



SymmetRE

Frequently Asked Questions

What is the Symmetry Reinsurance Treaty (SymmetRE)?

SymmetRE is a contractual risk-sharing agreement among participating captives. It is not a company, partnership, or other legal entity. Special features of this contract make it ideal for captives seeking to underwrite unrelated risk in a cost-effective way.

Why was SymmetRE started?

SymmetRE was created to meet the needs of captive owners who wish to diversify their underwriting portfolio by writing unrelated risk and stabilize loss costs. Traditionally, captives sought unrelated risk through the reinsurance market, but poor experience and more stringent security requirements (i.e. increased capital & surplus) have rendered captive participation in the traditional reinsurance market extremely difficult in recent years.

What are the capital requirements of SymmetRE?

SymmetRE is not an entity and therefore requires no commitment of capital.

Captives that write their parents' primary Workers' Compensation exposures will find that they need no additional capital in their captive. Those captives that do not currently write their parent's primary Workers' Compensation coverage may have to increase their captive's capital to support the increased premium writings. Capital requirements differ by domicile and you should consult your captive account manager to explore this issue further.

What lines of coverage can I put into SymmetRE?

SymmetRE accepts the primary exposures (\$100,000 per occurrence) for Workers' Compensation and Employers Liability coverage.

What if I am currently self-insured or subject to a deductible program?

In order to participate in SymmetRE a captive must underwrite the primary Workers' Compensation exposures of the parent. The parent can keep its existing program structure in place and use an indemnity contract or deductible reimbursement program to superimpose the benefits of captive funding within the existing program structure.

How are premiums determined?

The same independent actuarial firm calculates premiums for all participants. Premium is equal to the expected losses during the Treaty year. The selection of a single actuarial firm ensures common methodology. Any bias that may exist should be consistent for all participants.

The premium is converted into a Participation Percentage by dividing it by the sum of all participants' premium amounts. This Participation Percentage is used to allocate actual loss payments. As long as the actuary uses common methodology the rating integrity is preserved. Consistency is the key to equity among the participants.

My risks are being effectively managed, why would I want to share risk with others?

SymmetRE reduces the variability of losses without changing the expected cost of claims. This is clearly an economic benefit to participating captives. Companies that have an effective risk management program presumably have lower rates of loss than competitors. Since SymmetRE is rated based on expected losses, lower costs will translate into lower premium and lower Participation Percentages.

Sharing risk does not mean giving up the competitive advantage that effective risk management programs provide.

Also, participating captives may obtain sufficient unrelated risk to permit the captive to establish tax status as an insurance company. These are two significant improvements to any risk management program.

If I participate in the SymmetRE how will my current arrangement for claims payment and administration change?

For companies that use a captive to underwrite the deductible portion of their primary Workers' Compensation program, SymmetRE requires no restructuring of the current risk financing program. The captive can continue to reimburse the claims administrator or fronting carrier for claims, unaffected by participation in SymmetRE. SymmetRE is a reinsurance arrangement not an insurance arrangement.

For companies that do not currently use a captive or protected cell, no change is required with respect to the primary carrier or claims administrator. The captive (or cell) would simply write a deductible reimbursement policy and reimburse the company for losses falling within the deductible. The deductible amount must be at least \$100,000 per occurrence (or greater) as the first \$100,000 would be reinsured through SymmetRE.

How am I protected from adverse loss experience?

There are several safeguards built into SymmetRE to protect participants against adverse loss experience, including a low limit and a spread of risk.

1. Participant peer group underwriting affords a great deal of discretion over who may join SymmetRE.
2. The program covers only primary losses at a low limit. Losses within the low primary retention have relatively low variability and thus loss projections are relatively accurate in this range.
3. The SymmetRE pooling arrangement spreads risk over many different companies. The effect of adverse experience will similarly be spread over this large group.
4. The program has a batch clause that protects participants from a sequence of related events. (See SymmetRE Treaty Agreement, Article 6.5.) For example, an accident at a manufacturing facility that results in a number of injuries would be treated as a single claim for purposes of applying the limit.
5. A participant's maximum available reinsurance limit from SymmetRE is 200% (2x premium).
6. There is a "loss stabilization plan" (LSP) contained in the Treaty Agreement which is designed to shift some of the profit made by SymmetRE participants with higher than expected loss results, and return such funds to participants that incur losses through SymmetRE as a result of lower than expected individual loss results. The "loss stabilization" feature will work to reduce a participant's underwriting loss or profit depending on their individual results.

What happens if SymmetRE becomes insolvent?

SymmetRE is not an entity and cannot become insolvent. The obligations of SymmetRE are really the obligations of the participants (to each other).

Participating captives are unlikely to become insolvent. Few single-parent captives have become insolvent. In fact, captives typically survive the insolvency of their owners. Nonetheless, a great deal of careful consideration and research has been undertaken to assure that if a participant were to become insolvent, that any potential credit risk of remaining SymmetRE participants are minimized. Procedures have been established to ensure such protection. For example, SymmetRE's Manager (Marsh) will not pay a participant until any amounts due from

such participant are received ("Pay-as paid" clause). If a participant becomes insolvent, its participation is immediately terminated. Additionally, the Treaty contract provides for offset of amounts owed to the insolvent participant by amounts owed by such participant to the other members of SymmetRE. As a result of these contractual elements, the remaining participants are at risk of credit loss only in the event and to the extent that the insolvent participant owes more in loss payments to SymmetRE on a net basis than it is owed from SymmetRE.

Tests of the parent and captive's financial health are mandatory application requirements and are tested on an on-going basis.

How will SymmetRE affect my captive's cash-flow?

Premiums transferred to SymmetRE will always equal premiums received from SymmetRE. Under normal operation, SymmetRE will retain no cash. Each of the participating captives retains the funds needed to pay claims.

Companies will have to use their captive to underwrite primary Workers' Compensation exposures. However, the captive will retain funds until they are needed to pay claims.

Assuming captives are able to deduct reserves (including reserves for claims that have been incurred but not reported) when calculating taxable income, the captive's cash flow is increased by reducing the amount of tax payable.

What is the impact of SymmetRE on my captive's investment income?

Captives that are directly subject to U.S. taxation and are able to achieve status as an insurance company from their participation in SymmetRE will begin to deduct reserves when calculating taxable income. As a result of the accelerated deduction for loss reserves, the U.S. consolidated income tax return of which the captive is a member (if any) will defer payment of U.S. income tax which has the effect of increasing the amount of cash the taxpayer will have to invest, thus boosting investment income.

For offshore captives whose income is taxed as Subpart F income, participation will not have an effect on investment income.

Will SymmetRE impose restrictions on my captive?

SymmetRE requires demonstration of financial health of both the captive and its parent. Those companies whose captives fail to meet certain financial ratios will have to bring the captive in line with these requirements.

There are no specific provisions of SymmetRE that would prevent the captive from investing in its parent company.²

What is Federal Excise Tax and how does it impact the program?

Federal Excise Tax (FET) is a tax imposed by the U.S. Government for premiums paid to foreign insurers



covering U.S. risks. The purpose is to equalize the playing field between U.S. insurance companies that pay U.S. tax and foreign insurers, which may not. FET, however, is not due on arrangements that are treated as self-insurance for U.S. tax purposes.

By participating in SymmetRE, some companies may find the U.S. tax status of their captive change from self-insurance to true insurance for U.S. income and excise tax purposes thereby subjecting their transactions with their captive to U.S. FET. The FET applies at 1.00% on reinsurance transactions and 4.00% on direct contracts of insurance.

Captives domiciled offshore that participate in SymmetRE may find their transactions subject to FET in two areas. First, on the (insurance or reinsurance) arrangement between the parent and the captive; secondly, on the transactions between the captive and SymmetRE.

Captives can make a tax election under Section 953(d) of the Internal Revenue Code that exempts transactions from FET. This election has the effect of treating income in the captive as if it had been earned in the U.S.

Private companies (S Corps, partnerships, etc.) may find that the election subjects them to a second level of taxation.

A thorough discussion of this election is included in the Participants Information Document - Appendix 2. Note that due to a clause in the SymmetRE Treaty Agreement, foreign captives that do not make the election will be responsible for payment of FET associated with the transaction on behalf of the domestic / 953(d) captives.

Is SymmetRE subject to tax?

SymmetRE is not a taxpayer. Since it is not an entity it will not have any income. Participating captives are likely to be either directly taxed or have their income taxed as U.S. controlled foreign corporations. The filing of income tax returns is the responsibility of the participating companies.

What other frictional costs might I encounter as a participant?

The Marsh Management SymmetRE Fee should be the only frictional cost that participants will incur in their transaction through SymmetRE. The fee covers normal operational and management expenses of the pooling arrangement.³

The premium ceded to SymmetRE is the primary factor in the determination of the management fee. A fee schedule is included in Exhibit B of the Treaty Agreement.

There are several classes of frictional costs that a participant may need to take into account when structuring the transaction between the captive and its parent or policyholder.

1. Fronting costs in the event the captive chooses to reinsure its parent's risk.
2. U.S. domiciled captives will be subject to premium taxes based on their specific domicile regulations.

3. U.S. companies may find that the insurance policy between their captive and parent (policyholder) is subject to direct placement or self-procurement taxes. These taxes are imposed on insurance transactions with non-admitted insurance companies. They are imposed on a state-by-state basis at varying rates.

This is the same tax that may apply to ACE/XL and other offshore insurance placements. You should consult your tax advisors since many companies have already explored the applicability of this tax.

What if I want to leave SymmetRE?

We anticipate that only those companies that are looking for a long-term arrangement will enter SymmetRE. Nonetheless, participants may find reason to change their minds and decide to leave. For example, a participant may undergo significant operational changes that no longer make SymmetRE a good fit within their risk management program.

A participant can elect to exit SymmetRE by giving the manager 120 days prior written notice from the annual renewal date. In such an event the captive must secure unpaid claims with a letter of credit or other acceptable collateral instrument. The required amount is detailed in Schedule 4 of the Treaty Agreement.

How is SymmetRE run and governed?

The participants' committee is made-up of a representative of each participating captive and operates on the principle of one-person-one-vote. The participants' committee elects members to sit on sub-committees that direct the general operation of the Treaty arrangement. There are two main advisory sub-committees (Underwriting and Audit & Finance Committees) comprised of elected participants that will act on a range of issues which include:

1. Audit of the administration of the program (Audit & Finance Committee);
2. Review of underwriting information for participants, (Underwriting Committee);
3. Review of financial strength of participants, (Audit & Finance Committee);
4. Review any recommended changes to Treaty Agreement wording, (Underwriting Committee);
5. Setting of underwriting criteria for SymmetRE, and (Underwriting Committee);
6. Establishment of minimum financial standards for participants and their parents. (Audit & Finance Committee)

² Appropriate tax advice should be sought before entering into such a transaction

³ The cost of managing your captive is not contemplated in this amount. Details related to SymmetRE Expenses are contained in the Treaty Agreement.

The two advisory committees provide recommendations to the executive committee. The executive committee has the primary decision-making authority to determine all matters relating to the overall operation of SymmetRE. This committee is made up of seven elected participants including, the chairperson and deputy chairperson of the participants' committee, underwriting committee, audit & finance committee and past chairperson of the participants' committee.

Approval of new participants requires a supermajority approval from the participants committee.

It is important to recognize that the committees are advisory and decision-making bodies and not merely working groups.

Has anything like SymmetRE worked before?

Pooling arrangements are common in the insurance industry. SymmetRE capitalizes on the success of the Green Island Reinsurance Treaty. Green Island is managed by Marsh and has been in existence since January, 1997. It is recognized as the most successful facility of its kind. As of 2009, Green Island consists of 16 member companies with estimated annual premiums totaling \$380 million. SymmetRE will be structured in a similar manner as Green Island, and made available to companies with lower expected losses than Green Island's minimum threshold.

Who can join SymmetRE?

Captives insuring risks from parents in a wide range of businesses may participate. Applicants must complete the SymmetRE Application. There are a number of factors that will go into the selection of participants. To summarize the points, applicants must be able to demonstrate:

1. Financial strength of the participant (captive);
2. Financial strength of the participants' parent;
3. Attention to safety and loss control;
4. Risks acceptable to participants;
5. A recent valuation of the past 5 years of loss data and corresponding exposure information to support the development of loss estimates.

What risk factor should I be most concerned with?

Perhaps the most significant concern is the setting of Participation Percentages. This is performed by a single actuary to try to eliminate any bias introduced by using different firms. What is important is the relative Participation Percentage, not the calculation of the absolute value of claims. If the actuary's projections are too high by 10%, as long as they introduce the same 10% bias to all participants, experience in SymmetRE will be unaffected since the participants loss costs would still constitute the same percentage as they would have in the absence of the 10% bias.

In any one year there is roughly a 50% chance that the estimate of losses, and thereby the Participation Percentages, will be too high and a 50% probability that the estimation of losses is too low. It will be impossible to tell in any single year if the Participation Percentage accurately reflects your company's true exposure to loss.

In the event that the Participation Percentage is set too high, meaning that your company receives a higher allocation of premium and claims, participation in SymmetRE may still produce a net benefit when all other factors are considered.

What is the maximum limit of SymmetRE? How does that work?

The aggregate limit for each underwriting year for each member will be 2 times, or 200%, of that member's expected losses for the underwriting year.

As a practical matter, SymmetRE limits the amount that a participant can receive as payments (recoveries) from SymmetRE to substantially the same as 200% of premium (expected losses). This in effect also limits the most any single participant can pay into SymmetRE to the economic equivalent of 2 times their expected losses. Loss variability of the pooling arrangement is discussed in Section 9 of the Participants Information Document. The possibility that SymmetRE, and therefore a participant, will actually pay 2 times expected losses is statistically remote.

It is interesting to compare the impact of several different scenarios to existing programs where the parent of the participant retains primary limits. It must be stressed that the probabilities of these events actually occurring are extremely remote. Let's consider an example of a participant with a \$2,000,000 premium and total SymmetRE pool of losses of \$40,000,000. The most that the participant can receive as claim recoveries from SymmetRE is \$4,000,000.

Once the participant has received \$4,000,000 in claim recoveries the participant is still responsible for payments according to their Participation Percentage. In this case, the participant's obligation to pay claims terminates only when their claim payments made to SymmetRE reaches \$4,000,000. For this to happen ALL participants must breach their aggregate cap, an extremely remote possibility.

1. What happens if every participant exceeds the aggregate? In our example, the participant will effectively pay \$4,000,000 of losses to SymmetRE, but at the same time will recover \$4,000,000 of their losses from SymmetRE. In this example the participant, from an underwriting perspective, will not be worse off for participating in SymmetRE.

2. What happens if everyone, except your company, exceeds the aggregate limit, and your company incurs losses as expected (assumed at \$2,000,000)? In our earlier example, SymmetRE will incur \$78,000,000 in losses and your share will be 5%, or \$3,900,000. Given expected losses of \$2,000,000, we can view \$1,900,000 as the amount at risk. Note - this calculation does not consider the loss mitigation impact of the loss stabilization plan (LSP) which would serve to significantly reduce the underwriting loss. Based on this particular example, LSP would remove approximately \$1,400,000 of the loss so the resultant amount at risk would be \$500,000.
3. What happens to a participant that reaches the 200% level? The answer is largely dependent on the overall results of SymmetRE. If that occurs and the rest of SymmetRE performs as expected, the participant will make \$2,100,000 in loss payments to SymmetRE and will recover \$4,000,000 from SymmetRE (\$200,000 from the participant's own captive).

It is important to recognize several facts:

1. SymmetRE, through its size and the additional stability resulting from a greater volume of covered losses, should be expected to have significantly more loss stability than any one participant alone. The possibility of overall SymmetRE losses reaching the aggregate limit is remote. In addition, if that were to occur, it would probably be due to events that impact all participants, such as hyperinflation. The relative Participation Percentages would retain a good deal of their integrity in reflecting losses that we expect a single member to contribute to the pooling arrangement.
2. The discussion above regarding significant adverse loss experience (up to the policy limits) has dealt with pre-tax effects. SymmetRE permits captive owners who wish to diversify their underwriting portfolio to write unrelated risk and stabilize loss costs, and may permit participating captives to obtain sufficient unrelated risk to establish tax status as an insurance company and to deduct reserves (including reserves for claims that have been incurred but not reported) reducing taxable income and cash taxes. Upon factoring in the tax benefit of participating in SymmetRE, particularly over a number of years, the unique scenarios considered here would not necessarily render participation uneconomical over time.

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