

REINSURANCEFOCUS

reinsurance-related and arbitration developments

TREATY TIPS

CREATIVITY IN REINSURANCE AGREEMENTS

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The past year has seen considerable development and expansion of the catastrophe bond market, which has: (1) significantly expanded the capacity of the risk transfer market generally (i.e., traditional reinsurance, cat bonds, and other alternative risk transfer mechanisms); and (2) added many new sources of capital to the market, such as pension funds. Cat bonds are essentially 100% collateralized reinsurance agreements funded by investors which may, or may not, be insurance companies. Price competition between cat bonds and traditional reinsurance has resulted in declining rates in both markets, there has been innovation in the terms of the reinsurance coverage in cat bonds, and ceding insurers may find it beneficial to seek to include some of these innovations in their traditional reinsurance agreements.

Among the contract provisions which ceding reinsurers may wish to consider, all of which have precedents in the cat bond market, and which may require a premium adjustment:

- Multiyear contract term to lock in unusually low rates on line;
- Adjustable annual attachment point resets to avoid gaps in a reinsurance tower and provide for the drop down of layers to fill in for exhausted layers;
- Ability to add related ceding insurers or related risks to the contract after the initial year of cover;
- Reinsurance of a greater diversity of types of risks than has been traditional in a single reinsurance contract; and
- Early termination alternatives to increase financial management options.



Other provisions may not require any premium adjustment, for example:

- Streamlined or two-tiered arbitration provisions depending on the amount at stake or other business factors; and
- Availability of injunctive relief in certain circumstances.

Additional creativity may be possible to meet the needs of a ceding insurer's particular financial plan or financial or operational needs. Due to the current soft market, now is a good time to seek to innovate.



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