
Global Certificate Course in Reinsurance Pricing Models

Reinsurance Contract Types and Structures

In the global certificate course in Reinsurance Pricing Models, it is essential to understand the key terms and vocabulary for Reinsurance Contract Types and Structures. This explanation will cover the following topics: Treaty Reinsurance, Facultative Reinsurance, Proportional Reinsurance, Non-Proportional Reinsurance, Quota Share, Surplus Share, Excess of Loss, and Stop Loss.

Treaty Reinsurance is a type of reinsurance agreement where the reinsurer agrees to cover a specified portion of the risks that the ceding company underwrites during a specified period. There are two types of treaty reinsurance: Facultative and Automatic. In Facultative treaty reinsurance, the ceding company submits each risk to the reinsurer for approval, while in Automatic treaty reinsurance, the ceding company has the authority to bind the reinsurer to the coverage of the risks within the agreed-upon terms.

Facultative Reinsurance is a type of reinsurance agreement where the ceding company submits individual risks to the reinsurer for approval. The reinsurer can either accept or reject the risk. If accepted, the reinsurer will bear a portion of the risk, as agreed upon in the contract. Facultative reinsurance is often used for unique or large risks that the ceding company wants to transfer to the reinsurer.

Proportional Reinsurance is a type of reinsurance agreement where the reinsurer agrees to bear a proportional share of each risk underwritten by the ceding company. There are two types of proportional reinsurance: Quota Share and Surplus Share.

Quota Share is a type of proportional reinsurance where the reinsurer agrees to bear a fixed percentage of each risk underwritten by the ceding company. For example, if the ceding company enters into a quota share agreement with a reinsurer for 50%, the reinsurer will bear 50% of each risk underwritten by the ceding company.

Surplus Share is a type of proportional reinsurance where the reinsurer agrees to bear a proportional share of the risks underwritten by the ceding company, but only after the ceding company has retained a specified amount of each risk. For example, if the ceding company enters into a surplus share agreement with a reinsurer for 50%, the reinsurer will bear 50% of the risks underwritten by the ceding company, but only after the ceding company has retained the first 20% of each risk.

Non-Proportional Reinsurance is a type of reinsurance agreement where the reinsurer agrees to bear a specified amount of each loss, but only after the ceding company has incurred a specified retention. There are two types of non-proportional reinsurance: Excess of Loss and Stop Loss.

Excess of Loss is a type of non-proportional reinsurance where the reinsurer agrees to bear a specified amount of each loss, but only after the ceding company has incurred a specified retention. For example, if

the ceding company enters into an excess of loss agreement with a reinsurer for \$1 million excess of \$100,000, the reinsurer will bear the next \$1 million of each loss, but only after the ceding company has incurred \$100,000 of each loss.

Stop Loss is a type of non-proportional reinsurance where the reinsurer agrees to bear a specified amount of each loss, but only after the ceding company has incurred a specified retention, and the loss exceeds a specified percentage of the ceding company's premiums. For example, if the ceding company enters into a stop loss agreement with a reinsurer for 10% of the premiums, the reinsurer will bear a specified amount of each loss, but only after the ceding company has incurred a specified retention, and the loss exceeds 10% of the ceding company's premiums.

In practical applications, reinsurance contract types and structures are critical in managing the risks that insurance companies underwrite. Reinsurance enables insurance companies to transfer a portion of the risks they underwrite to reinsurers, allowing them to maintain their solvency and financial stability. Proportional reinsurance, such as quota share and surplus share, enables insurance companies to transfer a fixed percentage of each risk to reinsurers, ensuring that they have sufficient capacity to underwrite more risks. Non-proportional reinsurance, such as excess of loss and stop loss, enables insurance companies to transfer a specified amount of each loss to reinsurers, ensuring that they have sufficient capacity to absorb large losses.

When selecting a reinsurance contract type and structure, insurance companies must consider several factors, such as their risk appetite, capitalization, and underwriting strategy. For example, if an insurance company has a low risk appetite, it may prefer to enter into a proportional reinsurance agreement, such as quota share, to transfer a fixed percentage of each risk to reinsurers. If an insurance company has a high risk appetite, it may prefer to enter into a non-proportional reinsurance agreement, such as excess of loss, to transfer a specified amount of each loss to reinsurers.

Despite the benefits of reinsurance, insurance companies must also be aware of the challenges associated with reinsurance contract types and structures. For example, if an insurance company enters into a quota share agreement, it may have limited control over the risks it underwrites, as the reinsurer will bear a fixed percentage of each risk. Additionally, if an insurance company enters into an excess of loss agreement, it may have limited capacity to absorb large losses, as the reinsurer will bear a specified amount of each loss.

In conclusion, understanding the key terms and vocabulary for Reinsurance Contract Types and Structures is essential in the global certificate course in Reinsurance Pricing Models. Treaty reinsurance, facultative reinsurance, proportional reinsurance, non-proportional reinsurance, quota share, surplus share, excess of loss, and stop loss are critical concepts in reinsurance contract types and structures. By understanding these concepts, insurance companies can manage their risks more effectively and maintain their financial stability. However, insurance companies must also be aware of the challenges associated with reinsurance contract types and structures and carefully consider their risk appetite, capitalization, and underwriting strategy when selecting a reinsurance contract type and structure.