Biotechnology Company Adopts Captive-Centric Strategy

Challenge

In 2018 a biotechnology company ("Biotech") faced a complexity of risks, rapid corporate growth, and expansion into new therapy areas. Armed with an establish captive insurance organization, the leadership of Biotech set about developing an effective insurance strategy that would reflect their current and future needs.

Solution

The first stage was achieved over a period of two years – integrating key insurance programmes into multi-year, multi-line contracts with key insurance partners. The second stage was to consider how Biotech could leverage its risk appetite more effectively via its captive. A project team including experts within the insurance carrier industry and consultants in captive strategies was established in early 2020 to evaluate the economic and other benefits that Biotech could achieve through greater captive deployment and use of portfolio reinsurance. The specific goals agreed to were:

- Reduce the overall cost of risk and improve
- budgetary stability.
- Place Biotech's captive at the heart of their strategy.
- Align retention levels with corporate risk appetite.
- Manage risk volatility to within acceptable levels.

The project team began with designing an achievable 'target' risk financing program, with optimal retentions and limits for each key type of insurable risk, including non-damage business interruption resulting from manufacturing issues. This is a key risk in the life science industry. Stochastic modelling of the underlying risks to create independent loss distributions and collectively across all risk types helped to understand the economic benefits of taking higher retentions and increasing captive participation across a wide range of programs.

The team developed a strong understanding of the key features and benefits of structured reinsurance, selecting a potential partner to work with, and negotiating a multi-year, multi-line reinsurance program to manage the volatility of an unexpected frequency of mid-sized losses impacting the captive. They also remodeled the negotiated reinsurance program to ensure that the expected target savings would be achieved, and that the probability of undesirable loss outcomes would be within agreed tolerance levels. The overall strategy and target program were approved by senior management in early 2022 and implementation was successfully completed on time.

At this point a reinsurance partner was selected and a five-year structured reinsurance contract negotiated. The new reinsurance program enabled Biotech's captive to participate for the first time in several new programs as well as significantly increasing retentions on those programs it already participated in. In all, the reinsurance structure provided per event and, in some cases, annual aggregate protection across 12 separate insurance programs.

All the key objectives were achieved, with material premium savings realized whilst being able to demonstrate that volatility was being managed to within agreed risk tolerance levels. Against a backdrop of increasingly tough market conditions, captive participations stepped in to fill the gap. As traditional insurance markets restricted coverage flexibility to modify existing programs without negatively impacting local business units was provided.

About SRS

SRS is the world's largest independent insurance company manager. With over 25 years' experience, SRS provides management and consulting services to a wide range of insurance company entities, from single parent captives to complex commercial insurers and reinsurers. SRS has operations in the North America, South America, Europe, Caribbean, and South Africa.

There were several challenges that needed to be overcome in getting to the finish line. Pharmaceutical companies always present a big underwriting challenge to insurers, particularly in respect of Products Liability, Non-Damage Business Interruption, Cyber, and Directors & Officers Liability. To combine these risk classes with more traditional lines (such as property damage and business interruption, stock throughput, public liability and various financial lines), and to lock the coverage and key economic terms into a five-year non-cancellable contract, presented the team with a pretty unique 'ask'.

There were also challenges to unwind some of the existing long-term arrangements, replace fronting carriers where necessary, preserve market relationships and capacity, and to ensure all captive stakeholders were comfortable with the arrangements given the relatively small size and immaturity of the captive.

The experience of the teams enabled the project to be driven home within target parameters despite a rapidly changing backcloth in terms of market appetite to risk and the additional challenges of working remotely.

Results

So, one year on, what has been achieved? Biotech has always been a very well risk managed company, despite the challenges that rapid expansion always brings, and its loss record across all classes of insurance is testimony to that. The significant element of risk-sharing, characterized through a significant profit commission payable for low losses, is a key feature of structured reinsurance. Given how rapidly and substantially the market hardened across all lines of insurance since 2020, not only was the timing of the project pretty much perfect but the anticipated savings have now been magnified. Furthermore, preservation of coverage and budgetary stability – two of the key original goals – have been shown to be even greater achievements than the team might have anticipated back in 2020.