CAPTIVE REGULATORS STEPPING UP DURING THE PANDEMIC

Written By Karrie Hyatt

It's been five months since COVID-19 caused the federal and state governments to issue the "Safer-at-Home" orders causing havoc to businesses around the U.S. The pandemic is creating a protracted time of uncertainty and has the potential to be the slowest catastrophic event experienced in the insurance market.

The pandemic is changing the way many businesses operate and captives are changing as needed to provide support to their parent companies. With the contraction of the traditional market and the emerging risk of pandemic interruption coverage, captives are becoming and even better option for many businesses.

During this time of turmoil, captive regulators are showing that they can continue to provide top notch regulation while helping their captives, and their parent companies, through this time of upheaval. An informal survey of states shows that captive domiciles are helping their captives in myriad ways. Nearly all domiciles are offering regulatory filing extensions—either for all captives or on a case-by-case basis.

Some domiciles are waiving the requirement for notarized affidavits or providing workarounds. In some cases, regulators are allowing for electronic signatures. According to Travis Wegkamp, captive insurance director with the Utah Insurance Department, "Due to the strains on companies from the pandemic, and everyone trying to adjust to teleworking while still trying to meet deadlines, we are being very liberal in granting extensions for filings of annual statements, audits, etc."

"We emphasized that during this time, we understand the disruption caused by the pandemic and will be accommodating and flexible as possible to our captives," said Andrew Kurata, the captive insurance administrator for the State of Hawaii Dept. of Commerce & Consumer Affairs, Insurance Division. "We encouraged captives to reach out and communicate to the Captive Insurance Branch, and we will work with captives on a case-by-case basis to resolve issues."

Domiciles are also waving in-state meeting requirements and meeting prospective captive owners through video conferencing. States that require an in-state captive representative are relying on that person to conduct board meeting through teleconferencing or video conferencing.

Several state insurance departments, such as North Carolina, had already switched to online submittal systems for filings which has made the process much more streamlined. According to Debra M. Walker, senior deputy commissioner of the Captive Insurance Companies Division of the North Carolina Department of Insurance, "Fortunately, through our online captive filing system or email, captive insurers were already electronically submitting applications, other filings and special requests to the NCDOI. With those processes in place, while our team was working remotely, we were able to timely review and respond to this information, just as we would from our office."

Regulators are keeping an eye on captive's capital, surplus, and solvency. The potential for large claims payouts, loans to the parent company, the fluctuating stock market, and an unsteady economy could have a detrimental effect on a captive's financial stability. "The overall majority of the captives are well-capitalized. As such, more than ever, we will need to monitor the capitalization and solvency of our captives due to the fluctuating stock market and economic downturn, but at the moment it is not a significant concern," said Kurata.

The key for captive regulators right now is flexibility, while encouraging communication from their captives and staying in close contact with captive managers. According to Walker, "Where we determine that issues exist or may be arising, we will more closely monitor those insurers. The manner in which we do that depends on the situation. We may require more frequent financial reporting, periodic calls and virtual meetings to discuss developments, conduct examinations, or take other actions commensurate with the magnitude of the issues."

For Steve Kinion, director of the Bureau of Captive Insurance Products for Delaware, staying on top of the situation has been crucial to helping captives in real time. During a webinar in June on the subject hosted by International Center for Captive Insurance Education (ICCIE), Kinion said, "We have seen some surplus reduction. We did have a couple of captives that reached minimal solvency threshold, actually just got below the minimal capital threshold … through weekly conference calls with captive managers, where we gathered information, we decided to allow them to wait out the market. The markets have recovered tremendously since March and that solvency issue solved itself."

PANDEMIC INTERRUPTION COVERAGE

Pandemic coverage will be the next big risk put into captives. Because of lack of actuarial data, pricing in the traditional market will be expensive, so many regulators foresee that captives will be used for this type of coverage. The captive sector was already in a position to grow in 2020 before the pandemic hit. Now that the insurance market has constricted and pricing is soaring, captives will be an important way for businesses to access pandemic risk.

Going hand-in-hand with pandemic coverage is business interruption, and the range of specific exposures that it encompasses. Examples of business interruption products are loss of key supplier, loss of key customer, employee loss, supply chain interruption, and political risk. Businesses that are experiencing losses right now are learning that pandemic triggers are excluded from their business interruption policies.

- Consulting
- Case Management
- Big and Small Data Analysis & Predictive Modeling
- Claims Audits
- Risk Management

Aratai
INTERNATIONAL
LEADERS IN INTERNATIONAL HEALTH CONSULTING

customerservice@arataiinternational.com
www.arataiinternational.com

Call Us Toll Free: (888) 448-2470

Aratai International provides services to build and develop cost-effective and high quality healthcare strategies. We invest time in understanding your business goals, and we develop programs to help you reach them. We are committed to developing strong business relationships by exceeding your expectations.

MEDICAL LEGAL | CONSULTING | MANAGEMENT | DATA ANALYSIS

More captive owners and potential captive owners will be looking to add insurance that specifically does not exclude pandemic risk.

While captives will prove to be a good solution to obtaining business interruption and pandemic risk insurance, regulators do have concerns about how and why pandemic risk will be covered in a captive. Concerns about conditions, coverage triggers, and pricing are at the top of that list.

For Kurata, "Like any other new, or unique risk, with limited historical data, in my opinion the most significant concern would be the adequacy and accuracy of the premium pricing and underwriting and reserving of the coverage."

In a second ICCIE webinar in June, David F. Provost, deputy commissioner of the Captive Insurance Division with Vermont's Department of Financial Regulation – Captive Division, was most concerned about what will be the triggering factors for pandemic coverage, if pandemic risk would be a good product for pooling, and putting limitations on how that money could be loaned back to the parent company.

According to Wegkamp, "I expect to see pandemic risk being put into captives as both a business interruption type policy and as a standalone risk. I have no objections to either; however, given this new type of coverage we will be taking a look at the proposed policies to ensure they are well defined with specific triggers, exclusions, etc. What I don't want to see are broad generic policies that would appear to be a 'catch-all' for any type of business interruption or loss of income event."

For David Piner, director of the Captive Program at the Michigan Department of Insurance and Financial Services, speaking on ICCIE's webinar, "It all comes down to the price. A captive can underwrite an unusual amount of coverage, as far as variety goes, so certainly if they want to do something akin to a business interruption policy that wouldn't exclude pandemics, that's fine, but let's see how much you are going to charge for that."

However pandemic interruption coverage is used, one positive thing the pandemic can offer is data towards a future similar incident. "It's a unique opportunity given that many of these companies that are interested in writing pandemic coverage is that they've experienced first-hand what their potential losses are and how it's going to affect their businesses. It's not multiple years of history but it is some experience," said Wegkamp.

WHAT THE FUTURE HOLDS

Going forward, reaction to the pandemic and a hard insurance market will mean growth for captives. The licensing and regulation of captives will not likely see any significant changes, but regulators might see some changes in how captive owners assess their risk. The pandemic caught nearly everyone off guard and will, hopefully, remind captive owners to assess their risks and coverage more often.

"As far as how the pandemic may change or improve captive operations," said Walker, "It seems that the pandemic (as well as the hardening commercial market) will likely lead to captive owners further evaluating their insurance program and assessing the benefits of using a captive insurer to determine if there are business risks that should be insured by a captive."

Kurata agrees, "I think it is a strong reminder of the importance of prudent regulation of captives in that it is important to monitor the solvency of captives and that they are properly capitalized and not overly reliant on investment rates."

While the pandemic is an adverse event, captives are showing their capability to insure unusual risks. "The captive industry is a unique and inventive one; the owners and parent companies of these captives, like everyone else, have experienced an event like none we've ever faced before," said Wegkamp. "I'm certain there will be many changes and/or improvements proposed and experimented with to mitigate the effects of a possible similar event in the future." ■

Karrie Hyatt is a freelance writer who has been involved in the captive industry for more than ten years. More information about her work can be found at: www.karriehyatt.com.