



About AIG’s Fronting Fees for Captive Programs



At AIG, we believe that being a world class fronting company means delivering inventive and cost-effective solutions. We are committed to providing value for price, and in order to accomplish this, it is important to us that our pricing is clear and easy to understand.

Our role as a fronting company is to issue an insurance policy to an insured and then, transfer some or all of this risk either to the insured’s captive or to the insured itself. This reliance on the insured to reimburse us for losses paid under the policy, creates a credit exposure for AIG. In addition, we need to allocate capital to support our credit, operational, regulatory, tax and legal risks. Therefore, many factors must be taken into consideration when determining fronting fees for a captive program. Is it a single country or multinational program, and if the latter, how many countries are included? How many transactions—policies, premium transactions, certificates, claims, etc.—are involved with a program? What level of premium and claims will be going through our books? Are there any special servicing or reporting requirements? These are just a few of the issues we consider when pricing our services.

To provide you with greater clarity around the costs and other factors associated with providing fronting policies, this brochure explains the major factors.

Fronting fees for all of our captive programs include the following:

1. Program Design and Administration
2. Credit Risk
3. Cost of Capital
4. Claims Handling Services
5. Profit

Fronting fees for our multinational captive programs also include the following:

6. Global Program Coordination
7. Local Servicing and Policy Issuance
8. Cash Flow Management and Reporting

To ensure the success of captive programs fronted by AIG, we undertake a well-tested, disciplined process built around each of these eight items. The information below provides more details.

For All Captive Programs

1. Program Design and Administration

The AIG team with primary responsibility for the program, typically called ‘the AIG producing office’:

- Works with the client and broker to determine a compliant fronting structure designed to best meet the client’s objectives



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1. Program Design and Administration (Continued)

- Calculates and secures agreement upon the fronting fee
- Determines, with the broker, agreed upon policy wordings
- Identifies with the broker any additional policy documentation or certification requirements
- Manages general inquiries
- Processes mid-term amendments, additions and deletions
- Is responsible for ensuring that the program is executed in accordance with the client's expectations
- Manages collateral requirements
- Coordinates legal documentation, such as reinsurance and indemnity agreements
- Oversees claims issues such as responding to inquiries, issuing claims bulletins to the other parts of AIG involved with the transaction, monitoring the performance of third party administrators, billing, reporting on billing, loss payments and remittances, etc.

2. Credit Risk

Our fee includes a risk charge for the credit risk we assume in the fronting structure. In a fronted transaction, AIG faces the credit risk of non-payment by the counter party, and this risk is impacted by the creditworthiness of the counter party and the amount of our credit exposure, which is tied to expected losses. Economic protection for AIG may require a combination of hard and/or soft collateral to mitigate this risk. Clients may be able to provide hard collateral or parental guarantees to reduce the impact of this credit risk upon the fee.

3. Cost of Capital

AIG must allocate capital to support the fronting transaction's impact on our credit, operational, regulatory, tax and legal risks. Accordingly, our fee structure considers:

- The capital costs for AIG to front business as determined through rating agency and regulatory capital models
- Regulatory conditions that may require AIG to hold collateral to support cessions to non-admitted reinsurers that result in potential capital costs (e.g., Schedule F penalty in the U.S.).

As an example of an operational risk, a program with a complex structure and coverage spanning many countries has an increased probability of an operational or documentation problem that may cause the fronting insurer to incur unforeseen costs. While these are not underwriting risks, they are risks nonetheless, and all insurers set aside capital to support these additional risks.

Captive owners might want to consider getting the captive rated by an approved, recognized rating organization. This rating will reduce the impact of the cost of capital upon fee since it provides capital relief for the fronting company as balances ceded to a non-rated reinsurer are treated harshly from a rating agency perspective.

4. Claims Handling Services

The local office that issues the insurance policy is responsible for:

- Managing all claims handled directly by AIG, including, but not limited to, coverage determination, investigation, setting reserves and making indemnity or expense payments
- Overseeing third party administrators
- Providing claims reports and supporting documentation to the reinsurer(s) when needed

5. Profit

Our business needs to return a fair and reasonable profit. This return is factored into our fee structure.

For Multinational Captive Programs

1. Global Program Coordination

In addition to program design and administration, the AIG producing office is the global coordinator for the program. These global coordination responsibilities include:



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1. Global Program Coordination (Continued)

- Agreeing upon wording for manuscripted master policy and local policies
- Working with the client and broker to agree upon the premium allocation methodology
- Issuing requests to the AIG network and network partner to invoice, collect and remit premiums and issue the local policy
- Providing the broker with an agreed payment schedule including estimated premium due to the captive
- Providing weekly/monthly tracking of the status of policy issuance and premium payments due to the captive
- Managing network partners (approval, premiums, claims, reporting)
- Responding to specific local issues and complexities

2. Local Servicing and Policy Issuance

The local AIG network and network partners issue local country policies and provide the necessary service throughout the period of insurance. Their activities include:

- Issuing locally admitted policies in accordance with agreed requests and local regulations
- Ensuring that local policy wording is compliant at the local level and complements the master policy wording
- Reporting any issues preventing the issuance of documents to the AIG producing office for resolution
- Calculating applicable premium taxes/charges, etc.
- Issuing in-country premium invoices in accordance with agreed instructions
- Collecting premium in accordance with local payment terms and settlement to the AIG reinsurance administrator which is responsible for the cash flow management of the program
- Reporting to the AIG reinsurance administrator on receipt of premiums
- Settling local cessions, taxes, etc., to relevant bodies
- Providing status reports detailing where premiums remain unpaid, with commentary on the reason given for non-payment to the AIG reinsurance administrator and/or the AIG producing office
- Claims management and administration

3. Cash Flow Management and Reporting

The AIG reinsurance administrator is the focal point for the financial administration of our captive programs around the world. Specific responsibilities include:

- Transferring funds to the reinsurer(s) following receipt of individual premium payments by AIG local offices
- Tracking and onward payment of reinsurance premiums to the captive and other reinsurers as well as the reporting and billing of losses
- Ongoing tracking and dialogue with the AIG network to identify any issues likely to impact attainment of the agreed upon service standard
- Providing the reinsurer(s) with both (a) a premium advice explaining what premium will be paid to them, and (b) a remittance advice when the premium is paid
- Issuing loss billings, paid loss and reserve loss reports on an agreed frequency to the reinsurer(s)
- Issuing notice and evidence of loss in accordance with the reinsurance agreement and claims protocols
- Monitoring reinsurance aggregates, advising the excess reinsurer(s) when aggregates are eroded and breached
- Making claim settlement remittances to AIG offices reporting the paid losses

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