

CONSIDERATIONS IN EVALUATING REINSURANCE SECURITY

In world markets, very great sums are expended on the purchase of reinsurance protections which, like many general insurance contracts, promise the reimbursement of certain future payments if they are incurred. The ceding company obviously needs to have some confidence that the reinsurer will be in a position to meet this obligation, or the cedant would be advised to retain the business for his own account - at least he would then be in the position of having some additional premium to assist in meeting the additional retained liability. Otherwise, in the event of the failure of the reinsurer, the liability will revert to the cedant although the reinsurance premium has already been paid away.

As a consequence of such thoughts, quite an industry has developed in monitoring reinsurance security, which has recently been a very 'hot' topic, given the vast number of reinsurers participating in the market, often at cut-throat rates.

What factors should be considered in evaluating the relative security offered by different reinsurers?

The following are relevant items, but even this substantial list is probably not exhaustive -

1. Availability of information and data.
2. Country of origin - degree of supervision and political, economic and currency considerations.
3. Ownership - legal status of a subsidiary as an independent body
  - status of parent, if any, in terms of ability and willingness to assist in case of financial difficulties
  - existence of any guarantees.
4. Past performance - stability and profitability
  - whether this is a guide to the future
  - the problems of new companies
5. Adequacy of reserves - problems of data availability and analysis
6. Appropriateness of assets - liquidity and volatility of capital values.
7. Reinsurance protections - extent and security
  - problems of information availability
8. Management - integrity and competence.
9. Nature of the business being ceded - length of tail, maximum loss potential and problems of accumulation.
10. Trade-off of price v security - ultimately a commercial decision