ASSOCIATION OF INSURANCE AND REINSURANCE RUN-OFF COMPANIES

AIRROC® MATTERS

A NEWSLETTER ABOUT RUN-OFF COMPANIES AND THEIR ISSUES

www.airroc.org

Special Issue: AIRROC®/R&Q Commutation Event

Rendez-vous 2010

Message from CEO and Executive Director

Still Flying High

Trish Getty

Reflecting on the October 2010 AIRROC/R&Q Commutation & Networking Event, all of the work, coordination, planning, sweat, etc. were worth it since we had yet another resoundingly successful event. We are grateful to the Event Chair Art Coleman, the R&Q event workers, the sponsors and so many others who again made this possible.

Pleasant flashbacks include the honor given to our Editor In Chief, Peter Scarpato. His endless work on "AIRROC Matters" is greatly appreciated. In the beginning, I recall Peter's and Ali's dream to produce a meaningful newsletter. With the tireless, productive help of our excellent Publications Committee, they have succeeded without a doubt.

Gavin Souter, *Business Insurance* Managing Editor, gave an insightful keynote luncheon address, certainly food for thought as the market continues to shift.

During the Gala Dinner I sat beside Mindy Kipness and observed the wringing of her

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Message from Publications Committee Chair

A Bientôt, My AIRROC Friends

Ali Rifai

As many of you know this is my last issue as Publications Committee Chair of AIRROC Matters. This note reflects on our accomplishments and highlights the contributions of our Publications Committee members.

Our original black and white editions have given way to glossy, color ones with many added sections like "Present Value" and "Legalese." Innovative concepts were developed, like this *Rendez-vous* edition dedicated to the annual October meeting, and the Special Editor issue (the brainchild of our Editor-in-Chief Peter Scarpato) where brave souls volunteer to edit, with the committee's support and collaboration, a newsletter dedicated to a single theme deemed to be of interest to our run-off audience. Despite all the changes, we have remained true to our core mission of providing well written, timely and sometimes provocative articles we believed to be of interest to our core run-off audience.

Despite all the changes, we have remained true to our core mission of providing well written, timely and sometimes provocative articles we believed to be of interest to our core run-off audience.

Of course, none of this was possible without the dedicated members of this committee, who somehow found time in their busy schedules to volunteer. Each edition requires finding authors (although we've been blessed on this front as our struggle has generally been our inability to publish immediately all the articles we receive), getting the articles, reviewing and editing them, getting the advertisements ready and making

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The AIRROC/R&Q Commutation and Networking Event Oct 18-20, 2010. *See more inside…*

The right people in the right places

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Simply, we have the right people in the right places.

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A Bientôt, My AIRROC Friends

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sure that all is coordinated with the precision of a Swiss watch (well, almost!). As I mentioned during the Rendez-vous event, we are like a finely tuned orchestra: staffed with dedicated professionals, each performing the assigned task with precision; no *prima donnas*; no one more important than the other, and with the understanding that one wrong note will make the whole production falter.

As I proudly hand over my gavel to our incoming co-chairs Colm Holmes and Leah Spivey (see below), I want to thank each committee member, our publicist and design and production teams, and especially Peter Scarpato for making my tenure so easy and enjoyable. I also want to thank the Board members for their unwavering support and Trish Getty for her dedication, encouragement and support. I will cherish the experience but will not say goodbye as all have become, and hopefully will remain, my friends for a long time. So, as they say in Paris, *a bientôt.* ■

AIRROC Welcomes Incoming Publications Committee Co-Chairs Colm Holmes and Leah Spivey ...

Colm Holmes

Colm Holmes, located in Dublin, Ireland, is the CEO of Zurich's Centrally Managed Business. As a result of the review of banking by the group's Bank Steering Committee, Colm was appointed Head of Banking for Zurich, and now manages the run-off of the Banking operations predominantly in the UK and Ireland. In his capacity as CEO of CMB, Colm retains responsibility for Zurich's other run-off businesses and continues to develop exit strategies for these businesses.

Colm graduated from Trinity College in 1988 with an honours degree in Finance and is qualified as a Chartered Accountant in the UK. In addition to co-chairing the Publications Committee, Colm is a member of AIRROC's Board of Directors. He can be reached at colm.holmes@zurich.com.

Leah Spivey

Leah A. Spivey is a Vice President and Account Executive at Munich Reinsurance America's Business Run-Off Operations. Her responsibilities involve managing a portfolio of accounts with liabilities from 2001 and prior. Leah began her career at Kemper Group in Massachusetts and held various claims management positions at General Accident and the Home Insurance Company before joining Munich Re in 1993.

Leah graduated from the University of Massachusetts in Amherst with a BA in Journalism and Communications. She has her CPCU designation and is a certified training designer and developer. In addition to co-chairing the Publications Committee, Leah is a member of AIRROC's Board of Directors. She can be reached at lspivey@munichreamerica.com. ■

Rendez-vous 2010

AIRROC® Matters

Education Summaries July 15, 2010

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AIRROC® Board of Directors

Our Worldwide Depth Of Resources

Chadbourne's insurance and reinsurance practice brings worldwide resources to every matter concerning our clients.

Our lawyers draw on their broad range of legal expertise throughout the United States, Europe, Bermuda, Latin America, and Asia to address the most complex (as well as routine) transactional, regulatory, insolvency, investigatory, and dispute related issues.

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Our practice consistently achieves high rankings. In 2010, *Chambers USA* ranked David Raim, co-chair of our reinsurance group, as one of the top reinsurance attorneys in the United States. David Raim, John Finnegan, and John Sarchio of our U.S. reinsurance group, as well as Adrian Mecz and Chris Cardona of our London reinsurance group, were included on the "Best Lawyers" list published by *U.S. News & World Report*. Our U.S. and London based reinsurance groups were also awarded high rankings by both *Chambers USA* and *Chambers UK*.

The Chadbourne partners and counsel who keep on top of the industry for our clients are:

Partners – United States
Robin Ball
Carey Child
John Finnegan
Philip Goodman
Joy Langford
Mary Lopatto
William Perry
David Raim
John Sarchio
Howard Seife (Insolvency)

Partners – London
Christopher Cardona
Michelle George
Adrian Harris (Insolvency)
Adrian Mecz
Mark Pring

Counsel – United States
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It was the 6th year of AIRROC's successful Rendez-vous

Pictured: **1.** Tim Stalker (Stalker Vogrin), Mike Walsh (Boundas, Skarzynski), Nick Pearson (Edwards Angell). **2.** Reception with a smile! Bryina Starks, Ann Beaulieu (R&Q), Julie Jordan (R&Q), Julie Ponsford (R&Q). **3.** Jim Veach (Mound Cotton Wollan & Greengrass) & Carolyn Fahey (HB Litigation Conferences). **4.** Karen Amos (Resolute Mgmt.) & Brenda Craven (Hartford). **5.** Bryina Stark, such a gracious host. **6.** Richard White (Integrity Ins. Co.), Bob Shortell, Jim Moran (R&Q), Andrew McCarthy (R&Q). **7.** Opening Session. **8.** "Down to business." **9.** Richard Emmett (PRO). **10.** Ed Stanley. **11.** Mike Walker (KPMG), Della Van Kempen (Swiss Re), Simon Hawkins (PRO).

Pictured: **1.** Jeffrey McMurry, Patti Henry and Mark Akamine of CLO, Chris McColl (Reinsurance Solutions). **2.** Robert Shortell (independent consultant), Bina Dagar (Ameya Consulting, LLC) and Mike Flaherty (FTI Consulting). **3.** Bruce Friedman (Rubin, Fiorella) and Ali Rifai (Zurich). **4.** Klaus Kune and Andrea Lerch of Hannover Re. **5.** Susan Aldridge (Chadbourne Parke). **6.** Peter Scarpato (Conflict Resolved, LLC) and Trish Getty (AIRROC). **7.** AIRROC Matters production team: Jean-Marc Grambert (Myers Creative Services), Gina Pirozzi (G. Pirozzi Consulting). **8 & 9.** "Down to business." **10.** Bill Littel (Allstate), Vivien Tyrell and Daniel Seville (Reynolds Porter), Henry McGrier (Allstate). **11.** Andrew Maneval (Chesham Consulting), Mitchell King (Prince Lobel Glovsky & Tye), Charlie Fortune (Day Pitney). **12.** "Down to business."

HB Litigation Conferences Education Session Summary – Rendez-vous 2010

Challenges Facing Run-Off Companies in the Current Operating Environment

Left to right: John Parker (TIG/RiverStone), Steven Schwartz (Locke, Lord) and Mike Walker (KPMG). Attendees.

Summary by Maryann Taylor, Boundas, Skarzynski, Walsh & Black, LLC

The panel on Challenges Facing Run-off Companies was chaired by Marvin Mohn, General Counsel of Tawa Management Ltd. Joining him on the dais were Mike Walker, Partner at KPMG and head of Restructuring Insurance Solutions, Steven Schwartz, Partner at Locke Lord Bissel & Liddell and John Parker, Senior Vice President and Reinsurance Counsel of TIG Insurance Company. The discussion began with Mr. Walker providing the results of the Non-Life Run-off Survey for 2010 – UK Market conducted by KPMG. The key findings of the survey illustrated that the traditional APH-based run-off market is in decline, new run-off has different characteristics and that solvent schemes have risen dramatically. Total liabilities of the UK run-off market are estimated at £29.7 billion, a decrease of £7.7 billion since 2008. As of year end 2009, a total of 227 solvent schemes of arrangements had become effective with liabilities of UK companies subject to such schemes totaling approximately £527 million. It was noted that the characteristics of the schemes have changed in that the scale of the current schemes are getting bigger and the geographical reach expanding in that you have schemes being used by non-UK companies.

Mr. Walker also discussed the results of interviews with top management primarily in the UK that was conducted to ascertain their view on the challenges facing the run-off market. At the top of the list was Solvency II due to the great degree of uncertainty regarding the new capital requirements scheduled to come into effect December 31, 2012. The second concern mentioned most frequently was investments, not surprising given the current low interest rate environment. The lack of investment return is changing everyone's game plan. The third ranked issue was the UK asbestos situation and the uncertainty regarding the ultimate cost, which is estimated between £6 to £11 billion.

> *The consensus of the panel was that there is a tremendous amount of talent in the run-off market and how you deploy that talent and make money in a declining market is a significant challenge.*

Mr. Mohn commented that although Solvency II gets a huge amount of attention, the true impact will depend on the type of company and whether the objective to get capital released from the company in the short term verses a company that is pursuing a commutation or

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Left to right: John Parker (TIG/RiverStone), Steven Schwartz (Locke Lord), Mike Walker (KPMG) & Marvin Mohn (Tawa Management)

Education Session Summary - Rendez-vous 2010

Interactive Workshop – "SURVIVOR!"





Top row from left: Intense listeners Bob Sherwood (Midland/NYLB), Keith Kaplan (Reliance), Joe McCullough (Freeborn & Peters), and John Proscio (ROM); LPT team at work; Bill O'Farrell (ACE). *Bottom row:* Will they make it off the island?; Steven Herman (Asset Discovery Associates).

Summary by Bina Dagar, Ameya Consulting, LLC *and Peter Scarpato,* Conflict Resolved, LLC

The SURVIVOR! program was a new, more interactive presentation conducted over a morning and afternoon session. The workshop was introduced by Bill O'Farrell, who asked company executives Michael Fitzgerald, Thomas Ryan, Andrew Maneval and Jason Russ to present the case study of, and to develop options for, Maple Falls Insurance Company, a successful main street insurer considering run-off due to adverse development and regulatory problems from the expansive underwriting and emerging liabilities of its 1974 acquisition of Old Smokey Insurance Co., Ltd.

Facilitator Bill O'Farrell & Ceding Co. Team

The three run-off options under consideration - loss portfolio transfer ("LPT"), traditional run-off ("Run-off"), and company sale ("Seller") - were split among three teams of Leaders and Facilitators: LPT - Thomas Ryan, Lloyd Gura and Robert Hermes; Run-off - Joseph McCullough, Susan Aldridge and Andrew Maneval; and Seller - Michael Fitzgerald, Steven Anderson and Darryl Ashbourne. Audience members were split among the three groups. Their charge was to split up, review the information presented and documents received, and return at 11:30 AM to develop their proposals.

During the morning session each group diligently worked on their respective tasks:

- Run-off group explored putting the whole company into run-off, focusing on staffing issues, possible claims against management and their errant CAT modeling company, and questions about the depth of the reserve hole. Additionally, they considered selling the assumed reinsurance unit to fund the run-off operation or merging Old Smoky and Maple Falls.
- Seller group analyzed the balance sheet to determine the company's true value, examining items like goodwill, assets, bonds, insurance recoverables and renewal rights. Particular attention was given to the

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impact of midpoint or high/low reserve estimates.

- LPT group discussed various options including reinsurance protection, a suitable LPT provider and either a retention or co-insurance structure, ultimately debating whether they could ever buy an affordable LPT to avoid insolvency.


Facilitators Susan Aldridge and Andrew Maneval

The three groups reconvened in the afternoon to continue exploring strategic options available to the Board of Maple Falls Insurance Group in run-off during Year 3 and onward. The industry panels reviewed again the options and outcomes of selling, self-managing, and outsourcing. At the end of the session the three groups came together to discuss the results of their decisions.

The proponents of a sale felt that the overall sale value was $300 million and that the Board's decision not to do anything two years before cost the company's value to deteriorate from $400 - 600 million to $240 - $360 million. The proponents of a LPT concluded that new variables interjected some confusion. They agreed that potential reinsurance is a critical consideration for a LPT; they agreed to negotiate for additional reinstatement limits.

The discussion then moved to the need for protection for its high asbestos exposure of $200 million. The panel decided to shop the market for price while continuing to run off. At the same time, they wanted to continue to evaluate whether the current problem valued at $100 million would remain or increase. With some clarity three years later, the catastrophe exposure is known and certain but other aspects such as the non-products asbestos have come to the fore.

To limit the risk, the panel decided to structure a cover that would help with a worst-case scenario. The panel recognized that a LPT would become more expensive over time. They proceeded to discuss the structure of an acceptable LPT that would have a loss corridor plus an adverse development cover above the loss corridor.

After much discussion, the Runoff panel recommended continuing to run off for one more year while aggressively managing the commutation program. They agreed to retain the UK operation and seek retrocession behind the UK portfolio. They discussed the notion of a revamped system to consolidate the US and UK operations. The panel expressed their concern that the other options of selling the company and LPT would expose the Board to suits of negligent non-disclosure or material misrepresentation. This neatly corroborated with their conclusion to stay in run-off until the company has a better handle on potential losses.

All three panels held animated discussions and displayed unprecedented high group involvement. It was clear that participants had read the materials and were eager to contribute to the general discussions. Group leaders did an excellent job at keeping the discussions moving and reporting to the Board. ■


Speakers and Facilitators from left: Mike Fitzgerald (Scan Re), Jason Russ (Milliman), Bill O'Farrell (ACE), Andrew Maneval (Chesham Consulting), Thomas Ryan (Berkshire Hathaway), Susan Aldridge (Chadbourne & Parke), Robert Hermes (Butler Rubin), Jonathan Bank (Locke Lord), Kathy Barker (Armour), Joe McCullough (Freeborn & Peters)

A Special Award for a Special Editor: Peter Scarpato



From left: Ali Rifai (AIRROC Publications Committee Chair, Zurich); *Foreground*: Peter Scarpato ("AIRROC Matters" Editor-In-Chief, Conflict Resolved, LLC), *on his left,* John Parker (TIG/RiverStone), *on his right,* Oliver Horbelt (Munich Re); Ali Rifai delivers award to Peter Scarpato.

By Bina Dagar, Ameya Consulting, LLC

At the October 2010 AIRROC Commutation & Networking Event in East Brunswick, NJ, Peter Scarpato received a special award in recognition of his work as Editor-in-Chief of the newsletter, AIRROC Matters. Peter, who is Co-chairperson of AIRROC's Publications Committee, has created and upheld the vision for this newsletter from its conception, which coincided with the birth of AIRROC in 2004. He has worked tirelessly to produce a high-quality newsletter covering run-off company issues. Every newsletter is packed with articles of educational value that are topical and that provide news to the membership. Accepting the award, Peter called his role a "labor of love."

The newsletter is published three times a year with one special edition focusing on the annual Commutation and Networking event. Peter proactively manages each publication from its starting phase to it completion. As Ali Rifai, Co-chairperson of the Publications Committee put it, "Peter corrals the committee together. He is like a conductor without whom we would have a cacophony of sounds." Acknowledging the committee members, Rifai added, "Peter is a conductor of talented musicians."

Peter has proven himself a leader. He founded Conflict Resolved, LLC in March 2005 to do what he loves best – resolve disputes.

Peter has proven himself a leader. He founded Conflict Resolved, LLC in March 2005 to do what he loves best – resolve disputes. Since then, he has taken an active leadership role in other organizations, the latest being the Re/Insurance Mediation Institute (ReMedi), which he co-founded. Through ReMedi, Peter continues to spread the word about the benefits of mediation and to put to good use his experience as a frequent lecturer on alternative dispute resolution of insurance and reinsurance issues. Peter has published articles in various trade journals. Currently, he is on the Board of Editors of Harris Martin's Reinsurance Report. As if that is not enough, Peter is a frequent instructor for ARIAS-US arbitrator training workshops and volunteers his time to participate in mock mediation training sessions at NYU School of Law in New York City.

Peter gained a law degree from Rutgers University. He is a licensed attorney in New Jersey and New York; but his heart is in dispute resolution, which he declares allows him to be a part of the solution. He enjoys the give and take and working with people to resolve a problem.

Congratulations Peter on a well-earned award! ■

Peter Scarpato, Trish Getty (AIRROC CEO & Executive Director), Ali Rifai (Zurich)

Keynote Address by Gavin Souter

By Bina Dagar, Ameya Consulting, LLC

At the AIRROC Commutation & Networking Event in October 2010, Gavin Souter, Managing Editor of *Business Insurance*, gave the keynote address. Mr. Souter graduated with a B.A. in Theology from the University of Nottingham, England. His professional career includes stints as Assistant Editor of *The Stock Broker & City Investor*; Reporter at *Post* magazine; and Editor of *Reinsurance* magazine.

Gavin Souter, Managing Editor of *Business Insurance* and Keynote speaker

Commenting on the outlook for the property/casualty ("P/C") insurance market, Mr. Souter noted that on the surface the industry may appear not much changed over the past couple of years. However, the truth is that the market has been soft for five years now; the sluggish economy is unlikely to alter that especially when there is an increasing overcapacity and limited prospects for growth. With the low interest rate environment and the resulting low investment returns, cash flow underwriting of the past is not a viable option either. Despite this gloomy picture, the US insurance industry is looking fairly stable. Large commercial insurers' results tracked by *Business Insurance* showed decent profits for the first half of 2010, with the top ten insurers posting a 98.1% combined ratio. Generally, with a few exceptions, P/C insurers weathered the financial crisis reasonably. There have been no major insolvencies or insurers in financial difficulty. So one may conclude the industry is managing with average returns much to the envy of many other sectors.

A further analysis, however, would indicate that a change for the worse is nigh. A few common themes emerge. Many insurers are releasing redundant reserves to put their capital to good use. It is noteworthy, however, that there are certain points in the cycle where periods of low profitability coincide with insurers suddenly noticing redundant reserves.

Generally, with a few exceptions, P/C insurers weathered the financial crisis reasonably. There have been no major insolvencies or insurers in financial difficulty.

Rate declines across most lines point to a buyer's market. A Marsh analysis of commercial insurance rates showed further decreases in the third quarter of 2010. These are single digit declines but are all coming off years of rate declines. Moreover, the rate deterioration came despite $18 billion in insured catastrophe losses worldwide in the first two quarters of 2010. Granted, it would have to be a huge loss to affect the capital of the US P/C industry significantly.

One other noteworthy event is the move by the likes of ACE, Flagstone Re, AWAC and Amlin to Switzerland from Bermuda. The relocation started in 2008 with the surprising move of ACE, considered one of Bermuda's core companies. Others who plan to open Swiss operations are Endurance, Montpelier Re, and Arch. Some reasons offered for the move are Switzerland's well-established insurance and reinsurance market, its favorable regulatory environment, and its position as a point to expand into Europe.

Another issue of interest especially to the run-off industry is the recent court activity in Rhode Island on solvent run-off operations. A few months ago, a court granted GTE Re permission to convene a meeting of creditors to see whether the commutation plan has enough support. The plan, to be governed by a 2002 Rhode Island law, would allow structures similar to the solvent schemes of arrangement common in the United Kingdom.

Mr. Souter noted that schemes of arrangement generally have been very popular in the UK and are viewed as a very efficient way of running off business. While there are obstacles to the widespread growth of solvent run-offs in the US, this sector has potential to grow especially if other states see this as a way to raise revenues.

Mr. Souter felt that the overall market will be a difficult one for insurers. Without the prospect of rapid general economic expansion, and with the continued poor market conditions, insurers' attempts to expand their own business may result in some errors in judgment with its attendant consequences. ■

Education Session Summary – Rendez-vous 2010

Commutation Logistics: Challenges and Strategic Considerations for Run-Off Companies

Left to right: Mark Peters (Edwards Angell Palmer & Dodge LLP), Clifford Schoenberg (Mayer Brown LLP), Susan Grondine (R&Q)

Summary by Teresa Snider, Butler Rubin

Susan E. Grondine, Chief Claims Officer and General Counsel to R&Q USA, moderated a panel discussion with Clifford H. Schoenberg, a partner at Mayer Brown LLP, and Mark G. Peters, a partner at Edwards Angell Palmer & Dodge LLP. The panelists began their discussion with the premise that, in deciding on a commutation strategy it is important to understand with whom you are commuting and what your counterparty's motivations are. Is the company in run-off, an on-going live market, or in liquidation or scheme? Mark Peters noted that if the government is running the company, its motivations are different than a company in private hands. He also emphasized the importance of understanding whether your counterparty does a lot of commutations or is new to the commutation game. If the company does not routinely engage in commutations, you may need to provide additional guidance and information so that progress does not become stalled. You also need to be willing to lay enough cards on the table in order to develop trust with your counterparty.

Sue Grondine asked whether it is easier or more difficult to commute when one of the parties is in run-off. Cliff Schoenberg's view was that it depends on which company is in run-off and on the status of the other company. If the ceding company is in run-off, it may diminish the reinsurer's appetite to commute. An ongoing ceding company must consider business relationships and reputational issues and is thus more interested in keeping its policyholders happy than a ceding company in run-off, which is generally more willing to handle claims aggressively and to assert every legitimate defense to coverage. If a reinsurer is in run-off, it may be more interested in commuting. Indeed, it is often part of a run-off reinsurer's business plan to commute as many inward contracts as possible as quickly as possible. Even an ongoing reinsurer may have a strong desire to commute where, for example, it wants to exit a particular non-core business or wants to reduce the risk of adverse development on a volatile line of business. The ceding company, however, will not necessarily want to commute merely because a reinsurer wants to do so, even if the reinsurer is in run-off. The reinsurer's financial condition will be of paramount concern. If the reinsurer is in financial distress, the ceding company will have a strong incentive to enter into a commutation now rather than risk getting much less much later if the ceding company goes into liquidation.

> *If the company does not routinely engage in commutations, you may need to provide additional guidance and information so that progress does not become stalled.*

According to Mr. Schoenberg, the top nine reasons for a ceding company to commute are (1) concern about solvency risk - i.e., about the creditworthiness of the reinsurer; (2) desire to remove administrative and processing burdens; (3) business accommodation; (4) desire to retain the profits from favorably developing business; (5) desire to enhance cash flow; (6) the cedent is no longer subject to the surplus constraints that had motivated the purchase of reinsurance; (7) the largely cosmetic balance sheet impact, i.e., to increase net losses

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Lifetime Achievement Award: Bart Frazzitta

By Peter Scarpato, Conflict Resolved, LLC

Bart Frazzitta was presented with the prestigious Lifetime Achievement Award at the recent AIRROC / R&Q Commutations & Networking 2010 Event. As introduced by our Chair Jonathan Rosen, Bart has a reputation for achievement and integrity, having spent 46 years in every phase of the reinsurance industry, from regulator, to consultant, to current partner in the worldwide firm, Chiltington International, Inc.

In addition to his prodigious industry accomplishments, Bart, along with his wife Ginny, formed and currently runs The Esophageal Cancer Education Foundation (ECEF), following his diagnosis with and successful treatment of esophageal cancer. Through its website, **www.fightec.org**, and quarterly newsletter, the ECEF promotes the benefits of awareness and early detection of the disease. Congratulations Bart! ■

Bart Frazzitta and Jonathan Rosen (AIRROC Chairman, The Home)

AIRROC Person of the Year: Mindy Kipness

By Jonathan Rosen (AIRROC Chairman, The Home)

AIRROC's 2010 Person of the Year is Mindy Kipness, Senior Vice President of Finance for AIG's Chartis Insurance Company's Global Reinsurance Department. In an introduction by Jonathan Rosen, Chairman of the AIRROC Board, at this year's 6th Annual AIRROC Rendez-vous Event, her career accomplishments were highlighted. Mindy has worked fifteen years with AIG and Chartis combined, and nine years with Everest Re. Jonathan also shared with the attendees at the Opening Night Gala Dinner glowing comments from Eric Kobrick, Deputy General Counsel & Chief Reinsurance Legal Officer of AIG, about Mindy's richly deserved award.

Mindy's remarks epitomized her considerable experience and expertise in reinsurance coupled with her trademark humor. Stepping to the podium, she dramatically played the introduction to the Neil Sedaka song, "Breaking Up is Hard to Do," to illustrate her theme for run-off and reinsurance commutations. Mindy noted that "the divorce should always be civil," further illustrating her firmness in resolving matters with reinsurers in a gracious way.

Mindy has negotiated or participated in close to $1 billion of successful commutations during her AIG/Chartis career. She represents AIG/Chartis on four insolvent creditors committees and on the ROM Board of Directors. Her background is in accounting, reinsurance and finance. She describes her primary responsibility as oversight of the Global Reinsurance Finance team. The team handles commutations and reinsurance management reporting, which includes monitoring and reporting business metrics and relationships with all Chartis counterparties for senior management. She provides the accounting support to the AIG Legal Department and Chartis cedents' Reinsurance Accounting and Collections Departments as it relates to reinsurance recoverables, disputes and collection of collateral. She credits her co-workers for making her job both easier and more rewarding and considers her co-workers part of her extended family. But with a wry smile, Mindy also characterizes her role as "midwifery," delivering a stunning result even if the process may sometimes be long and painful.

Mindy reports that she learned many of her business and negotiating skills that she applies to the world of reinsurance collections by working as a child and teenager in her father's clothing store in New York City. There she developed her signature disciplined but congenial style through cash register savvy ("Everything balances!"), bookkeeping ("The numbers count!"), and sales ("You are now forewarned!").

In later years, Mindy worked side-by-side with the AIG and Chartis Global Reinsurance Department's senior reinsurance officers, honing her negotiating and insurance skills. A list too large to recount, she notes only that she is proud to have participated in many heated but always respectable negotiations which always ended with a "handshake and a smile!"

Mindy and her husband Stanley love traveling, seeking out blues music (perhaps where they sing "Breaking Up is Hard to Do"?) and antique stores. No doubt her engaging but savvy personality is particularly useful in her antiques search for whimsical treasures. Antique store owners around the world beware!

Knowing how to break up, being well-grounded in the financial, contractual and negotiating aspects of reinsurance recoveries, and being cynical, all wrapped in a gracious manner, describe Mindy Kipness, the well-deserved winner of this year's AIRROC Person of the Year. ■

Mindy Kipness (AIG) and Jonathan Rosen (AIRROC Chairman, The Home)

Rendez-vous 2010 Gala Dinner

1. *Seated from left:* Trish Getty (AIRROC), Jeffrey Burman (AIG), Andrew Maneval (Chesham Consulting), George Mitchell. *Standing from left:* Mike Zeller (Board Member/AIG), Stanley Kipness, Mindy Kipness (AIG), Jonathan Rosen (AIRROC Chairman/The Home), Kathy Barker (Board Member/Armour). **2.** *Seated from left*: Ed Gibney (CNA & AIRROC Secretary), Bill Littel (Allstate) Larry Schiffer (Dewey & LeBoeuf), Frank Kehrwald (Board Member/Swiss Re). *Standing from left:* Bryina Starks (CNA), Gary Stropoli (Chartis), Janet Mercer-Rose (Munich Re), Steve Koziol (Chartis). **3.** *Seated from left:* Keith Kaplan (Board Member/Reliance), Rose Ellen Gibson (Chartis), John Burke (Chartis), John Parker (Board Member/TIG/RiverStone). *Standing from left:* Karen Amos (Board Member/Resolute Mgmt.), Jeffrey McMurry (CLO), Marianne Petillo (Board Member/ROM). **4.** *Seated from left:* Mike Walker (KPMG) Alan Quilter (R&Q), Vicki Moore (KPMG). *Standing from left:* Charles Thresh (KPMG), Steve Petch (R&Q), Julie Ponsford (R&Q), Don Wustrow (Chiltington)

5. *Seated from left*: Bina Dagar (Ameya Consulting, LLC), Clive O'Connell (Barlow Lyde), Michele Watson (Inpoint Services), Art Coleman (Board Member, Event Chair/Citadel Re). *Standing from left:* Ken Wylie (Sidley Austin), Bart Frazzitta (Chiltington), Virginia Frazzitta, Eileen Bretherick (Citadel Re), Mike Fitzgerald (Board Member/Scan Re). **6.** *Seated from left:* Brenda Craven (Hartford), Melissa Cook (R&Q), Chris Hollender (ARGO Group), Sally Cassidy (FM Global). *Standing from left:* Kevin Apple (R&Q), Henry McGrier (Allstate), Thierry Verhaegen (ARGO Group), Bruce Friedman (Rubin, Fiorella), Jonathan Bank (Locke, Lord). **7.** *Seated from left:* Dave Kaston (Zurich), Ali Rifai (Board Member/Zurich), Rudy Dimmling (Zurich), Oliver Horbelt (2006 AIRROC Run-Off Person of the Year/Munich Re). *Standing from left:* Dominic Sharp (Zurich), Sheila Chapman (Zurich), Mike Baschwitz (Zurich), Colm Holmes (Zurich), Patrick Tiernan (Zurich) **8.** *Seated left to right:* Allan Hepworth (Ince & Co.), Peter Hastie (Insider Magazine), Steve Hennessy (Navae Syndicates). *Standing from left:* Bob Sirois (CNA), Jim Moran (R&Q), Leah Spivey (Munich Re), Chris Coelho (ACE), Simon Hawkins (PWC), (Navae Syndicates).

Women's Networking Luncheon: Success Stories

Top: Trish Getty, Ann Duffy (ISIS), Barbara Murray (Lumbermens). *Lower left:* Kathy Barker (Armour). *Lower right:* Bryina Starks (CNA), Andrea Viera (BMS Intermediaries), John Todd (BD Cooke), Teresa Snider (Butler Rubin), Janet Mercer-Rose (Munich Re), Leah Spivey (Munich Re), Elaine Collier (Omega General)

By Teresa Snider, Butler Rubin

The Women's Networking Luncheon was held on Tuesday of the conference and, as with last year's lunch, men were also welcome to, and did, attend. Following a delicious lunch, Trish Getty moderated a discussion on "Success." Joining her at the front of the room to share their views were panel members Barbara Murray and Ann Duffy. Barb Murray is the 2009 AIRROC Run-Off Person of the Year and Senior Vice President of Reinsurance at Lumbermen's Mutual. Ann Duffy a principal member of Isis Consulting Inc.

Barb Murray explained that success is an evolutionary process, and can be reached personally and professionally at any age and at all levels of employment. Ann Duffy agreed that success is a journey, but defines success as working with people whom you enjoy being with and reaching a balance in professional and home life. For Trish Getty, success is working with people for whom you care, being happy at work, and getting to know new people.

Trish Getty then turned the discussion to obstacles to and prerequisites for success. According to Barb Murray, sometimes the biggest obstacle to success can be oneself. It is essential to take control of your own destiny, rather than giving that power to others.

She listed a few of the factors that can lead to success: appreciating the value of education, being genuinely interested in what you are doing and having the ability to work with others. It is also important to be a risk taker and to be willing to make difficult decisions knowing that sometimes you'll make the wrong decision. Both panelists agreed that being passionate about your work is essential to success, although Ann Duffy cautioned that you need to work hard even during those times that

From left: Jeanne Kohler (Edwards Angell), Barbara Murray (Lumbermens), Trish Getty (AIRROC), Ann Duffy (ISIS)

you don't enjoy your work. She also advised that it is important to keep your contacts within the industry and build your network. Trish asked some of the audience

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Has "London Market Run-Off" Run Off?

By Mike Walker and Steve Goodlud, KPMG LLP (UK)

We were forced to consider this question on reviewing our findings from the latest KPMG Run-Off Survey: Non-Life Insurance 2010, published in October.

Apart from some notable exceptions, the trend in the size of the UK non-life run-off market has been downward for the last five years. Asbestos and environmental liabilities on older policies are being extinguished through settlement or commutation. Claims arising from recently discontinued business appear to affect only certain pockets of the market and have a shorter lifespan thanks to changes in policy wordings. And since the Katrina, Rita and Wilma hurricane season in 2005, the insurance sector seems to have withstood natural catastrophe losses just as well as it has coped with the recent financial crisis.

But is the story as simple as that?

UK Run-Off Market

The graph on the following page depicts the size of the UK non-life run-off market over the last five years, measured by total liabilities. The size of the market at the end of 2009 was £29.7 billion (US$47.3 billion). As can be seen, total liabilities have shrunk steadily since 2005 apart from one exceptional year when liabilities jumped as a result of the recent financial crisis and its impact on exchange rates and specialist monoline insurers.

> *Apart from some notable exceptions, the trend in the size of the UK non-life run-off market has been downward for the last five years.*

Why is it shrinking? Of course run-off does eventually run off. The strategy of many run-off companies in the London market is one of acceleration towards finality, whereupon trapped capital can be accessed. This is a key reason for the reduction in size of the market; where like-minded parties willingly enter into settlements and commutations. This strategy has also been instrumental in collapsing the London market excess of loss spirals, which had multiplied losses throughout the market. Such activity also minimises legal costs which would otherwise be incurred through protracted litigation.

Not all companies, however, follow this approach. We now appear to be at a point where large swathes of legacy business are under the control of run-off consolidators which prefer the long game. A clear example of this different run-off strategy is Equitas. For the first ten years after its formation, Equitas focused on large-scale settlement activity which reduced its total liabilities by two thirds. In 2007, its business came under Berkshire Hathaway's control. The approach appears to have changed since the handover as reported undiscounted liabilities of Equitas have remained at about £5 billion (US$7.5 billion).

The UK sterling to US dollar exchange rate also has a significant influence of the size of the market when it is expressed in UK sterling. Notwithstanding the settlement and commutation activity described above, a large proportion of traditional London market run-off liabilities remain long-tail US asbestos and environmental claims. If the effect of exchange rate movements is removed, then the general trend in size of the market is consistently down.

The demise of the monoline insurers was a recent, exceptional phenomenon. The collapse of their businesses alone increased the size of the UK run-off market by over £7 billion in 2008. Combined with an exchange rate of approximately £1 to US$1.45, the 2008 year end saw a spike in the market. One year on, a weakening US dollar and significant restructuring by monoline insurers re-established the downward trend.

Run-Off Activity in the UK

The UK has been a very active marketplace for the acquisition of discontinued business by run-off consolidators. Indeed, it became a seller's market for a number of years as competition amongst acquirers drove up prices. Circumstances have, however, changed over the last few years. The financial crisis made an impact as finance for deals (on acceptable terms) became harder to find. The supply of run-off portfolios coming to the market has also been reduced: there are fewer opportunities left to pursue at the moment.

With respect to acquisition opportunities, the situation may change in the lead up to Solvency II, a European Directive due to be implemented across the European Union at the end of 2012. Under Solvency II, European insurance groups are expecting an increase in regulatory capital and solvency costs of maintaining run-off business

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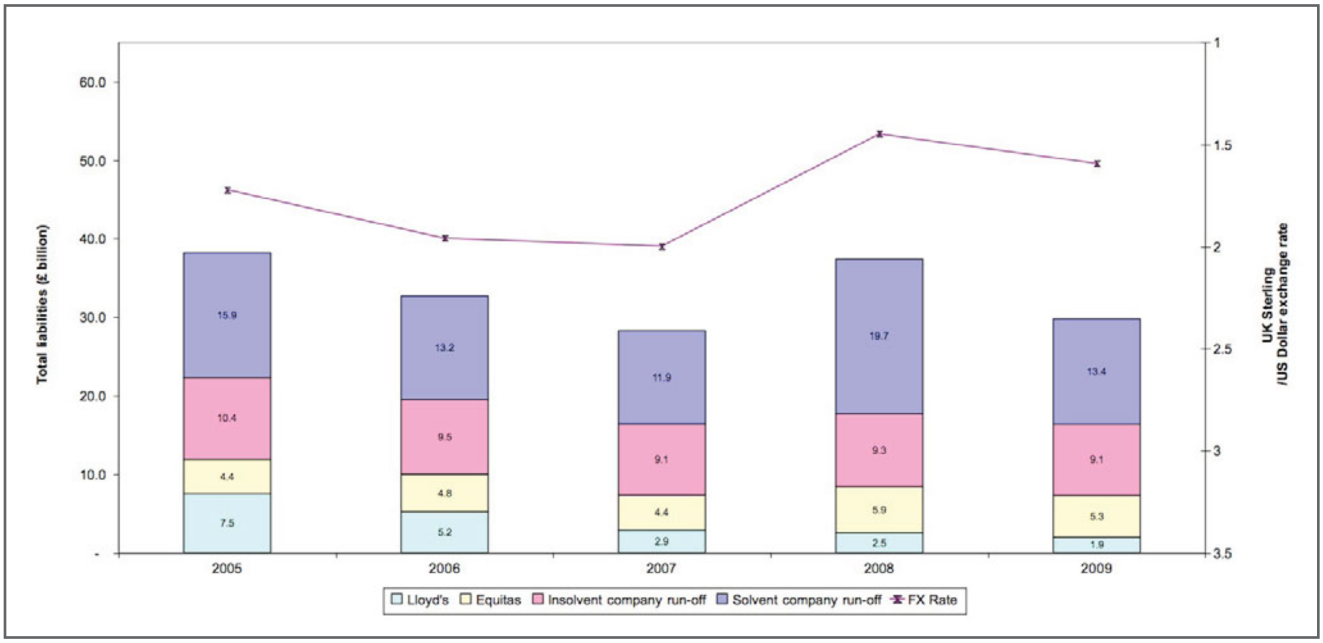

Source: A.M. Best - Best's Statement File - UK, KPMG LLP (UK) 2010, Lloyd's

under that regime. It is anticipated that there will be a flurry of activity as groups reorganise their structures to maximise capital efficiency, leading to the combining of different books of business to take advantage of diversification benefits or to the discontinuance and/or disposal of unwanted portfolios. Some companies in run-off may want to avoid Solvency II altogether and could look to sell out beforehand.

The UK has been a very active marketplace for the acquisition of discontinued business by run-off consolidators.

Demand is still high from investors in run-off, in the company market and at Lloyd's, and Solvency II may bring a number of new opportunities for acquirers. All of the deals done in the UK over the last two years have been with the most active run-off consolidators, both in respect of insurance company acquisitions and run-off service providers. There is no great surprise here. Run-off service providers in particular are going through a difficult period: as the run-off market shrinks demand for outsourced back office administration services is drying up. Such organisations are having to diversify their services and look at opportunities in the live market.

Future Prospects For UK Run-Off

The UK run-off market is far from dead. For as long as insurance is written, there will be a run-off sector. The losses which comprise it will be divided into two categories: old and new.

Old claims relate to long-tail latent clams written under loss occurring policies. In the UK these will include UK asbestos claims written under compulsory employers' liability policies which cannot ordinarily be accelerated. The future UK mesothelioma cost to insurers is estimated at £10 billion and mesothelioma deaths are not expected to peak until 2016 at approximately 2,000 per annum, about ten years after the US peak. The majority of UK mesothelioma claims are, and will be, against insurers still writing business and so they fall outside our statistics for the size of the run-off market. They are generally managed in-house.

New claims relate to losses arising from current policies. In general, and absent significant disputes, these will tend to have a shorter lifespan as policy wordings have various exclusion provisions for long-tail claims and they limit the time within which claims can be brought.

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Traditional London market run-off falls within the old category and this is coming to an end for those who have sought it: those left seem to be in for the long term, provided run-off costs are covered by investment returns. This is a critical issue which still confronts the insurance sector as a whole due to the current economic environment. With interest rates remaining very low and therefore investment yields depressed, a major challenge

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Commutation Logistics: Challenges and Strategic Considerations for Run-Off Companies

Continued from Page 15

or net premium; (8) resolution of a dispute; and (9) elimination of regulatory penalties on long-outstanding recoverables. On the flip-side, reinsurers commute (1) to exit a line of business or better position the company for a merger or sale; (2) to reduce the risk of adverse loss development; (3) to enhance policyholders' surplus to the extent the commutation payment is less than posted reserves; (4) to avoid increases in loss reserves which it is known will soon be reported; (5) to reduce RBC requirements; (6) to reduce claims administration and processing burdens; (7) as a business accommodation; (8) to resolve a dispute; and (9) because of concerns about a cedent's solvency and the desire to avoid dealing with the liquidator.

Ms. Grondine also asked whether the state of the economy posed any obstacles to commutations. Mark Peters noted that the credit crunch may reduce interest in commutations, particularly where the cedent is limited in its investment options. For example, the New York Liquidation Bureau can only invest in certain places and

Mark Peters (Edwards Angell), Susan Grondine (R&Q), Clifford Schoenberg (Mayer Brown)

have may no incentive in the current financial market to commute to raise cash to invest. Understanding your counterparty's motivations will enable you to understand whether commutation is possible at all, and, if so, what strategies you should employ to make sure the deal gets done. ■

Has "London Market Run-Off" Run Off?

Continued from Page 23

exists for insurers to maintain profitability. Run-off companies in particular are under great stress, with no new premium income to rely on. A disciplined approach to cash flow management through claims handling and the collection of reinsurance is fundamental for survival during these difficult times. Not all of them may see it through unscathed.

Whilst the insurance market has emerged relatively unharmed from the recession, and has fortuitously avoided paradigm-shifting losses from recent major catastrophes, insurance companies still face a number of difficult challenges; for example, cycle management whilst pricing is soft, investment performance in a low interest rate environment, and the time and cost associated with the burden of compliance in a changing regulatory framework. It seems inevitable that these challenges, and the continuing macro-economic uncertainty, will impact upon the size and characteristics of the UK non-life run-off market in the future. ■

Women's Luncheon

Continued from Page 21

members to talk about attributes that lead to success. Vivian Tyrell remarked that good relationships and teamwork are essential, while Kathy Barker pointed to having good problem-solving skills.

> *…concern was expressed by several people that the generation now entering the workforce has unrealistic expectations as to salary and the speed at which they will achieve success.*

The discussion then turned to whether today's youths are developing the personal communication skills important for later success. Although the pessimistic view is that there will be a generation only be able to communicate with a cell phone in their hands, or by their ears, optimists in the group thought that children are able to navigate between social groups in ways the generations ahead of them have been unable to do. However, concern was expressed by several people that the generation now entering the workforce has unrealistic expectations as to salary and the speed at which they will achieve success.

After the luncheon, Barb Murray summed up with a pithy quote about success: "Don't get hung up on how you get there, just be glad that you arrived." ■

Making it Happen!

Chairs of Event Education Sessions

Kathy Barker (Armour), Jonathan Bank (Locke Lord), Carolyn Fahey (HB Litigation Conferences)

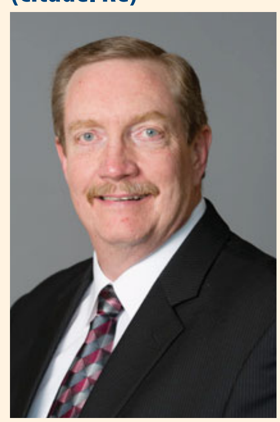
Education & Event Committees

Kathy Barker (Armour), Art Coleman (Citadel Re), Karen Amos (Resolute Mgmt.), Ed Gibney (CNA)

AIRROC Publications Committee

Standing left to right: Peter Scarpato (Conflict Resolved, LLC), Jonathan Bank (Locke Lord Bissell & Liddell LLP), James Veach, (Mound Cotton Wollan & Greengrass), Nick Pearson (Edwards Angell Palmer & Dodge LLP), Vivien Tyrell (Reynolds Porter Chamberlain LLP), Michael Walsh (Boundas, Skarzynski, Walsh & Black, LLC), Colm Holmes (Zurich). *Sitting left to right:* Nicole Myers (Myers Creative Services), Leah Spivey (Munich Re), Bina Dagar (Ameya Consulting, LLC), Trish Getty (AIRROC), Maryann Taylor (Boundas, Skarzynski, Walsh & Black, LLC), Teresa Snider, (Butler Rubin Saltarelli & Boyd LLP) Ali Rifai (Zurich). *Not pictured:* Nigel Curtis, Francine Semaya, Nick Williams (Clifford Chance), William Maher (Wollmuth, Maher & Deutsch LLP), Gina Pirozzi (G. Pirozzi Consulting), Lawrence Zelle (Zelle Hofmann), Joseph Monahan (Saul Ewing LLP) and Frederick Pomerantz (Wilson Elser).

Event Chair: Art Coleman (Citadel Re)



Our hat is off to you, Mr. Event Chair! We have achieved another tremendously successful event.

List of Sponsors:

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Message from CEO and Executive Director

Continued from Page 1

hands before she was announced as the 2010 AIRROC Run-Off Person of the Year. The honor was quite special to her and certainly well-deserved. Her colleagues and our AIRROC membership expressed their congratulations to Mindy throughout the event. Congratulations, Mindy!

We thank the Education Co-Chairs of the event, Kathy Barker of Armour Risk Mgmt. and Jonathan Bank of Locke Lord Bissell & Liddell, the speakers and facilitators for a tremendous interactive workshop, and especially Bill O'Farrell of ACE for writing the "Survivor" program.

Due to work demands, Ali Rifai of Zurich has stepped down from the position of Publications Committee Chair, while maintaining his seat on the AIRROC Board of Directors. The board has appointed Co-Chairs Leah Spivey of Munich Re and Colm Holmes of Zurich to replace Ali. We thank Ali for his six years of dedicated service.

Meanwhile, Janet Kloenhamer has stepped down from the AIRROC board to pursue another career unrelated to insurance. We also thank Janet for her four years of dedication and contribution as Co-Chair of the Legislative/Amicus Committee.

This was election year for the AIRROC Board of Directors. The board expanded the number of board seats from thirteen to fifteen. New members of the board are Leah Spivey (Munich Re), Colm Holmes (Zurich), Glenn Frankel (First State/Hartford) and Ed Gibney (CNA). Replacing Ed Gibney as AIRROC Secretary is Bill Littel of Allstate. Congratulations to all.

It was fabulous to again see so many familiar faces and to meet new attendees. You may have noticed that the AIRROC branding represents the winds of change and that I defined "success" during the AIRROC Women's Luncheon as loving what you do. Count me successful because I love working for AIRROC, particularly because of the many special people I have come to know over the past six years. ■

Welcome and Opening Remarks

Larry Schiffer (Dewey & LeBoeuf LLP)

Synopsis of Captive Insurance Companies

Summary by Nasri Barakat, International Consulting

The presentation regarding the Captive Insurance Companies in Run-Off was given at the AIRROC meeting by Mr. Glenn Weber, Managing Director & Risk Finance Practice Leader at AON Global Risk Consultants, and Bruce Wright, Esq., Partner at Dewey & LeBoeuf LLP.

Each of the presenters focused on several aspects of the captive and its winding down. Mr. Wright opened by giving a definition of a captive and the various types of business it insured. He briefly discussed the "single parent captive" with unrelated business, affiliated group, pool and their variations. He then discussed the formation of the stock/direct, and Stock Fronted holding company relationships in a captive arrangement. In addition, he discussed the formation of Risk Purchasing Groups, mutual direct and mutual fronted captives. He also gave a brief overview of the reciprocal captives arrangements. Because of the large number of captive arrangements, the presentation was brief yet still included a description of the agency captive including single-producer captive, multi-producer captive, and "cell company captive." Bruce also touched on the late formation of captives set up between banks and mortgage companies before the sub-prime mortgage disaster when banks intended to capitalize on the profitability of mortgage insurance by creating a captive of their own to insure bulk mortgages heretofore written by mortgage insurers. Hospitals also formed captives for the purpose of providing insurance for their staff physicians E&O coverage and so did other groups including attorneys, accountants and other professionals who were simply unable to find available coverage in the open market. Others just formed captives in order to capitalize on opportunities in the retail area such as captives to write customer warranty programs including appliances. Others include trade associations such as the ones earlier mentioned.

Each of the presenters focused on several aspects of the captive and its winding down.

The normal scenario inevitably includes direct insurance with the named or additional insured and a reinsurance arrangement. A fronting company writing the direct insurance is a necessary ingredient since the captive is not licensed to write direct insurance. The insured's coverage through the captive is fronted by a licensed company and the captive excess coverage is reinsured with reinsurance. The captive's lack of licensing requires a collateralization of the risk which is commensurate with the exposures.

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Kathy Barker (Armour)

Bruce Wright (Dewey & LeBoeuf LLP)

Glenn Weber (AON Global Risk Consultants)

The normal scenario inevitably includes direct insurance with the named or additional insured and a reinsurance arrangement.

The captive as a unique arrangement is often supported by collateral and, with the possibility of the pyramiding of letters of credit, can and often does become a drain on the capital resources of the parent. The liabilities of the captives are often the liabilities of the parent. This is certainly true when workers as well as vendors and customers may become claimants. The incentive to form captives used to be the potential for tax benefits. However, for some companies captives may be less central to their business. Since the boom in captive formation in the 70's and 80's, regulatory reforms have created other efficient forms of risk retention. In addition, the deindustrialization of the U.S. has changed the nature of the risk. Litigation reforms and a pro-business judiciary lead to quicker and smaller payout of claims diminishing the benefit for captives where holding the reserves and investing the amounts was crucial to the profitable operation of a captive.

"The captive as a unique arrangement is often supported by collateral and, with the possibility of the pyramiding of letters of credit, can and often does become a drain on the capital resources of the parent."

The current reality is that many companies, through mergers and acquisitions, find themselves with one or more captive they may or may not be equipped to handle. All this led to the need to unwind captives and run off the liabilities. The former tax benefits are no longer incentives. Companies can achieve some of the same or similar benefits with large deductible programs as well as large retentions. These are the reasons for captives to try to commute their liabilities and liquidate the company.

The program was interesting and beneficial. The question and answer portion was also very informative. ■

Art Coleman (Citadel Re)

James Veach (Mound Cotton Wollan & Greengrass)

Plea for More AIRROC Legislative Action

Summary by Michele Watson, Inpoint

The discussion of SSAP 62 as a useful tool in the run-off toolkit, to be presented by Swiss Re's Jason Richards and David Scasbrook at the July 15th membership meeting, was rescheduled for a future membership meeting. AIRROC Publications Committee member and AIRROC booster James Veach stepped in to encourage AIRROC to raise its voice in legislative initiatives that may affect run-off.

Mr. Veach described the reaction of state regulators to the passage of the Patient Protection and Affordable Care Act of 2009 ("Health Care Act") one week before the Spring Meeting of the National Association of Insurance Commissioners in Denver, Colorado. Specifically, Mr. Veach recounted the Commissioners' efforts to address the Health Care Act as it worked its way to the President's desk and the steps that state regulators have taken since the Health Care Act passed.

Mr. Veach then recounted the NAIC's anticipated passage of the financial reform legislation. This same legislation passed the Senate (60 to 39) on the afternoon of the AIRROC meeting. Mr. Veach's thesis was that the 2,100 page Health Care Act and the 2,600 page Dodd-Frank Act threaten to shift the fulcrum of insurance regulation. Together they represent a greater threat to state insurance regulation than what surfaced in the late 1980s during the Dingell hearings.

Mr. Veach's thesis was that the 2,100 page Health Care Act and the 2,600 page Dodd-Frank Act threaten to shift the fulcrum of insurance regulation.

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Mr. Veach urged the members to consider expanding AIRROC's role with respect to legislation that affects run-off. Pointing to a recent NAIC White Paper on Restructuring Mechanisms, he proposed that AIRROC encourage the enactment of legislation that would allow insurers with assumed reinsurance business to prepare Regulation 141 Plans that would allow a troubled insurer/reinsurer to commute itself away from insolvency and complete its run-off.

Finally, Mr. Veach noted that the AIRROC Matters publication plans to include items setting out regulatory initiatives, statutes, circular letters that impact the business of run-off. He encouraged AIRROC to become a spokesperson for run-off community and speak out (and up) on matters of common interest to the run-off community. ■

Run-Off in Europe

By Thomas Willkowei and Thomas Freudenstein,
Global Re

Until 2002, the then Gerling-Konzern Globale Rückversicherungs-AG (today GLOBALE Rückversicherungs-AG) with some 1,200 staff around the globe, ranked number six in international reinsurers. Local branch establishments and subsidiaries on every continent represented the reinsurance company of the Gerling Group in all major markets. The range of products included nearly all classes of Life and Non-Life reinsurance.

In 1998, the company acquired Constitution Re in order to strengthen its position among the top players. There were four factors which then triggered the decision to run off the non-life business of the GLOBAL Re group. First, the terrorist attacks on September 11, 2001 resulted in a loss of more than $600 million USD. Second, the decline of capital markets led to depreciations in excess of €1 billion EUR. In addition, the American companies were repeatedly confronted with loss burdens of an unexpected size from asbestos-related and environmental damage claims. Finally, Constitution Re did not meet the expected profit targets.

As a result, the company was in need of capital. The search for a financially strong partner or buyer remained without success.

All this prompted the decision in October 2002 to discontinue writing new non-life reinsurance business and commence a run-off of existing portfolios. With gross loss reserves on 31st December 2001 at around € 9.5 billion, this meant launching one of the by then biggest run-offs ever.

GLOBAL Re in Run-Off – or – Life Goes On ...

After the decision to go into run-off we were able to quickly adapt GLOBAL Re, under a new owner, to the new situation by restructuring the entire company. Our primary goal has been – and continues to be – to perform the solvent run-off of all obligations towards our clients with due consideration of all requirements of the responsible regulators while not jeopardizing our own liquidity at any time. This is the only way to meet all justified claims of our ceding companies all the way to the end of the run-off.

We determined early on that it would take targeted action to reach finality. Minimising risks, commuting exposed risks and repatriating excess capital early on were the steps that brought increasing stability to our portfolios.

The primary goal of a run-off is the termination of all business relations (under conditions as favourable as possible). This can be achieved by two different approaches. Passive management will continue to handle any losses incurred until the natural expiration of the last contract. We determined early on that it would take targeted action to reach finality. Minimising risks, commuting exposed risks and repatriating excess capital early on were the steps that brought increasing stability to our portfolios. We were able to achieve this by benefiting from the different run-off experiences and specialised knowledge of the various markets (particularly in the USA and Great Britain) we gained via our worldwide network.

Meanwhile, eight years have passed and looking back we may pride ourselves of our successful action. Since the start of the run-off we commuted gross loss reserves to the tune of € 5.2 billion through more than 1,100 commutation transactions, reducing the loss reserve total of our group from € 9.5 billion 2001 to below € 1.6 billion at 31st December 2008.

The European Run-Off Market as Seen by the German Market Leader GLOBAL Re

The run-off market is more extensive than many expect. While fully accurate figures are not available,

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Tom Freudenstein (Global Re)

there are a number of studies that allow for an approximation. A study conducted by PWC comes up with a total of €205 billion of loss reserves being run off in all of Europe, some 81 billion of which in Germany and Switzerland alone. Another study by KPMG shows a figure of €45.4 billion for the German-speaking part of Europe. It is a surprise, therefore, that in spite of this conspicuous run-off volume, the number of market players specialized in run-off remains very small.

However, the particular character of the European run-off market also raises a number of questions which we want to deal with now. First and foremost, there is no single European run-off market. We should therefore use the plural "markets" when we speak about run-off in Europe.

To begin with, it should be pointed out that there is no such thing in Europe as THE insurance location. Insurers' headquarters are rather spread across the entire continent. Nevertheless, there are some cities with a stronger presence of insurance and reinsurance companies, the more prominent ones being Cologne, Munich, Paris, Milan, Madrid Zürich and, of course, London. There are also various local insurers very deeply rooted in their respective regions. This wide geographic spread of company headquarters inhibits the continuous presence, short ways and frequent contacts for exchanging information and swapping rumours as is typical of the London market.

The publication of companies in distress and disclosure of loss reserve volumes in their annual reports still allow a very reliable indication of the overall volume of the London run-off market.

The European markets are comprised of larger-size companies while the London market has its multitude of small Lloyds syndicates and small specialist carriers. Liability risks were written in large number, and with extensive reinsurance of asbestos and environmental risks. A good example of how long a run-off takes in the German market is presented by Hamburger Internationale Rückversicherung Aktiengesellschaft. This company had already been in run-off when it was taken over by Chiltington in 1990. To this very date, there are reinsurance contracts that still have to be managed. In Great Britain, a run-off market emerged earlier as many market players, especially smaller syndicates and monoliners, had a weak capital base. In the 80s and 90s, this resulted in a multitude of insolvencies, entailing the run-off of their entire portfolios. The publication of companies in distress and disclosure of loss reserve volumes in their annual reports still allows for a very reliable indication of the overall volume of the London run-off market. In Europe, on the other hand, companies are larger and their business is more diversified which has so far prevented the occurrence of such dramatic run-offs of entire companies due to their insolvency. Most of the portfolios in run-off only make up a small part of the corresponding company's total loss reserves and are quantifiable neither in annual reports nor in the statistics of insurance associations or other information accessible to the public. In the light of this situation, the results of the mentioned studies are all the more surprising.

While the solvent run-off of GLOBAL Re and Gothaer Rück in Germany has reset the focus on a run-off as an independent business model, this does not change the lack of transparency of the run-off market which we believe to be due to the particular infrastructure of the European insurance markets.

During the last eight years of run-off management, we have observed a number of similarities within the European countries, but there also are a number of distinct differences.

Similarities

Many companies have had negative experiences with the London market. There are a number of reasons for this, and it is easy (and common) to blame London for everything that went wrong. The fact is that there is still a degree of distrust with regard to anything that comes from London.

Traditionally, there has not been a separate run-off industry in the European insurance markets. Very often portfolios in run-off contain old burdens from major losses (e.g. asbestos) or ill-fated risks written internationally. The servicing of active and run-off policies is done by the same department in many companies. Others prefer to leave this work to the claims department or the outward reinsurance manager. For economic reasons, the divestment of the run-off segment as a department devoting its entire attention to this business is only opportune for a larger reserve volume. It is therefore found with the major insurers and reinsurers, such as Axa, Swiss Re,

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Hanover Re, Munich Re, etc. This also means that there is only very little outsourcing of run-off business.

Traditionally, there has not been a separate run-off industry in the European insurance markets.

The concept of run-off does not receive much publicity in Europe. So far, the leading personalities in the markets prefer not to be openly associated with this topic. However, with the Commutation Rendez-Vous in Germany, and a lot of other run-off meetings/events in Europe, this is changing rapidly; the German chapter of ARIAS, for example, included a discussion about Solvent Schemes of Arrangement, a typical run-off topic, in its 2009 member conference. But the run-off market continues to be viewed as a highly sensitive area. Disclosure and voluntary communication of problem areas is avoided. In the minds of many managers the term run-off is still associated with failure, problems and unpopular measures.

Finally, the experts in many countries expect to see an increase in run-off activities following the implementation of Solvency II.

Differences

Language is a core problem for an American company entering into commutation negotiations in Europe. There may be reluctance or even inability to negotiate in English. This can be an obstacle to effective communication. One side might perceive an item to be agreed, while the other side believes that it has only set the stage for further negotiation. It always helps to engage a negotiator who is fluent in both languages.

Besides the different languages, we have noted a number of cultural differences when it comes to the preparation and negotiation of commutations.

In Germany, Switzerland and the Nordic Countries, a very technical approach is the norm. Once a commutation initiative is on its way, a lot of time will be spent on preparing and reconciling the numbers. The negotiation itself should be professional and straight forward, with both sides trying to reach a common ground to achieve finality.

It is our experience that it is very hard to start a commutation initiative in France. Without a personal relationship, it is almost impossible to get access to the decision maker. Once this hurdle is overcome, a very professional negotiation should be expected. Since loss reserves are secured by deposits in France, there usually is little room for credit risk discounts.

Language is a core problem for an American company entering into commutation negotiations in Europe.

In Italy and Spain, the negotiation approach is more emotional than in other European countries. In the USA, the parties may have a dinner after the deal has been signed. Here, a number of dinners may be required just to start the negotiation. There is a high acceptance of commutations if the reinsurer is financially impaired; there is little to no interest if the financial condition is stable. We have observed different approaches when it comes to organizing a run-off infrastructure. In southern Europe, insurance companies usually do not have an individual or department that specifically deals with run-off. This means that often there is only limited knowledge with regard to run-off tools.

Finally, the use of the term run-off appears to embrace quite different time frames. In Germany, for example, run-off includes the objective to achieve finality as quickly as possible. This sometimes seems to be different in other markets, especially where an excess of providers offering their services leads to a tendency to stretch the handling of orders deliberately.

Conclusion

There is run-off in Europe and it is possible to achieve finality, but you cannot view Europe as a single market. You have to implement different strategies to approach the individual markets and you need to be aware of the cultural differences. We recommend a local specialist who speaks the language and who has sufficient market experience to support the commutation initiatives.■

Challenges Facing Run-Off Companies in the Current Operating Environment

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run-off to expiry strategy. One of the key concerns is how the FSA and US Legislators will deal with Solvency II. The Solvency II capital requirements are problematic because while you must be Solvency II compliant, not many people know what that means.

The panel also discussed the declining market from the viewpoint of service providers and whether the service sector has the ability to survive. One of the primary reasons for the problem cited by the panel was the lack of new insolvencies which has created a problem for deployment of service providers. Independent Insurance Company was one of the last large insolvencies. It went into liquidation in 2001 and the many insolvencies of the 1990's are winding up. The consensus of the panel was that there is a tremendous amount of talent in the run-off market and how you deploy that talent and make money in a declining market is a significant challenge.

The slow down in the reinsurance dispute market was the next topic addressed by the panel. Mr. Schwartz made the point that part of the reason for this situation is that many of the contentious issues have been resolved, such as how to handle asbestos and environmental losses, by the courts. In addition, there has been a lot of consolidation in the industry, both live and run-off, which cuts down on the number of players. Fewer players translates to more internal ways to resolve reinsurance disputes. Mr. Parker said that the slowdown is not only a function of the economy but also a maturing of the books of business. The panel acknowledged that they are not able to identify any new issues on the horizon that will have the same traction for controversy as the asbestos and environmental losses. In their experience, Chinese drywall or the finite risk disputes, for example, have not really generated the insurmountable differences that applied to some of the larger issues faced by the community over the last couple of decades.

In closing, the panel concluded that the trend in the UK and elsewhere is an attempt by companies to get their arms around their run-off business, rather than surgically remove it and sell it as was the tendency in the past.■

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