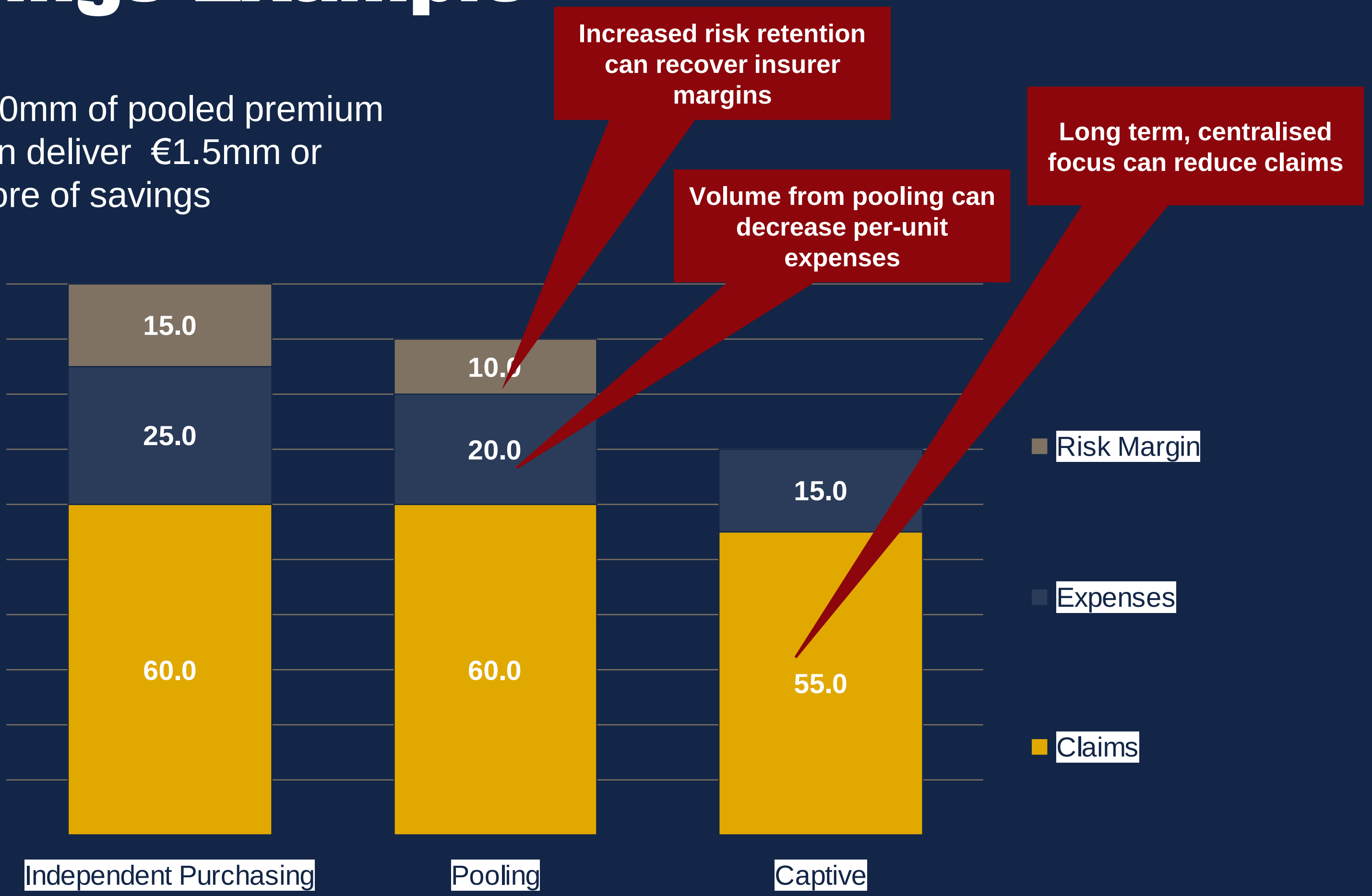
Global EB
Savings Example

- €10mm of pooled premium can deliver €1.5mm or more of savings



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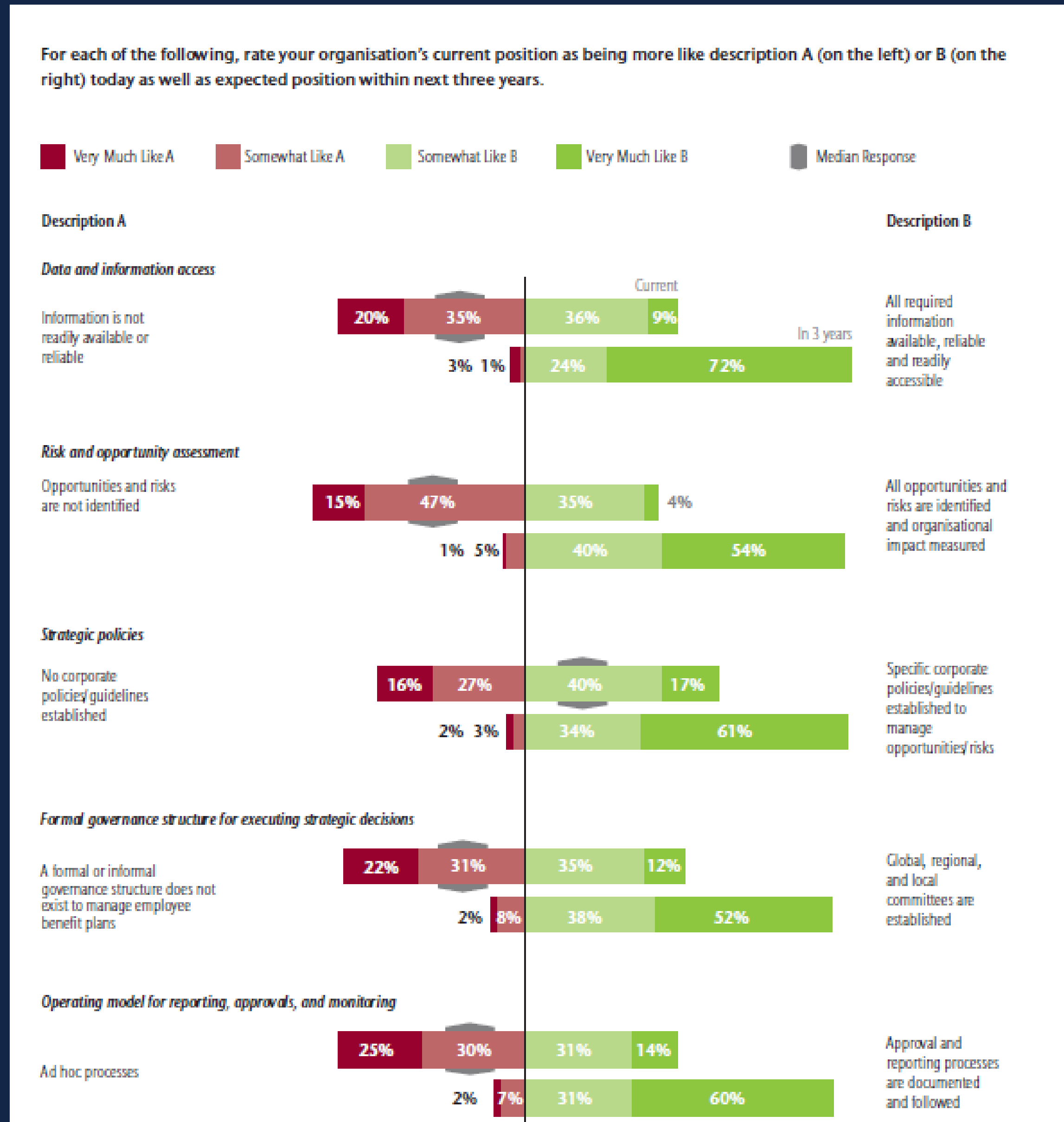
Data Utopia



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QUESTIONS?