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# ***Basics of Green Card Reinsurance***

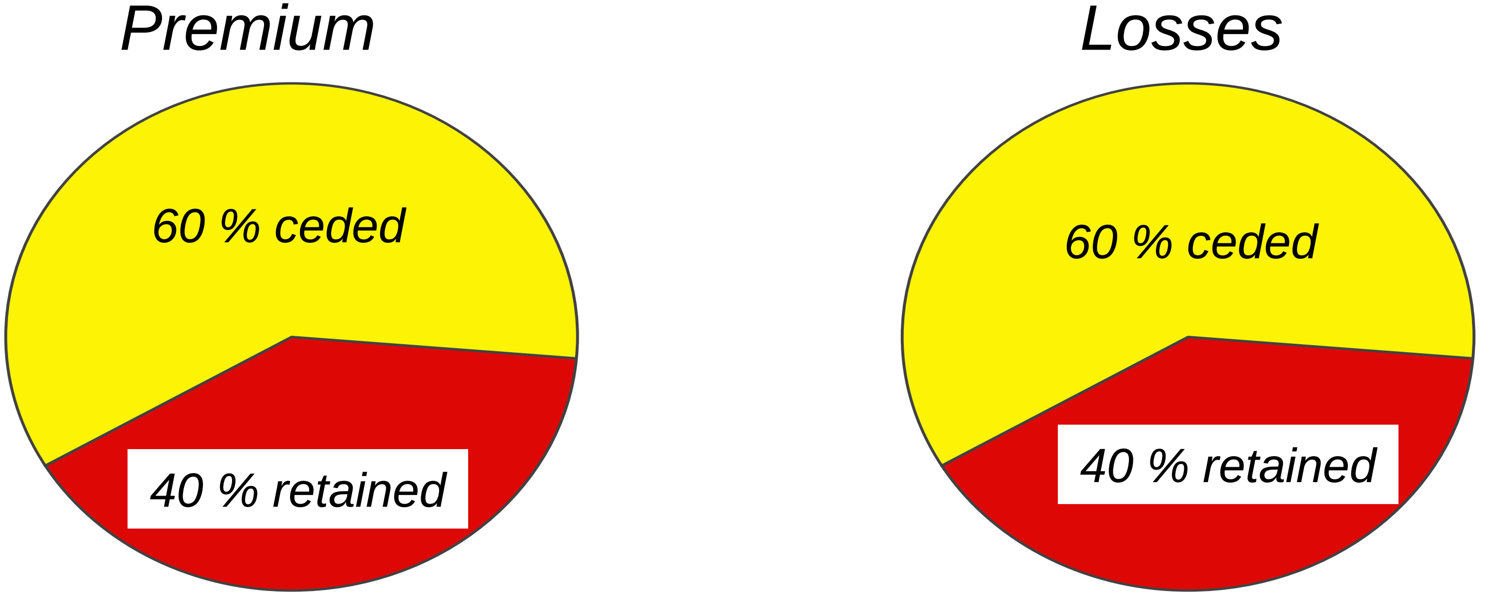
Sarajevo, 8th March 2001

# *1st alternative:*

# *Reinsurance on the basis of Quota Share*

*Example:*

- *40 % Retention*
- *60 % Cession*



# *Quota Share Characteristics (Example)*

1. *Retention : 40 % of claims and losses*
2. *Cession: 60 % of claims and losses*
3. *Commission : e.g.25 % of ceded premium payable to the Reinsured*
4. *Cash loss: Amount exceeding USD x*
5. *Accounts: Quarterly within 6 weeks. Confirmation within 2 weeks after reception. Settlement within 2 weeks after confirmation.*

## *Advantage of Q/S treaty for Reinsured*

- ***Replacement of capital (solvency ratio)***
- ***Reinsurance premium is payable in arrears***

## *Disadvantage of Q/S treaty for Reinsured*

- ***Significant amount of premium ceded to Reinsurers***

# *2nd alternative:*

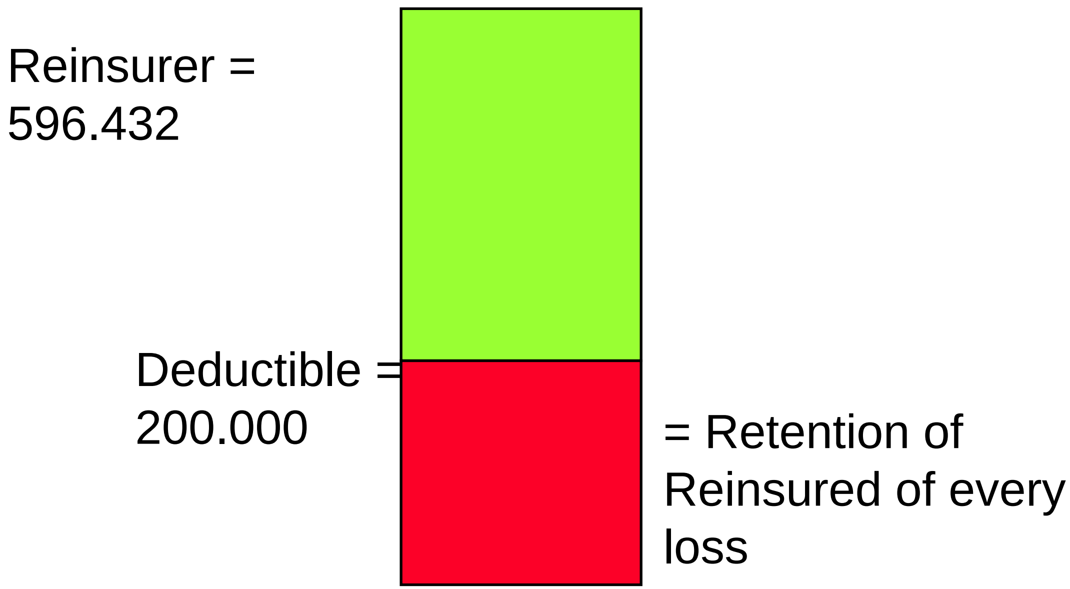
# *Excess of Loss (XOL) Reinsurance*

## ***Principle:***

***Reinsurer takes over the part of a loss which exceeds the (pre-defined) deductible***

## ***Example:***

Loss: 796.432



# *XOL Characteristics (Example)*

1. *Limit : in Green Card XOL by definition always “unlimited”*

2. *Deductible: USD 200.000*

3. *Based on the loss history of the specific portfolio, the Reinsurer quotes (calculates) a reinsurance premium. The reinsurance premium is expressed as a % of the Subject Premium Income (SUPI).*

# *XOL Characteristics (Example)*

*4. Definition of SUPI:*

- *Gross (Green Card premium before deduction of brokerage, commission)*
- *Net (Green Card premium net of reinsurance premium inuring to the benefit of this cover)*
- *Premium income (Collected premium income attributable to the reinsurance period)*

# *XOL Characteristics (Example)*

*It is important that both Reinsured and Reinsurers have the same understanding of the SUPI definition. Since in Bosnia Green Card is issued together with the domestic Motor Third Party Liability (TPL) policy the SUPI here is the total Motor TPL Premium. In other countries, e.g. Romania Green Card policies are issued independently from the domestic Motor TPL policy and therefore only the Green Card premium represents the SUPI.*

5. *Basis of cover: Losses occurring during the reinsurance period*

# *XOL Characteristics (Example)*

*6. Reinsurance Premium*

- *The Reinsured estimates an "Estimated Premium Income" for the reinsurance period to come for quotation purpose.*

- *The Reinsurer quotes a reinsurance premium expressed as a % rate of the SUPI (= EPI)*

- *During the reinsurance year: the Reinsured pays a Minimum & Deposit Premium (M&D) on a quarterly basis in advance and in equal installments to the Retrocessionaire. Standard: 1. Jan., 1. Apr., 1. July and 1. Oct.*

# *XOL Characteristics (Example)*

*6. Reinsurance premium (continued):*

- *Because of the estimated character of the EPI on which basis the M & D premium is calculated, the M & D varies between " 80 % and 90 %" of the (estimated) earned reinsurance premium.*

- *After the end of the reinsurance period, the reinsured pays to the reinsurers the adjustment premium, being the difference between the actual earned reinsurance premium ( = SUPI * reinsurance rate) and the M & D Premium already paid.*

***Advantage of XOL treaty for Reinsured***

- ***Reinsurance premium depends heavily on treaty performance***
- ***Relatively small amount of premium ceded***
- ***Easy administration***

***Disadvantage of XOL treaty for Reinsured***

- ***Reinsured retains deductible on <u>every</u> loss***

# *Specific XOL Clauses*

***1. Index clause:***

- *Green Card is a long-tail line of business.*
- *Index clause aims to keep the level of the deductible at the time of loss settlement as originally agreed.*
- *How : by indexing the deductible and the limit with an index agreed in advance (usually wage or consumer price index).*
- *The index to be used is the respective index of the country where the loss occurred.*

# *Specific XOL Clauses*

***1. Index clause (continued) :***

*Example:*

- *German Wage Index*
- *Basis: 1. January 1994 (inception date of cover) in Germany*
- *Date of Loss: 5. October 1994*
- *1st payment: 16. May 1996 DM 455.673*

  *2nd payment: 28. Aug. 1998 DM 323.432*

  *3rd payment: 12. July 2000 DM 223.555*

- *Layer: Unlimited XS DM 200.000*

## ***1. Index clause (continued) :***

*Example A:*

| Payment date | Unindexed payment | Index | Indexed payment |
|---|---|---|---|
| 16.5.96 | 455.673 | 132 | 455.673 |
| 28.8.98 | 323.432 | 144 | 276.265 |
| 12.7.00 | 223.555 | 151 | 182.101 |
| Total | 1.002.660 | | 914.039 |

*Outstanding losses: nil*

*Indexation of deductible:* $\frac{1.002.660}{914.039} * 200.000 = 219.391$

*Reinsurance recovery: 1.002.660 less 219.391 = 783.269*

## ***1. Index clause (continued) :***

*Example B :*

| Payment date | Unindexed payment | Index | Indexed payment |
|---|---|---|---|
| 16.5.96 | 455.673 | 132 | 455.673 |
| 28.8.98 | 323.432 | 144 | 276.265 |
| | | | |
| Total | 779.105 | | 731.938 |

*Outstanding loss: DEM 250.000*

*Indexation of deductible:* $\frac{779.105}{731.938} * 200.000 = 212.888$

*Reinsurance recovery: 779.105 less 212.888 = 566.217*

# *Specific XOL Clauses*

***2. Ultimate Net Loss Clause***

*Defines what constitutes the loss amount recoverable under the cover:*

*Recoverable: - all loss payments*

*- all loss adjustment payments*

*Deductions: - all recoveries, claims and salvages from other reinsurance protections which inure to the benefit*

*of this cover*

*- salaries of employees and office expenses*

# *Specific XOL Clauses*

## *3. Net Retained Lines Clause*

*Defines what constitutes the ultimate net loss amount recoverable under the cover:*

*1) only that part of a loss which the company retains net (after any priority reinsurance cessions) for its own account*

*2) the liability of the reinsurer shall not be increased due to one of the following reasons:*

*- reinsured's error or omission resulting in an increased net retention; e.g. wrong reinsurance coding in the reinsured's books*

*- nor by a failure of the reinsured to reinsure according to its normal practice, e.g. reinsured has not bound the risk in his books into a priority cession*

*- nor by the fact that the reinsured can not recover a loss from another reinsurer participating in this cover.*

# *Specific XOL Clauses*

***4. Currency Fluctuation Clause***

*handles losses occurred in a currency other than the contract currency (DEM). All paid loss amounts shall be converted into DEM at the rate of exchange of the settlement date.*

# London Agreement

1) **<u>Legal and organizational bases for the  London Agreement of 19/20 October 1989</u>**

- UNO recommendations of 1949 and 1984 and the Multilateral Guarantee Agreement of 15 March 1991

- EEC Guideline of 24 April 1972
  or relevant future international agreement

# *London agreement*

**Purposes of the agreement:**

To realize a European internal market by facilitating the free traffic of persons, goods and services in Europe.

To provide comprehensive protection for victims of traffic accidents by ensuring that motor vehicles normally used in one country have adequate insurance protection when visiting another country.

# *London agreement*

The International Green Insurance Card guarantees that claims will be adjusted in accordance with the compulsory insurance of the host country.

Within the scope of application of the Multilateral Guarantee Agreement, this card is superseded by the official registration.

# *London agreement*

The body responsible for administering and applying the London Agreement is the Council of Bureaux.
In the individual member countries, the national Green
Card Bureaux are responsible for implementing the
London Agreement as a

**Handling bureau:**
established by motor liability insurers, recognized by the government and responsible for adjusting claims to indemnification within the respective country as prescribed by this agreement

# *London agreement*

**Paying bureau:**

responsible for issuing Green Cards and fulfilling the concomitant obligations vis-á-vis the handling bureau

# *London agreement*

**Rights and obligations of the handling bureau:**

- To clarify the circumstances of accidents and allocate liability
- To inform the paying bureau and act in its best interest, yet in conformity with the relevant law of its country
- To exercise exclusive competence in applying and interpreting the law of its country

# *London agreement*

- To exercise unrestricted authority in adjusting claims falling within the purview of compulsory insurance

- To fulfill its obligation to consult and reach agreement with the paying bureau regarding the adjustment of claims that exceed the conditions or minimum sums insured stipulated by the law governing compulsory insurance