Marsh | GREEN ISLAND Reinsurance Treaty

Green Island Reinsurance Treaty

Program summary

Established in January 1997, Green Island is a treaty reinsurance arrangement. Green Island enables captive insurance companies to diversify their underwriting portfolio. Through a pooling mechanism, participating captives "share" their loss experience by transferring a portion of their risk in exchange for assuming a percentage share of the risks of other treaty participants. By accepting other participants' risks, participating captives can diversify their underwriting portfolio by writing unrelated premium.

In addition to providing captives with risk diversification, participation in Green Island may result in a reduction in the variability of expected losses for individual members as each member will be writing a smaller portion of a large pool of losses. This potential benefit has been proven time and again for individual members over the life of Green Island. The reduction in loss variability produced by the pooling mechanism is designed to stabilize cash expenditures on losses assumed by participants.

Proven success

Since its inception in 1997, Green Island has grown substantially and is the largest, most diversified facility of its kind, with 22 participating captives and estimated annual premiums of US$600 million in 2021. Green Island has grown to a level that enables it to accept participants of various sizes — including the very large — while still, typically, providing significant amounts of unrelated risk.

General operation of the program

Green Island is based on the assumption and distribution of a low limit primary retention, typically allowing losses to be estimated with a high degree of confidence. Participants can currently cede to Green Island the first US$300,000 per occurrence of the following lines of coverage:

- Workers' compensation (WC) and employers liability or Federal Employers Liability Act (FELA) liability;
- General liability, including products and completed operations (exclusions may apply); and
- Auto liability.
- WC or FELA are mandatory for participation, while remaining lines are optional.

Participation in the program is governed by a reinsurance agreement detailing accounting for losses, premium determination, transaction timing, membership application, appointment of advisors, and other issues involving management of the treaty arrangement. The direction of the program is largely determined by the Participants' Committee and a number of subcommittees.

Potential advantages of the Green Island approach

- **Source of unrelated risk**: Can provide a source of recurring third party business by transforming related risk normally retained by a company into unrelated risk.
- **Reducing the variability of claims:** By participating in the treaty arrangement, members can diversify their captive's underwriting portfolio and reduce loss variability. The assumption of less variable claims should serve to stabilize captive cash flow and can assist with the internal budgeting process.
- **No additional capital or surplus required/lower frictional costs:** Captive owners have flexibility to structure the underlying program in a cost-effective way, including the use of selfinsurance, deductibles, or retrospective rating plans.

- **Transitioning from a ”Humana captive” structure:** As companies streamline their corporate structure and reduce the number of subsidiaries, they may seek to transition from a so-called “Humana model” captive strategy. IRS Revenue Ruling 2002-90 set the safe-harbor at 12 subsidiaries, with no one subsidiary accounting for more than 15% of the risk. Green Island may provide a suitable alternative structure that relies on unrelated risk as a positive factor in the test for status as an insurance company for US federal income tax purposes.
- **Fewer significant collateral concerns:** Green Island offers simultaneous accounting of premium payments and claims recoveries, meaning that credit risk may be decreased and participants can invest captive funds prudently and with fewer restrictions.

Other matters

By accepting other participants’ risks through Green Island, participating captives are left with “unrelated risk,” which is an element considered by the IRS when determining if a captive is an insurance company for tax purposes. IRS Revenue Ruling 2002-89 outlined a safe-harbor for captives writing at least 50% unrelated risk (providing that other key factors in the ruling are met).

With the implementation of FASB Interpretation 48 (FIN 48), companies are required, as part of the preparation of financial statements, to evaluate all transactions and make a determination of whether related tax benefits meet a “more-likely-than-not” recognition threshold (>50% certainty). If a position meets this threshold, a company would recognize for financial statement purposes the appropriate portion of the tax benefit that is likely to be realized upon ultimate settlement in its financial statements; the company would accrue interest and possibly penalties on the unrecognized portion of the tax benefit (the excess, if any, of the benefit claimed on its tax return over the amount recognized on its financial statements).

The amount of the tax benefit to be recognized by each company will depend on each company’s individual facts and the degree of confidence related to the position. Disclosure of the details of the uncertain tax position in financial statement footnotes may be required.

One of the goals of Green Island is to provide members with substantial unrelated premium and risk diversification. Each member should make its own evaluation of whether its captive will qualify for Federal insurance company tax treatment. Marsh makes no representation or assurance that Federal income tax treatment as an insurance company will be achieved by Green Island participants.

Candidates for Green Island

In order to be considered for participation in Green Island, ideal candidates must demonstrate:

- Existence of an active captive or a willingness to form a captive.
- At least US$4 million in retained losses within the first $300,000 layer of WC, FELA, general liability, and auto liability (WC/FELA only or lines combined).
- Financial strength of the participating captive and parent company.
- Strong risk management program with an excellent record on loss management and safety.
- Historical loss and exposure data that supports development of credible loss estimates.

Contacts

Donna Weber
+1 516 815 8344
donna.weber@marsh.com

Tanja Korff
+1 802 864 2752
tanja.korff@marsh.com

About Marsh

Marsh is the world’s leading insurance broker and risk advisor. With around 40,000 colleagues operating in more than 130 countries, Marsh serves commercial and individual clients with data-driven risk solutions and advisory services. Marsh is a business of Marsh McLennan (NYSE: MMC), the world’s leading professional services firm in the areas of risk, strategy and people. With annual revenue over $17 billion, Marsh McLennan helps clients navigate an increasingly dynamic and complex environment through four market-leading businesses: Marsh, Guy Carpenter, Mercer and Oliver Wyman. Follow Marsh on Twitter @MarshGlobal; LinkedIn; Facebook; and YouTube, or subscribe to BRINK.

Marsh is one of the Marsh McLennan Companies, together with Guy Carpenter, Mercer, and Oliver Wyman. This document and any recommendations, analysis, or advice provided by Marsh (collectively, the “Marsh Analysis”) are not intended to be taken as advice regarding any individual situation and should not be relied upon as such. The information contained herein is based on sources we believe reliable, but we make no representation or warranty as to its accuracy. Marsh shall have no obligation to update the Marsh Analysis and shall have no liability to you or any other party arising out of this publication or any matter contained herein. Any statements concerning actuarial, tax, accounting, or legal matters are based solely on our experience as insurance brokers and risk consultants and are not to be relied upon as actuarial, tax, accounting, or legal advice, for which you should consult your own professional advisors. Any modeling, analytics, or projections are subject to inherent uncertainty, and the Marsh Analysis could be materially affected if any underlying assumptions, conditions, information, or factors are inaccurate or incomplete or should change. Marsh makes no representation or warranty concerning the application of policy wording or the financial condition or solvency of insurers or reinsurers. Marsh makes no assurances regarding the availability, cost, or terms of insurance coverage. Although Marsh may provide advice and recommendations, all decisions regarding the amount, type or terms of coverage are the ultimate responsibility of the insurance purchaser, who must decide on the specific coverage that is appropriate to its particular circumstances and financial position.

1166 Avenue of the Americas, New York 10036

Copyright © 2021, Marsh LLC. All rights reserved. MA8-10185 534965778