The Outlook for Insurance Captives in 2024

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The captive insurance industry is evolving rapidly, poised to reach a projected \$250 billion global market value by 2028. This surge among businesses seeking alternative coverage methods and cost reduction underscores the need for a comprehensive understanding of trends, challenges and opportunities. As we look ahead to 2024 and beyond, it will be helpful for businesses and investors to examine the trends and future trajectory of captive insurance market, and assess the advantages and disadvantages of captive arrangements to determine how they maybe be able to use them to navigate an ever-changing financial landscape. Advantages and Disadvantages of Insurance Captives The formation of an insurance captive is complex and requires careful consideration of multiple factors, including tax implications, regulatory environment and operational considerations. Before deciding whether an insurance captive is the ideal solution for a company's risk management needs, it is important to carefully weigh its advantages and disadvantages. One of the main advantages of forming an insurance captive is that it can reduce the amount of risk retained by the parent organization. This reduction is achieved by transferring some of its risk to a third party. Insurance captives also offer companies access to more competitive pricing options than traditional insurers while providing greater control over claims-handling processes. On the other hand, one of the drawbacks associated with setting up an insurance captive is that it requires substantial costs including capitalization requirements, as well as formation and legal fees that can be prohibitive for smaller organizations. In addition, insurance captives are subject to state and federal regulatory requirements, which can result in considerable administrative costs and paperwork. Regulations can also change over time. For instance, the Internal Revenue Service (IRS) recognizes insurance captives as legitimate risk management tools only if risk distribution and risk shifting are present. In general, captives must meet certain operational standards and may be subject to additional taxes imposed by the IRS. While insurance captives offer potential tax benefits, they do not automatically guarantee them, and these benefits must be assessed on a case-by-case basis depending on individual circumstances. Ultimately, forming an insurance captive requires careful consideration of multiple factors. Trends in Insurance Captives Despite the potential difficulties, many companies are turning to this risk management strategy. Between 2019 and 2022, the global captive insurance market increased 24.8% with total premiums written reaching \$72 billion in 2021. This growth is expected to continue in the coming years, driven by factors such as rising insurance costs and the

need for more control over insurance coverage. However, the impact the downturn in 2023 is going to have is not yet known. Regardless of the effects of the past year, several trends could impact the use and growth of insurance captives, including: Diverse coverage: The use of captives for nontraditional risks is expected to continue and increase, spanning areas such as life, health and annuity insurance. For example, in 2019, Marsh Captive Solutions established the first captive insurance program for a retirement plan, enhancing risk management for employee benefits. Cyber insurance: Cybersecurity risks are a growing concern for businesses of all sizes and industries. It is likely captives will continue to play an increasing role in providing tailored coverage for these types of risks. These solutions address the rapidly evolving nature of cyber threats and offer businesses greater flexibility and customization. Increased regulation: Regulatory bodies globally are increasing their oversight of insurance captives. Stringent regulations are being enforced in the United States and Europe to counter tax avoidance and prevent misuse, and ensure businesses are in compliance. This may lead to greater reporting and capital requirements for captive insurers, which could impact their profitability. Technological advancements: Technology is rapidly changing the way insurance is provided, and captives are no exception. Insurtech companies are providing new solutions, some of which could revolutionize the industry, including advanced data analytics and tools, software platforms for claims and risk management, and blockchain technology. For example, with its secure and transparent digital framework, blockchain could streamline policy management, reduce fraud, increase efficiency, enhance claims processing, and provide real-time risk insights. As technology evolves, captives will need to continue to embrace technological advancements to remain competitive. Globalization: As businesses scale operations globally, international captives will continue to gain prominence. While captives are more efficient for providing insurance coverage for multinational risks, businesses will need to navigate complex regulations and tax laws in each country. Alternative risk transfer: Captives are one form of alternative risk transfer (ART) offering businesses unique risk transfer options outside of traditional channels. ART solutions, like captives, risk retention groups and insurance-linked securities, may gain traction as businesses look for new ways to manage unique or difficult-to-insure risks. Expansion Into new markets: As companies become more comfortable with captives, we will likely see the expansion of captive insurance into new markets and industries, addressing where traditional insurance coverage is limited or unavailable. Collaboration with traditional insurers: Collaboration between captives and traditional insurers will provide more comprehensive insurance solutions, combining customized and general coverage. The future for captives is likely to be shaped by increased regulation, technology, globalization and new alternative risk transfer solutions. While these can also bring challenges and a need to stay ahead of emerging risks, they are likely to remain a popular option for businesses looking to manage their risks in a more customized and cost-effective way. The benefits are likely to outweigh any obstacles in the years to come and as a result, we can expect to see continued growth and innovation in the captive insurance industry.

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