

A STRAIGHT FORWARD GUIDE TO CAPTIVES

INTERNATIONAL CAPTIVE PRACTICE – ASIA PACIFIC

SO, WHAT IS A CAPTIVE?

Put simply a Captive is an insurance entity that is set up and run on behalf of a company (which typically is not in the insurance business itself) as a fully owned subsidiary of that organisation. The sponsor is therefore both the policyholder and the shareholder of the captive.

Owning a Captive enables a company to self-insure a proportion of its own risk, (typically predictable attritional losses) resulting in the premium funds and interest thereon is remaining within the Group. In many cases the Captive acts within the Group as the central co-ordination point for risk financing across the Group's business units / trading subsidiaries. Captives can also be used to deliver insurance products, complimentary to the sponsor's core product offering, to enhance their revenue.

When properly set up and managed, Captives provide an ideal solution for organisations wanting to manage their balance sheet and reduce their cost of risk as part of their risk management strategy.

WHO WOULD BENEFIT FROM A CAPTIVE?

Whilst there is no rigid profile of a typical Captive owner, common features include:

- Significant retentions under conventional corporate risk programmes;
- Ability to capitalise a regulated entity;
- Perceived high cost or poor value of insurance;
- A lack of insurance markets for key risks;
- Strong emphasis on risk management;
- Appetite to retain greater risk;
- Premium spend in excess of \$500,000;
- Currently act as agents and sell customer insurance products.

However, none of these should be regarded as prerequisites.

Captive owners include:

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| - Public bodies | - Charities |
| - Quoted companies | - Governmental entities |
| - Private companies | - Trade associations and groups |
| - Partnerships | - Joint Venture companies |

A Captive is a licensed insurance entity established to provide self insurance of retained risk to its sponsor.



BENEFITS OF OWNING A CAPTIVE

There are a number of distinct benefits to a company operating a Captive and these include:

- Lower and more stable cost of risk
- Access to the greater capacity and lower costs of the reinsurance markets
- Better control over and management buy-in to risk management
- Control of insurance terms and conditions
- Control of claim settlement
- Co-ordination of multinational programmes
- Shareholder tax planning opportunities
- Opportunity to participate in underwriting profit of the risk
- Increase revenues (customer insurances only)

WHERE ARE CAPTIVES BASED?

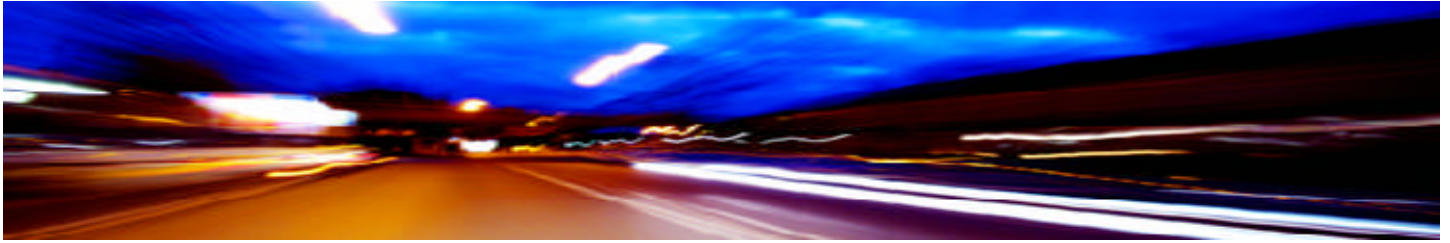
Captives tend to be set up and managed in Jurisdictions with insurance and company laws and regulations, appropriate to Captive insurance, and a solid business infrastructure. The choice of domicile depends on the needs of the individual client (for instance, Captives in EU territories are permitted to accept risks from across the EU). Captive domiciles in the Asia Pacific region include:

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| - New Zealand | - Labuan, Malaysia |
| - Singapore | - Guam |
| - Hawaii | - Hong Kong |
| - Vanuatu | |

Other domiciles include:

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|--------------------------|---------------|
| - Bermuda | - Guernsey |
| - British Virgin Islands | - Switzerland |
| - Cayman Islands | - UAE |
| - EU | - USA |

Willis can establish and manage Captives in any reputable major domicile throughout the world.



SETTING UP A CAPTIVE

Setting up a Captive can be achieved in a number of stages:

- Feasibility
- Potential need identified
- Feasibility study undertaken
- Establishment
- Decision to proceed
- Appointing advisers
- Writing the business plan
- Incorporation and licensing
- Management
- Commence trading
- Establish governance framework
- Establish operating and compliance infrastructure

The time required to complete this process varies, dependent on domicile and business plan. Typically it would take three to six months in major onshore jurisdictions and 6 – 12 weeks in Captive friendly domiciles.

THE CAPTIVE FEASIBILITY STUDY

The study is undertaken by Willis in co-operation with the client and takes an in-depth look at a number of topics, including:

- The client's strategic objectives
- Principles of risk financing
- Captive and other risk financing options
- Overview of existing insurance programmes
- Risk retention analysis
- Evaluation of risk financing facilities
- Identification of covers suitable for a Captive
- Captive domicile review
- Recommended underwriting guidelines
- Capital / solvency requirements
- Claims analysis
- 5-year business plan and financial projections
- Accounting and taxation considerations
- Operating matters

The scope of this study, its costs and deliverables will be discussed, agreed and documented at the inception of the project.

Following this exercise the client can decide whether or not a Captive is the most appropriate insurance vehicle for them. We recognise this is a considerable commitment and so we offer a Captive clinic at no charge to quickly analyse key information from your client to assess whether the Captive concept appears to have validity and if further work is warranted.

COSTS

- Phase 1: Initial assessment of business case – free consultation with client to discuss potential value of feasibility study.
- Phase 2: Captive feasibility study carried out by Willis International Captive Practice, typically up to 10man days' work and costs in the region of \$25,000 dependent on scope.
- Phase 3: Captive formation – cost dependent subject to negotiation and on type of business plan, location and other specifics.
- Phase 4: The Captive annual running costs range greatly depending on location and complexity of business plan and service requirements. However, few feasible Captives will have running costs below \$75,000 per annum.

THE NEXT STEP

Ideally consideration of a Captive should start well in advance of renewal but we can be brought in at any point. If you have a client who is interested in discussing retention financing or Captives or you feel might be interested in exploring whether a Captive maybe the most appropriate risk financing vehicle for their organisation, then please contact:

Peter Lowe
CA, ANZIIF, OPIB
Director, Willis International Captive Practice
Willis New Zealand Limited
Tel: +64 9 920 2997
Mob: +64 21 909 148
Email: lowepj@willis.com

George Ong
CPA ACII ARM
Divisional Director
Willis Management (Singapore) Pte Limited
Tel: +653 6422 0654
Email: ongg@willis.com

