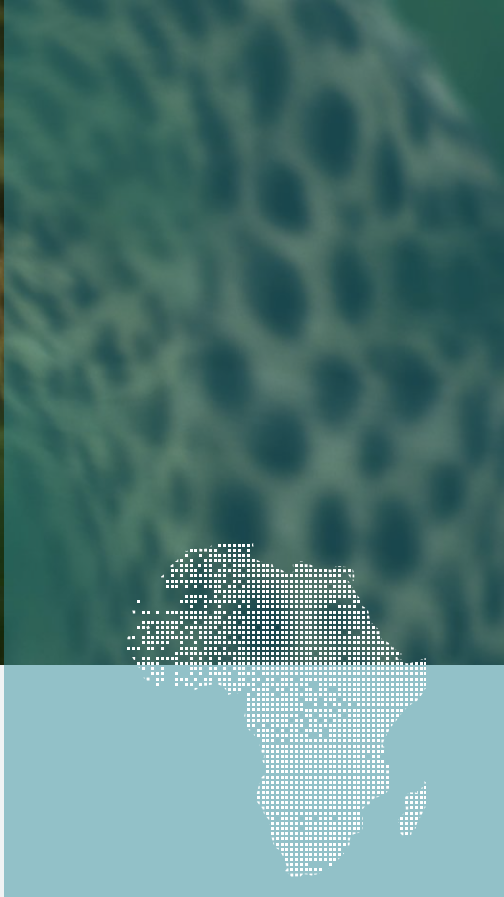




# Basics of Facultative Reinsurance

Daphne Sitole  
10 June 2021



01

About Munich Re

02

What is Facultative Reinsurance?

03

Typical Facultative Classes of Business

04

Advantages & Disadvantages of Facultative

05

Overview of Proportional & Non-Proportional Fac

06

Underwriting Information Required

# About Munich Re



# Munich Re Facultative & Corporate (F&C)



**More than 550 Experts** Represented in  
>20 countries, we offer:

- Best in class knowledge
- Underwriting expertise
- Tailor-made solutions

## Our Regions

- North America
- Latin America & Liberia
- Asia Pacific, Middle East and Africa



# Facultative Property / Engineering Team MRoA

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<b>Alice Shoba</b> Junior Underwriter	<b>Nyiku Nkuna</b> Junior Underwriter Munich
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# What is Facultative Reinsurance?

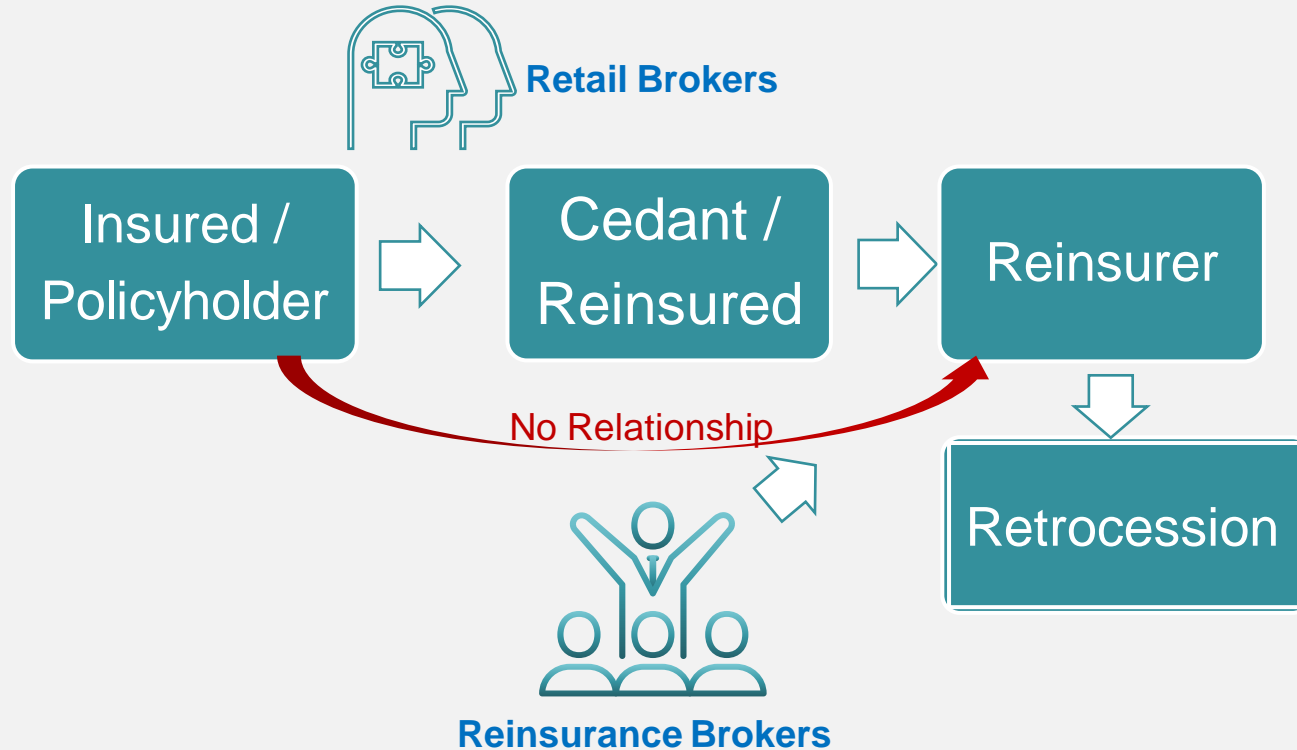


# Quick Recap on Reinsurance “Munich Re”

Reinsurance is a transaction whereby one insurance company (**the “Reinsurer”**) agrees to indemnify another insurance company (**the “reinsured”, “cedant” or “primary” company**) against all or part of the loss that the latter sustains under a policy or policies that it has issued.

For this service, the Ceding Company **pays** the Reinsurer a **premium**.

The purpose of reinsurance is the same as that of insurance to **spread the risk**.



# Definition of Facultative Reinsurance

“Facultative reinsurance involves a practice between insurance companies whereby a ceding company offers special or individual risks that it **decides to reinsure** to a proposed reinsurer which has the **free choice to accept** part or all, **or** may **reject** part or all, of risks offered”.

*Reinsurance* (1st Edition) - Kenneth Thompson.

Original Insurer is **not obliged to offer** and the Reinsurer is **not obliged to accept** (optional)



- Each risk is considered **individually**
- Each risk is a **separate reinsurance contract**

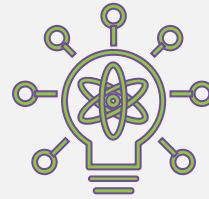




# Characteristics of Facultative & Treaty Reinsurance

## Facultative Reinsurance

- ❑ Earliest form of Reinsurance
- ❑ Single Risk Placement
- ❑ Right to accept or reject each risk on its own merit
- ❑ Risk Selection process (portfolio steering) protect balance sheet
- ❑ Can protect treaty from adverse UW results
- ❑ Adapts to short-term ceding philosophy of the insurer (Fac Buy Strategy, Tailor Made Solutions)
- ❑ Signing slip to confirm each transaction
- ❑ Can reinsure a risk otherwise excluded from the treaty



## Treaty Reinsurance

- ❑ No individual risk acceptance by the reinsured
- ❑ Obligatory acceptance by the reinsured of covered business
- ❑ A long-term relationship in which the reinsurer's profitability is expected, but measured and adjusted over an extended period of time
- ❑ Less costly than “per risk” reinsurance
- ❑ One treaty contract encompasses all subject risks.

# Typical Facultative Classes of Business



## Property / Fire



- Chemical, Heavy Industry, Energy, Mining
- Property Portfolios, Retail
- Airports & Ports
- Motor Assembly Plants
- Food & Beverage Manufacturing Industry
- Paper Mills
- Printers
- Telecommunications
- Hospitals and Clinics

## Engineering



### Once off policies (Projects)

- Construction All Risks (CAR)
- Erection All Risks (EAR)
- ALoP/DSU following CAR or EAR
- Renewable Energy

### Annually renewable policies

- Electronic Equipment Insurance (EEI)
- Machinery Breakdown Insurance (MB) and Loss of Profits (MLoP)
- Plant All Risks (PAR) or Contractors Plant and Machinery (CPM)

## Marine



- Hull and Machinery
- Pleasure Craft
- Cargo Insurance
- Goods In Transit
- Once-off Project Cargo Insurance
- Stock Throughput Insurance
- Marine Liabilities

## Casualty



- General Liability with all the necessary extensions
- CAR Section II
- Professional Indemnity
- Passenger Liability
- Personal Accident
- Motor
- Fidelity Guarantee

## Cyber



### First Party & Third Party Cyber

- Very high risk appetite:**  
Automotive/Aerospace/Manufacturing, Pharmaceuticals, Financial Institutions, Energy, Retail, Telecom/Media
- Medium risk appetite:**  
Healthcare / Hospitality, Transport, Media, Professional Services, Food and Beverage, Defense, Agriculture
- Low risk appetite:**  
Public Authorities, Airlines, Gambling, Metal Processing, Education, Gaming

## General risk appetite

- General light and non-manufacturing risks
- Pharmaceuticals
- Telecommunications & financial institutions
- Hospitals and healthcare
- Property owners & retail
- Automotive industry
- Metal processing and metal goods
- General chemicals
- Metro municipalities
- Low & medium hazard warehousing
- Beverages, breweries and wineries
- Agricultural risks
- Food and beverages
- Cement, rubber and tyres
- Plastics, printing and paints
- Sugar mills
- Airports and ports
- Schools and universities
- Tank farms and filling stations

## Out of scope

- ✗ Recycling & scrap
- ✗ Abattoir & poultry
- ✗ Stand-alone cold storage
- ✗ Fertilizer & explosives
- ✗ Edible oils
- ✗ Foamed plastics
- ✗ Primary smelting
- ✗ Leather, textiles, upholstery and mattresses
- ✗ Wood products, timber and sawmills
- ✗ Tobacco

[www.mentimeter.com](http://www.mentimeter.com)

Code: 2357 7838



- Name at least 2 Classes of Business that were affected in the 9/11 Catastrophe**

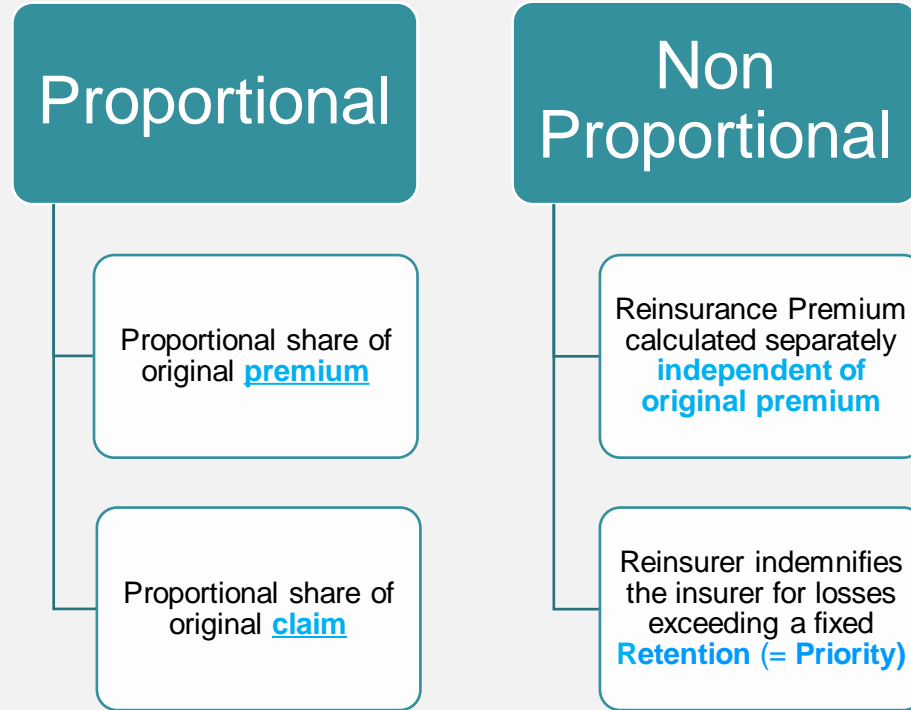
# Overview of Proportional and Non-Proportional Facultative



# 4



## Example of Prop vs Non-Prop

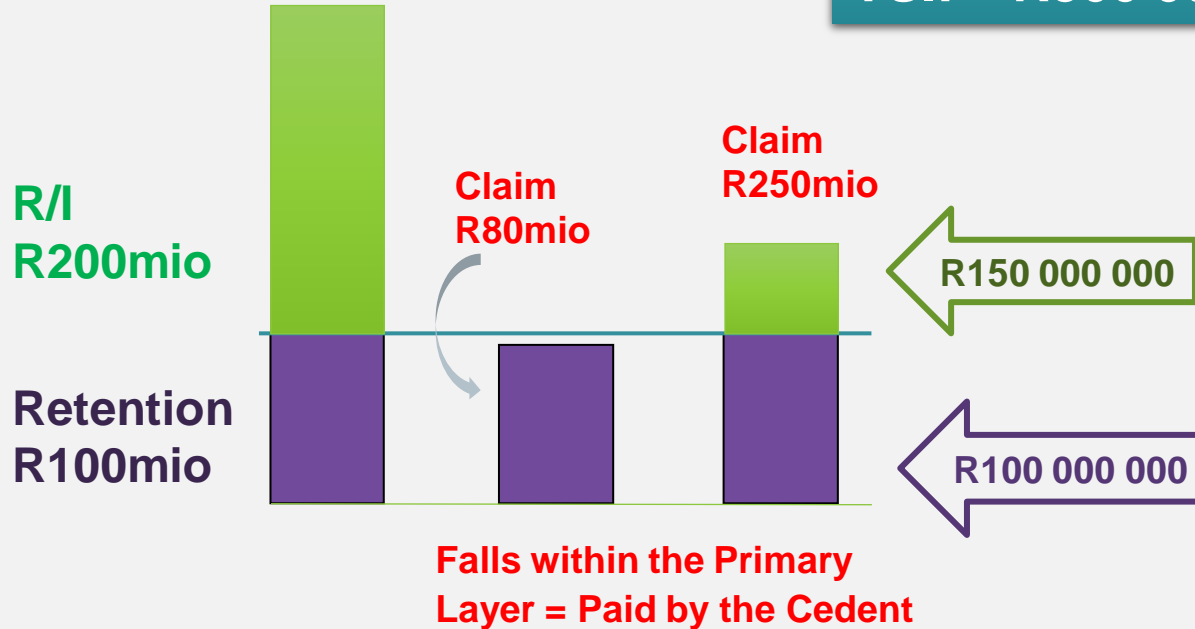




	<b>Retention 20%</b>		<b>Reinsurance 80%</b>	
			<b>Cedent</b>	<b>R/I</b>
<b>Sums Insured</b>	<b>R100mio</b>		<b>R20mio</b>	<b>R80mio</b>
<b>100% Premium</b>	<b>R100,000</b>		<b>R20,000</b>	<b>R80,000</b>
<b>CLAIM</b>				
<b>Large Loss</b>	<b>R60mio</b>		<b>R12mio</b>	<b>R48mio</b>
<b>Partial Loss</b>	<b>R8,000</b>		<b>R1,600</b>	<b>R6,400</b>

# Non Proportional Example

**Buildings Combined**  
**TSI: R300 000 000**



# Advantages & Disadvantages of Facultative Reinsurance

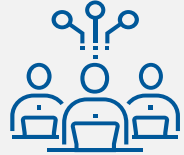


# Advantages of Facultative Reinsurance



- Need for technical expertise
- Original u/w can **pick and chose those risk which require protection**. They only pass reinsurance premiums over on those risks which are identified as being definite need of reinsurance protection.
- Reinsurance u/w can consider the risk on an **individual basis** and has the option to **accept or decline** the proposal.
- Spreading of risk**, which is a major benefit of reinsurance
- If a broker is involved, it will benefit from the **brokerage fees** received from placing facultative reinsurance
- The cedant will also gain reinsurance **commission on the cession** to partly reimburse it for the expenses incurred in obtaining and servicing the original business.

# Disadvantages of Facultative Reinsurance



- ❑ Can be **expensive** as the insurer is reducing premium income by paying a portion to reinsurers.
- ❑ It can be **time consuming** – The insurance company must contact **several reinsurers** for each risk offered to **obtain the best terms**. On large risks there can be a panel of reinsurers, each of which **requiring separate negotiations** with the insurer.
- ❑ Large amount of **administration** involved as insurer must disclose full details of each risk to the reinsurer(s).
- ❑ The insurer may **not be able to confirm cover immediately** as it needs to wait on the facultative reinsurer to revert back on the acceptability of the risk.
- ❑ Due to the above, the **rates of commission** offered will be **lower** on facultative cessions than under treaties.

# Disadvantages of Fac vs Advantages of Treaty

## Disadvantages of Facultative Reinsurance

- Uncertainty
- Administration intensive
- Errors and Disputes
- Reinsurance Commission



## Advantages of Treaty

- Certainty
- Administration is less
- Continuity
- Commission

# Underwriting Information Required



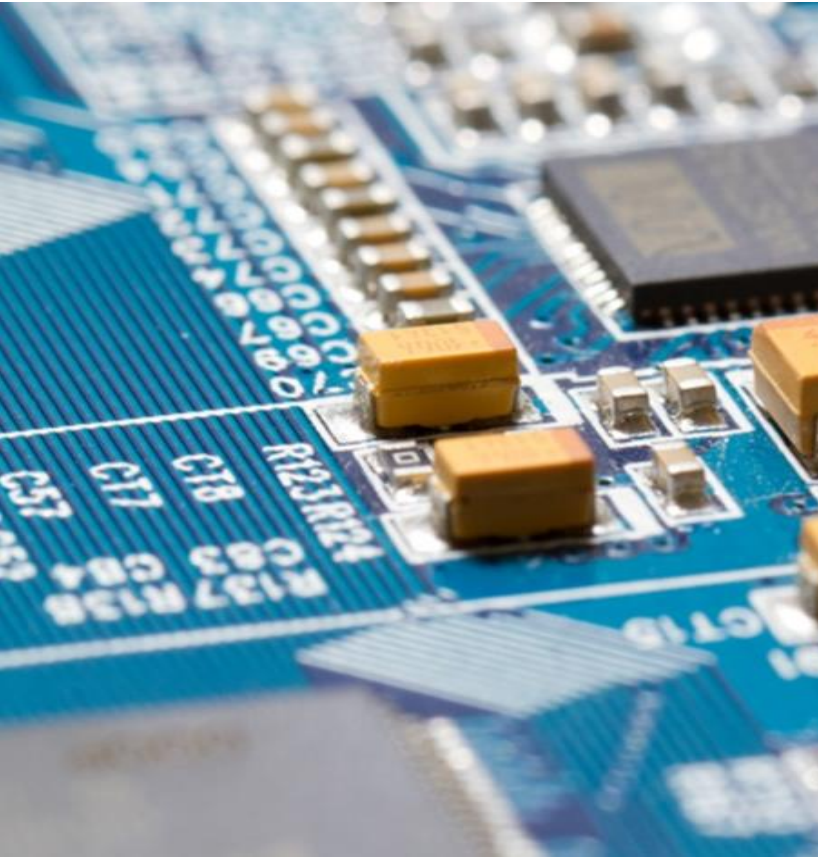
# Underwriting Information Required

- Name of Cedent & Retention
- Insured Name (Risk)
- Type of Cover
  - ❖ Buildings Combined
  - ❖ Assets All Risks
  - ❖ Misc (i.e. Burglary/Theft, Money)
- What do they do (Nature of occupation)
- Policy Period
- Physical Address of Insured Premises
- Total Sums Insured
  - ❖ Breakdown per location between Physical Damage and & Business Interruption
- Deductible Structure
- Structure of Placement (Prop/Non-Prop)
- Original Policy Wording





# Underwriting Information Required, continued...



## Loss History

- Minimum last 3 years
- Details of Loss & Mitigation Measures
- FGU Details “from the ground up”.

## Property Survey Reports

- Not older than 2 years
- Feedback on previous risk improvement requirements
- must cover at a minimum the basic “4” **COPE**
  - ❖ Construction details (Standard/Non-Standard)
    - Fire Walls/Doors
    - Spatial Separations
  - ❖ Occupation details – how, what, where (processes)
  - ❖ Protections – Sprinklers, Extinguishers, etc.
  - ❖ Exposure (Plant & Human Element)
    - + Natural Catastrophe
    - + P.M.L and M.F.L Scenarios

# No amount of premium can justify a bad risk



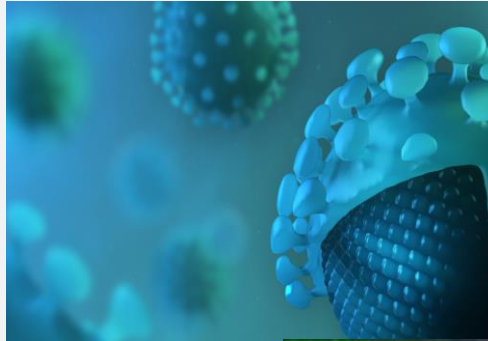
A fire extinguisher under the table



**Risk Quality is the Driving Force**

# Future Challenges of Facultative Reinsurance

- Water
- Pandemics
- Climate Change
- IOT
- Cyber
- Drones
- Driverless Cars



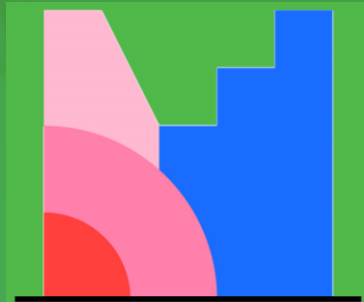
Thank you  
Any Questions



*All images used are from MRM Media Portal.*



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