GUY CARPENTER

BC POULTRY INSURANCE STRATEGY

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MARSH & McLENNAN COMPANIES

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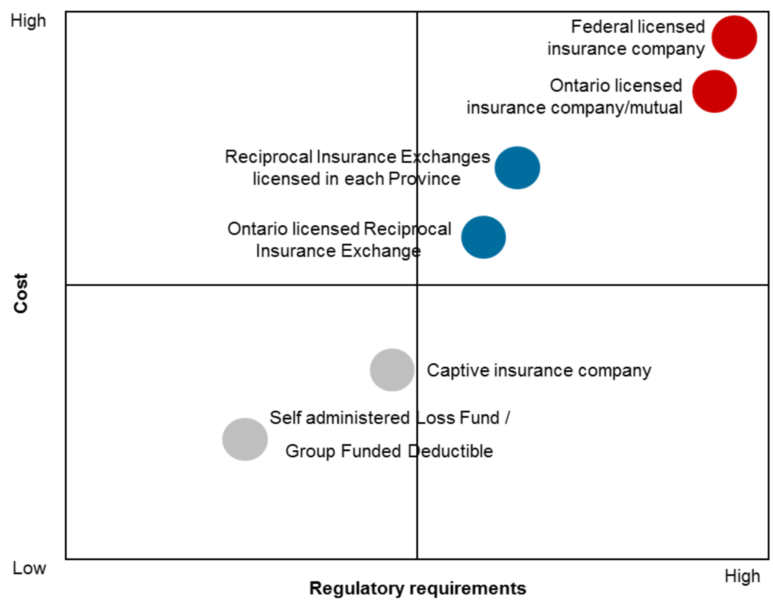
Group Funded Deductible

While premiums paid to a large traditional insurance company are pure expenses to the policyholder, certain other forms of risk management strategy can have an equity component. An equity component is typically more interesting to program members than pure expenses because there is an opportunity to build net worth.

A Group Funded Deductible (C&D Fund) is a custom designed strategy that would include an equity component for its program members, BC poultry producers.

The following diagram shows where a Group Funded Deductible stands relative to other forms of risk transfer vehicles.



The next table provides greater resolution on the operational benefits of a Group Funded Deductible. The rating scale should be looked at relative to delivery of the C&D insurance policy. Green is considered the most favourable for delivery of C&D polices, red is the least favorable, and yellow is neutral or in between.

Relative Program Comparison	Group Funded Deductible	Captive Insurance Company	Reciprocal Insurance Exchange	Licensed Insurance Company
Regulated entity, licensed under a regulatory body	Yellow	Yellow	Red	Red
Extensive, detailed documentation (financial reports, actuarial reports, etc.)	Green	Yellow	Red	Red
Need to hire and maintain own staff	Green	Yellow	Yellow	Red
Freedom of operation (Offerings/coverage, limits, premiums, capital levels, etc.)	Yellow	Yellow	Yellow	Yellow
Set up and operating costs (focus member contributions on loss funding)	Yellow	Yellow	Yellow	Red
Lean operational structure	Green	Yellow	Yellow	Red
Responsiveness of fund to losses (timeliness of loss payments)	Green	Green	Green	Yellow
Fund solvency requirements	Green	Yellow	Yellow	Yellow
Member "premiums" are tax deductible	Green	Green	Green	Green

The C&D Fund model is a form of mutualisation. While member policyholders are not directly responsible to each other for each other's claims, their fortunes are tied to the results of the insurance program. If the C&D Fund grows, the members benefit through the inherent equity in their shares of the C&D Fund. On the other hand, if the C&D Fund erodes, members are responsible for making decisions regarding the management of the C&D Fund. In either case, the Fund will require a certain amount of active management by the members.

From an accounting perspective the insurance premiums are treated as ordinary business expenses on the member's income statement, as is the case when paying premiums to a third party insurer. But unlike insurance premiums paid to a third party insurer, the surplus that builds inside the C&D Fund belongs to the program members

Capitalization Of The C&D Fund & Reinsurance

The C&D Fund must be capitalized and this can be accomplished by combination of an initial capital infusion from members and the first annual premium payment.

The JSCP (actuarial) report of September 13, 2017 suggests an initial capital infusion of $1,000,000 in the event that a captive insurer is formed. This capital assumption also applies to formation of the C&D Fund. A good portion of this amount can be subsidized through the AgriRisk Initiatives program offered by the Federal Ministry of Agriculture. Our understanding is that this program makes available up to $750,000 in the form of a perpetual interest free loan to be used as seed capital for programs like this.

The JSCP report goes on to recommend an annual premium of $198,000: assuming stop loss reinsurance with a retention of $100,000 at a cost of $105,000; administration expenses of $63,500; and a minor amount for adjusters fees. These expenses would also be applicable to operating the C&D Fund.

Reinsurance is required by the C&D Fund for financial risk management purposes. Reinsurance transfers risk from the C&D Fund to third party reinsurance companies in exchange for a premium. The premium is paid annually, and the coverage applies on a stop loss basis, meaning that the reinsurance layer pays after the C&D Fund retention of $100,000 is exhausted.

The C&D Fund will require third party administration, accounting and actuarial services. The estimated cost of these services has been noted above. Likewise for adjusting expenses.

Premium tax would not be incurred directly by the C&D Fund, but would be incurred indirectly through the fronting insurer. A fronting insurer is required issue retail insurance policies to the program members. The fronting insurer also deals with regulatory filings. A typical fronting fee is 5% of the gross insurance premium flowing through the program, plus the premium tax noted above.

Ownership Of The C&D Fund

The C&D Fund is a catastrophe program by nature. It is not expected to respond to frequency claims. In the absence of frequency claims it would be expected that the C&D Fund will grow over time, particularly so with the proper use of reinsurance to protect the C&D Fund.

Ownership of the growing fund is an important governance issue, and there are different ways to deal it. Our recommendation is to use a form of rolling ownership based on annual premium contributions.

For example, if program member A contributes 25% of the total C&D Fund premium in year 1, Program member A is entitled to 25% of the equity balance at the end of year 1. This equity belongs to program member A but does not vest for three years and so cannot be taken out of the fund until the beginning of the fourth year. This is intended to encourage continuous membership and growth of the C&D Fund. The component of profit earned during year 1 is allocated to a surplus account for each member for record keeping purposes and is carried forward to year 2. At the beginning of year 2 the equity weightings are recalculated based on premium contributions for year 2. In the example given below the equity weighting for program member A for year 2 is 26.83%. The cycle then repeats itself annually.

Program Member	Underwriting Year	Total Fund Premium	Member Premium	Weighting By Premium	Underwiting Profit After Reinsurance Recoveries	Weighted Underwriting Profit	In Trust Current Year	In Trust Cumulative	Vested	Cumulative Vested
A	Year 1	200,000	50,000	25.00%	100,000	25,000	25,000	25,000	-	-
	Year 2	205,000	55,000	26.83%	110,000	29,512	29,512	54,512	-	-
	Year 3	202,000	52,000	25.74%	90,000	23,168	23,168	77,681	-	-
	Year 4	165,000	41,000	24.85%	100,000	24,848	24,848	102,529	25,000	25,000
	Year 5	185,000	45,000	24.32%	75,000	18,243	18,243	120,772	29,512	54,512
	Year 6	195,000	48,000	24.62%	85,000	20,923	20,923	141,695	23,168	77,681
	Year 7	198,000	53,000	26.77%	95,000	25,429	25,429	167,125	24,848	102,529
	Year 8	190,000	50,000	26.32%	100,000	26,316	26,316	193,440	18,243	120,772

Governance, Moral Hazard And Conflict of Interest

The Fund is essentially a small insurance company that will have to be managed by its members at the equivalent of board level. The members will have to establish protocols regarding moral hazard and conflicts of interest.

After establishing governance protocol the mechanics of operating the Fund can be routinely managed by a third party administrator. The third party administrator then becomes responsible for general administration of the Fund including accounting, banking, actuarial, reinsurance and risk management, and claims management.

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