REINSURANCE AND ITS IMPACT ON RISK MANAGEMENT

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Abstract

Capital and reserves of insurance companies, although are considerable amounts but compared with heavy accepted obligation is very small and insignificant. So in front of big events and the risks are extremely vulnerable. Development of economic activities, a large industrial unit, large fleet of aviation and naval, liability and accumulation risk in different fields of Liabilities insurance in insurance companies has increased continually. In world, the insurance industry has technology of constant and smoothness. In terms of existing the reinsurance system that is essential for any insurance company, all technical information and modern methods Issuing and compensation from a company to another company and so on quickly is transferred to all insurance companies operating in the international arena. The purpose of this article is familiar with a variety re-insurance systems and its impact on reducing the risks of companies.

Keywords: Reinsurance, Risk - Management, Control system, Commitments

1. INTRODUCTION

Insurance company to reduce its heavy obligations does not have way except transfer part of its commitment to other insurance company. This transfer is done in different ways, which is called reinsurance. As the insurer insure their property and assets in insurance companies. Insurance companies also insure themselves in other insurance company in front of the great heavy losses that may threaten their financial situation (reinsurance insurer). In fact, insurance companies will share third party called reinsurance insurer in the financial results of its obligations [3]. Reinsurance is the practice whereby insurer contribute other person called reinsurance insurer on the financial results of its insurance obligations in various ways. With reinsurance, risk among several insurance companies inside and outside the country will be divided. So in the event of large losses from financial situation an insurance company will not face a risk, in simple terms reinsurance means division and distribution of risk.

Mr. Aymerson in insurance contracts book published in 1783 has general definition reinsurance: “Reinsurance is contracts that based on insurer by considering specific premium transferred insured risk to second company while against primary insurer is responsible (Hoshangi, 1966). In reinsurance, insurers assume all or part of obligations of the quitter insurer against the amount of insurance premium. Basically, assignment of all portfolio of insurance company to a reinsurers is incorrect and It is essential that the insurance company directly or quitter undertake compensation of part of risk for greater precision in risk selection and the excess cede to reinsurers. To assignment all portfolio insurance says fronting [3].
Reinsurance is a specialized field that has no communication with general population. Therefore, only those who are active in reinsurance sector of the insurance company or insurance students are familiar with it more or less. So in this field written or published fewer articles. In general, purpose of reinsurance is risk reduction in term of statistical view and minimizes losses for the insurer. Insurers, risk assigned in order to reduce risks that have pledged. Reinsurance insurer's duty is support policyholder insurance companies against high losses and global distribution of risk. Directly the insurance company from its reinsurance insurer expects that:

- Be able to run a large risk to the company's ability increase in this area.
- In results of the technical operations of policyholder create stability.
- From policyholder institute support against general damage or heavy damage that is over from the financial resources.
- Geographical distribution of risks insured against the risk of catastrophic done the most desirable.
- It has been a way of entering and leaving in International markets.
- It receive technical and administrative assistance and facilities to improve procedures and systems such as computer and specific problems and technical and managerial [5].

2. BACKGROUND OF REINSURANCE
The first sign from Reinsurance record cruise in 1370AD. Louis IV by issuing a decree issued certificate reinsurance in France in 1681 AD. Reinsurance developed and spread in Europe in the eighteenth century until several regulations actually was developed in this field in1864 AD. So 1864 is a turning point in reinsurance. The first reinsurance companies were insurance companies depend on other firms. Today, many companies are still working too much power in the field of the world reinsurance. It noted to Swiss Reinsurance Company [7]. The first reinsurance company, which began as an independent and professional, is insurance company of Cologne Re which, was established in Cologne, Germany in 1864. In 1996 this company was in seventh ranks of reinsurance companies in terms of premium volume.

In England there were also many companies dependently that some of them left the scene of insurance and some are still working. But first companies that were established in England as a professional reinsurance companies by name Merkantail & General 1907 and British & European in 1908. Reinsurance in developing countries is often provided by public companies that these reinsurance company can be cited Chile in 1920 [4].

Table 1 - Names of 15 first reinsurance company rankings are issued based on the volume of premium (According Journal of reaction, March 1998)

<table>
<thead>
<tr>
<th>Row</th>
<th>Company name</th>
<th>premium volume (Millions of dollars)</th>
<th>Country name</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Munich Re</td>
<td>10,475</td>
<td>Germany</td>
</tr>
<tr>
<td>2</td>
<td>Swiss Re</td>
<td>4,372</td>
<td>Swiss</td>
</tr>
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3. LEGAL ASPECTS OF REINSURANCE AND ITS IMPACT ON REDUCING THE RISKS

Insured person not involved in the reinsurance contract and reinsurance doesn’t have also responsible against him/her. When reinsurer transfer risk, new contract create between policyholder insurer and reinsurance insurer. So briefly we can say:

• Reinsurance contract does not have any direct connection with insurance contracts.

• There is no a legal relationship between the insurer and reinsurance insurer in reinsurance contract that be able to communicate with each other and Insured person cannot do any legal action against a reinsurance insurer [3].

So as a principle must be admitted the relationship between insured and the insurer and the relationship between policyholder insurer and reinsurance insurer on the other hand are completely separated from each other. Under this principle, the insurer doesn’t have right which can’t directly request loses from reinsurance insurer, unless explicitly emphasize in reinsurance contract or special agreement is made. In some reinsurance markets, particularly in the United States of America with a special close-up (cut through) acquired the right in case of insurer issuer of insurance face with financial problem or credit and be unable to pay damages referred directly to reinsurance insurer and receive their compensation.

Today, during contracting reinsurance parties in contract can be expected that in case of conflict which country apply their law and in some cases such issue is not predicted according to customary international are governed law of given country [6].

Different types of reinsurance that can be leading to a decrease of risk:

1- Facultative Reinsurance (FAC)
2- Treaty Reinsurance
3- Facultative / Obligatory (FAC / Oblig)
4- Reinsurance Pool
1- **Facultative Reinsurance (FAC)**

This type of reinsurance is oldest form of reinsurance contracts [5]. Facultative Reinsurance is a form of reinsurance operations that reinsurance operations are performed case by case and separately for each risk.

Policyholder be entered into negotiations with a reinsurance insurer for any risks that need to reinsurance and will be concluded necessary contract. This insurer in reinsurance operations called contract leader. In this relationship should provide enough information about the risks to reinsurance insurer. Especially for large risks required such reports of visits, maps and ... for reinsurance insurer. Reinsurance insurer according technical knowledge and expertise assess accurately proposed risk and it will decide to accept or reject [3]. In Facultative Reinsurance, each transfer is considered an independent contract and is valid a certain time that is usually for one year and does not automatically renew, so that normally leader assumes share of its risk. In next step policyholder insurer offers to other insurers either directly or by reinsurance broker and policyholder insurer after receiving confirmation from all of reinsurance insurers, two copies of the contract are set and after signing sends for reinsurance insurers. Reinsurers insurance after signing a copy of it will be returned to Policyholder insurer. In Facultative Reinsurance, policyholder insurer is obligated to pay premiums on determined time [1].

Use cases of Reinsurance:

1-1 If that request reinsurance in the form of contracts is not interesting for reinsurance insurer.

1-2 Risk or venture be outside of existing contracts of policyholder insurance company.

1-3 Maximum and minimum maintenance be at particular risk of policyholder insurance.

1-4 A Facultative assignment be intended to a mutual assignment from reinsurance insurers.

2- **Treaty Reinsurance**

Treaty reinsurance is a kind of reinsurance operations that is done based on contract for limited or unlimited period between policyholder insurer and reinsurance insurer. In these contract obligations of each party is determined completely accurate. This type of reinsurance operations whereby all risks within the fit the contract is automatically covered by reinsurance policyholder insurer awarded what is in range of contract [3]. Major items in a reinsurance contracts include contributions to maintenance policyholder insurer, liability of reinsurance insurer, reinsurance fees, fees of reinsurance interests, geographic area, period of contract, premium save, storage of deferred compensation, cash compensation, how to send bills, exceptions of the contract and other common close in areas of field or topic contract [8].

As mentioned in Facultative Reinsurance, policyholder insurer after determining kind of contract as relative or non-relative entered into negotiations with a particular insurer that later called contract leader and in the field various items that were mentioned above to be agreed then contract agreed intended offers to other reinsurance insurers either directly or by reinsurance broker after receiving confirmation from all of reinsurance insurers attempt to providing summary contract that is called slip.
3. Facultative / Obligatory Reinsurance

Facultative / Obligatory Reinsurance that also called open reinsurance so that policyholder in assignment of risk in contract area has authority however in the case of assignment; reinsurance insurer is needed to accept. In other words, this contract is open [5].

This contract is usually signed for a limited number of insurance risks that have large capital and values. Since decision about assignment or not assignment is responsible for insurer and It is possible that policyholder insurer insure just risks that face with more damage, so practically reinsurance insurers isn’t seeking such contracts and are more interested that accept such risks through Facultative Reinsurance that have greater freedom in the analysis and their selection.

Facultative / Obligatory reinsurance contract will be concluded after filling capacity automatically contract and as a complementary tool for a limited number of insurance risks that has capital and value. Facultative / Obligatory reinsurance contract must have the following requirements:

3-1- There has been number of acceptable insurance risk to assignment.

3-2- The premium and its assignment amount are determined.

3-3- The target of policyholder insurer is not just high risk assignment insurance [3].

4. Reinsurance Pool

In this method, a number of insurance companies in a country or region established a pool and all or part of their portfolios allocated to pool as partnership agreement or capital surplus. This pool acceptance set from the member companies again be divided between them according to the following two factors.

4-1 - Assignment amount in each of members.

4-1 - Assigned portfolio profitability [3].

Pool management is usually assigned to one of the members. This member undertaken responsible running of the pool, preparing bills, maintains accounts and reinsurance operations including acceptance and concession. Costs of pool are divided to ratio volume of reinsurance operations, including the assignment or acceptance between all of members. In fact pool has no income or loss and balance of operation is zero.

Reinsurance pool has elements as the following:

1- Technical Committee: is responsible monitor on technical operations of pool

1- Executive Committee: they determine executive affairs of pool.

2- General Assembly: they are responsible for general rules - politics and policy of pool - determine pool's maximum capacity approval of the report of pool performance.
4. DISCUSSION AND CONCLUSION

It is true that the reinsurance helps in reducing risks but it has advantages and disadvantages as follows. One of facultative reinsurance advantage is to have freedom of action and other advantage is this type of contract is appropriate for the risks individual and case. But the disadvantages of facultative reinsurance are as follows:

1 - Delays in obtaining reinsurance coverage that due to require negotiate; sending information, assessing risk is inevitable.

2 - The high cost of contract because for every risk should negotiate separately with reinsurance insurer and for a lot of information to be exchanged.

3 - Limiting reinsurance insurer.

Treaty reinsurance advantages include generally accepted risk reinsurance insurer's commitment in the context of the contract; Low cost of operation treaty reinsurance compared to facultative reinsurance and the biggest disadvantage is the lack of maintenance of good risks, or risks that could keep it for reinsurance insurer.

Among the various forms of reinsurance has been alluded to Facultative / Obligatory (FAC / Oblig ) reinsurance . It is a form of treaty reinsurance. However, that cession of Facultative / Obligatory reinsurance is as force usually been determined by the government and has form of legal, this reason it is called legal reinsurance [2].
REFERENCES


