Index


Abandonment option, 97
Abbado, 197–198
Abbreviations, 827–828
Aborted bid insurance, 771
Above-market coupon, 317
Absolute risk, 11
Accelerated quota shares, synthetic, 521
Accidents, types of, 27
Accountability, 574
Accounting for true sale, 349
Accounting fraud, 565
Accounting issues, 274, 281, 662–671
Accounting period, 83
Accounting reserves, 123, 575
Accounting rules, 19, 78
Accruing accounting method, 80, 82
Accrual notes, 313
ACE USA PowerProducts, Inc., 605
Acquisitions, 28–29, 36, 100, 185–186, 208–210, 296
Active management, arbitrage CDO, 385–386
Actuarially fair premium, 151
Actual per-period cash flows, 82
Adhesion, insurance contracts, 149
Adjusted present value (APV) rule, 93–94
Administrative costs and expenses, 153
Advance payments, 480–482
Advance payment supply bonds (APSBs), 214–217, 481
Adverse development cover (ADC), 559–560, 570–571
Adverse liquidity shock, 363
Adverse market events, 24, 29
Adverse selection:
characteristics of, 15, 73, 162–168, 187, 384, 574–575
Advisory agent, 281
Affirmative warranty, 147
Agency costs, 44–45, 56–57, 60, 93, 134, 278, 300, 453–455, 538, 544
AGF, 702, 704, 708
Aggregate capital shocks, 611
Aggregate excess of loss (XOL) reinsurance treaties, 192–195, 570
Aggregate ILWs, 607
Aggregate retention protection, 613–614
Agricore United, 594
Agricultural projects, 447
Agrupamientos complementares de empresas (ACEs), 459
AIG Risk Finance, 572–573, 592, 595, 597
Airbus Industrie, 99–100
Airline Mutual Insurance (AMI), 542
Akerlof, George, 63–64, 66
Aleatory insurance contracts, 139, 143, 145–146
All-equity firms, leveraging and, 41–45, 55–56, 58
Allianz, 193, 434, 615–617, 730
Allied-Lyons, 336–337
Alpha test, 450
Alpha Wind, 730
Alternative risk transfer (ART), 70, 138, 487, 490, 530, 533, 545, 553, 577, 612, 773–774
Amadeus Funding, 397–398, 401
Ambac Assurance Corp., 206, 328
Ambiguity rule, 149
American International Group (AIG), 217–222, 435, 439, 569–570, 591, 730
American International Specialty Lines Insurance Co., 569
American Skandia Life Assurance Corp., 501
American-style options, 246, 322, 330
Amortization/amortization period, 78, 315, 362, 385, 440
Am Re, 735–736
Analysts, functions of, 114
Anchorage Finance, 327
Book ROI, 83
Book-to-market ratio, 88–89
Borrowing conditions, 73, 300
Boulez, 197–198
Bowie, David, 473
Bowie Bond, 472
Brady bond, 386
Brazilian real, 36
Break-even return, 83
British Bankers’ Association (BBA), 29
British currency, pound and sterling, 25
Broker(s), 150, 171–172
Broker/dealers, 249, 793–797
Browning-Ferris Industries Corp., 802
Build-operate-transfer (BOT), defined, 446
Bull floaters, 310
Bundesbank, 802–803
Bundle of assets, 92
Bundling exposures, 747
Business continuity risks, 28–29
Business cycle, 610
Business failure, financial distress costs, 31, 46–48
Business insurance, types of, 169
Business interruption insurance, 170, 506, 513–515, 578, 581, 584, 603–604
Business risks, 3, 30
Business units, 3, 5–6
Cactus Funds, 478
Callable debt, 9
Callable notes, 362, 374
Call options, 18, 48, 235–246, 278, 280, 301, 317, 520
Cal Quake (Swiss Re), 730
Canadian Imperial Bank of Commerce (CIBC), 353
Capital asset pricing model (CAPM), 88–90, 821–822, 824
Capital at risk (CaR), 805, 807, 809–812
Capital budgeting, 3, 34, 76, 81, 86–100, 133, 820–826
Capital Dynamics, 433
Capital gains, 43
Capital-intensive projects, 277
Capitalization method of reserve management, 175
Capital markets, 44, 46, 109, 130, 183–184, 303
Capital-protected notes (CPNs), 423–428, 430, 436, 493
Capital-rich firms, risk transfer and, 109
Capped bull note, 306
Captives, 276, 527–540, 546
CAREVA (capital-at-risk-adjusted economic value added), 824
Carryforwards, 110
Case studies:
credit derivatives, 672–688
enterprise risk management, United Grain Growers, 744–763
insurance securitization, trend review (2004), 698–743
insurance under Basel Accord, 652–661
patent law, 621–638
project finance collateralized debt obligations, 689–697
representations and warranties insurance, 764–776
special purpose entities (SPEs), 662–666
weather derivatives vs. insurance, 639–652
Cash, generally:
distributions, 8–9, 284
inflow, 24, 45, 59, 85, 360–361, 365
outflow, 85–86, 360, 365
reserve, 356
settlement, 228–229, 252
Cash arbitrage CDO, 383–389
Cash CDOs, 375, 391, 410
Cash collateral account (CCA), 356–358, 366, 378, 384, 427
Cash flow, 3–4, 39, 78, 134, 185, 195, 384–385, 538, 691
Cash flow return on investment (CFROI), 106–107
Cash flow waterfalls, 282, 286, 360–362, 369, 392, 431, 438–439, 442
Cash-for-stock purchases, 339
Cash-or-nothing digital option, 241–242
Cash-settled CDS, 252, 255
Cash-settled swap transactions, 482–483
Casualty insurance, 140, 143, 203, 219
Catastrophe Equity Put (CatEPut), 328–330, 332
Catastrophic excess of loss (XOL), 194, 497–498, 529
Catastrophic insurance futures contracts (Cats), 516–519
Catastrophic insurance-linked note (ILN), 615
Catastrophic loss, 111, 184–185, 194, 325–326, 332, 494. See also Cat bonds
Constant proportional portfolio insurance (CPPI), 427–429
Contingency agreements, 529
Contingent capital, 70, 73, 320–339, 615
Contingent cover, 609–617
Contingent debt, 504, 565–566, 572
Contingent risk capital, 816
Contingent risk finance, 333
Contingent risk transfer, 321
Continuous conveyance, 373
Contract of indemnity, 140
Contractors, project finance, 446–447
Contracts, 35, 451. See also Insurance contracts
Conversions, 278, 299
Convertible debt, 67, 323
Convertible, 298–302, 338
Convex corporate tax schedule, 110
Conveyance, 478
Cookie jar problems, 131–132, 574
Cooperative insurance companies, 170
Core risks, 30–31, 114
Corporate finance principles, 78
Corporate finance theory, 41
Corporate financing decisions, adverse selection costs, 62–75
Corporate insiders, 65
Corporate law, 45
Corporate risk securitizations: business interruption insurance, 513–515
credit default insurance, 508–511
earthquakes/theme parks, 503–507
implications of, 470
residual value protection, 507–508
transmission and distribution (T&D) asset insurance, 511–512, 572
Corpoven Accrogas, 465
Corridor notes, 313
Cost-minimizing corporations, 156
Cost of capital, 62, 79, 89, 103, 106, 126, 321, 404–405
Counterparties, 303, 354, 404
Country club shares, 13
Coupon rate, 127, 129, 357
Covenants, 54, 299–300, 453–454
Coverage tests, collateralized debt obligations, 382–383
Credibility, significance of, 54, 131–132
Creditanstalt, 397
Credit default, 359–360
Credit default insurance, 508–511
Credit default swap (CDS), 252, 359, 365, 391, 393, 461, 549, 675–677. See also Single-name credit default swaps (CDSs)
Credit derivatives:
asset default swaps, 260
characteristics of, 71, 365, 375, 381, 404–405, 674–675
credit exposure, 687–688
credit-linked notes, 263–265
documentation, 685–686
equity default swaps, 260–262 funded, 677–681
growth in, 672–673
insurance v/s., 683–686
misuse of, 681–683, 686
nonfunded, 675–677, 685
portfolio credit default swaps, 257–260
protection sellers, 249–250
risk management and, 673–674
scope of activity, 247–249
single-name credit default swaps, 251–257
total return swaps, 262–263
Credit insurance, 71, 117, 199–213, 367
Credit-linked notes (CLNs), 263–265, 381, 393, 395, 406–407, 461, 556, 675, 677–678, 681–682
Creditors, 16, 45, 71–72, 111
Creditor-writers, 54
Credit protection, 72, 118–120, 363, 375, 381, 410, 460
Credit protection sellers, 248–250, 252, 256–257
Credit quality, 71
Credit rating, 11, 36, 70, 207, 274, 276, 287, 291, 360
Credit reinsurance, 289, 367
Credit spreads, 677
Credit Suisse, 479
Credit Suisse First Boston (CSFB), 217, 219–220, 434, 513, 696, 735, 737
Creditworthiness, 36, 205, 299, 319
Credit wraps, 331–332
Crime and fidelity insurance, 170
Crisis management, 48
Cross-border activities, 115
Cross-currency swaps, 530
Cumulative present value, 102
Cumulative probability, 49
Currency derivatives, 366
Currency exposure, 300, 316
Currency-indexed debt, 316–317
Currency risk, 316, 354, 366, 404, 441–442
Currency swaps, 231–232
Current assets, 52, 61
Custodian(s), functions of, 281, 346
Customer(s):
  acquisitions, 28–29
  information, risk transfer and, 36
  loss risk, 28–29
  retention, 28–29
Cutty Sark, 148
Cyclical industries, 98
Daimler-Benz, 802
Deal documents, execution of, 286
Dealers, 35–36, 425. See also Broker/dealers
Dean Witter Reynolds, 637
Debt, 8–9, 15–16, 40–46, 48–55, 63–67, 71, 73, 79, 82, 93, 117, 119–121, 126, 133, 184, 274, 299, 572
Debt-for-tax treatment, 297
Debt service coverage ratio (DSCR), 361, 440, 459–460, 470
Debt-to-equity ratio, 296, 760
Decision rules, 3, 54
Deconsolidation, 298
Deductibles, 158–161, 525, 529, 601
Deepening insolvency, 50–51
Default risk, 9, 291–293
Default-risky debt, 119–121
Defeasance, 493
Deferment option, 96–97, 99
Deferred taxes, 110
Delegated monitoring/monitors, 71–72
Delta, 24, 238
Denmark, equalization reserves, 177–178
Dental insurance, 158
Depfa Bank PLC, 460–461, 696
Depreciation, 21, 78, 133
Depressed-price asset sales, 47
Derivatives Policy Group (DPG), 795–796
Detachable gold warrant, 318
Deutsche Bank, 433, 435, 802–803
Development finance projects, 448
Diff swap, 233
Digital call options, 314
Digital credit default swaps, 252
Digital option, 241
Direct equity, 355
Direct writing, insurance companies, 172
Directors and officers (D&O) insurance, 170, 578–581, 611
Disappearing deductibles, 160
Disclaimer, 686
Disclosure, 566, 574, 576, 670
Discounted cash flow (DCF), 82–83, 91
Discounted expected net cash flows, 86
Discounted net cash flows, 83
Discounted present value, 52
Discounting, pretax/posttax, 92
Discount rate, 24, 42, 90–91, 127
Distress costs, optimal leverage and, 56–57
Diversifiable risk, 37
Diversification, benefits of, 37, 192
Diversified payment rights (DPRs), 467
Diversified Strategies, 434
Dividend enhance convertible stock (DECS), 338
Dividend(s), 8, 10, 19, 40–41, 43, 45, 51, 66, 74–75, 302, 328
DLJ, as information resource, 735, 737
Documentation, 404, 410, 647–648, 685–686
Domestic Re, 730
Double securitization, 436
Double-trigger ART, 599
Down-and-in put option, 240–241
Down-and-out call option, 240
Downgrade risk, 25–26
Dresdner Bank, 802
Drexel Burnham Lambert Group, Inc., 24
Dual currency bond, 316
Dual-indexed FRNs, 314–315
Dual-trigger insurance, 607
Due diligence, 70, 147, 185, 197, 513
Earnings, 21, 78–79, 113–116, 185, 299, 575
Earnings before interest and taxes (EBIT), 85
Earnings before interest, taxes, depreciation, and amortization (EBITDA), 85, 470, 599, 603–604
Earnings per share (EPS), 78–79, 591
Earthquake bonds (SR), 495–496
Earthquake Fund Ltd. (Swiss Re), 495–496
Earthquakes, see Natural disasters
Econometrics, 91
Economic book capital, 104
Economic profit (EP), 103
Economic reserves, 123
Economic value added (EVA), 103–107, 823
EDS-CDS, 417–418
Eiffel 1, 457–458
Electric power production, 99
Electricité de France, 511–512, 707, 709, 711, 713, 726–727
Emerging markets, 386
Emerging Issues Task Force (EITF), 350, 663–664
Employee benefits insurance, 169
Employee Retirement Income Security Act (ERISA), 692
End users, defined, 36
Energy hazards, 28
Energy Insurance and Mutual Insurance, 542
Energy Investors Fund Funding, 696
Energy projects, 443, 447
Enterprise, Inc., 288–291, 324–325
Enterprise risk management (ERM), 744–764
Enterprise-wide risk management (EWRM), 527, 530, 577, 582, 591
Environmental hazards, 28
Environmental liability, 171, 569–570
Environmental perils, 28. See also Natural disasters
Environmental projects, 443
Equalization reserves, 177–178
Equal-weighted portfolios, 544
Equilibrium price, 64
Equity default obligation (EDO), 411–412
Equity default swap (EDS), 260–262, 415–417, 419, 545
Equity holder, conflict with debt holder, 53–55
Equity-linked notes, 304–308
Equity market neutral funds, 420
Equity risk, 13, 337, 399
Equity swaps, 308
Equity tranche, 355–343
Errors and omissions (E&O) insurance, 148, 169–170, 572–573
Escrow, 287
Essential public infrastructure capital (EPIC), 460–462, 696
Eurobonds, 429
Eurodollar, 231, 366, 442
Europe Interbank Offered Rate (EURIBOR), 434, 499, 513
European call options, 53, 239
European CDO, 386–387
European International Reinsurance Co. Ltd., 432
European ladder call option, 315
European Monetary System, 25
European put options, 53, 128
European Union (EU), 799
Eva Air, 538
EVA spread, 103–104, 107
Event-contingent surplus notes, 325
Event-driven funds, 421
Event risk, 299
Event triggers, 493–494
Excess of loss (XOL), generally, 328, 379, 397, 497, 520, 537, 550, 559–560, 591, 596, 613
Excess of loss (XOL) reinsurance treaties, 190–195
Excess spread, 356–358, 362, 378, 493
Exchangeable debt, 304–305
Exchange and Clearing House Organization (ECHO), 221
Exchange offer, 45
Exchange options, 245, 307
Exchange rate, 24–25, 115, 744
Exchange-traded catastrophic loss derivatives, 516–522
Exchange-traded contracts, 231
Exchange-traded derivatives, 521
Exercising an option, 141
Exotic options, 239–240, 431
Expectations, implications of, 77
Financial Accounting Standards Board (FASB):
Emerging Issues Task Force (EITF), 350, 663–664
Financial Accounting Statement 140 (FAS140), 350–351, 665
Financial Accounting Statement 133 (FAS133), 607
Interpretation No. 46 (FIN46R), 298, 353–354, 373–374, 380, 386, 446, 662–671
Financial assets, distinguished from financial capital, 8
Financial assets securitization investment trust (FASIT), 284
Financial capital:
基本 forms of, 8–9
capital structure, 11–13
financial assets compared with, 8
options theory and, 14–19
priority, 9–11
seniority, 9–11
structure of, 11–12
subordination, 9–11
terminology, 7–8
value of firm, generally, 13–14, 19
Financial distress, 46–48, 59, 73, 75, 93, 111, 133, 185, 299
Financial engineering, 377
Financial enhancement rating (FER), 220
Financial exchanges, 221–222
Financial flexibility, 130–131
Financial guaranties, 202–207. See also Guaran
ties; Guaranties
Financial Guaranty Insurance Co. (FGIC), 206
Financial mutual organization, 12–13
Financial risk(s), 23–27, 30, 35
Financial risk transfer services, 684
Financial Security Assurance, Inc. (FSA), 206
Financial slack, 73–74
Financial statements, components of, 349–350
Financial strength rating (FSR), 220
Financial surety bonds, 205
Financing decisions, empirical evidence, 67
Financing leg, 475
Finite quota share treaty, 561–562
Finite risk:
blended, 566–567
characteristics of, 73, 546–547, 550–554
contract dates, 555

Expected cash flow, 77, 94, 280, 590
Expected loss(es), 374, 542, 610, 666–667, 807
Expected market ROI, 83
Expected net cash flow, 83, 85–86, 100
Expected residual returns (ERRs), 666–667
Expected return(s), 3, 77, 80, 90–92
Expected value, 63
Experience account, 553
Expert systems, 164
Expiration date, 314
Export credit agencies, 448
Export receivables, 463, 466–467
Export-import banks, 448
Extendable notes (ENs), 362, 374
External credit, 117–118, 358–359, 447, 455
External debt, 73
External finance/financing, 65–67, 74
External risk transfer, 290, 349
Exxon, 29

Facilities planning and construction, 98
Factoring, 201–202
Factor loadings, 88–89
Factor risk premium, 88–89
Facultative reinsurance, 186–187, 189
Fad-sensitive industries, 98
Fair market value, financially distressed firms, 46–47
Fair value, 131
Fama/Jensen organizations, 12–13
Fannie Mae, 303, 368, 521
Farming industry, 99, 109, 730
Fashion-sensitive industries, 98
Feasibility studies, 449
Federal Deposit Insurance Corporation (FDIC), 213–214, 307, 653
Federal Energy and Power Corporation of America, 604
Federal Home Loan Bank, Dual Indexed Consolidated Bonds, 314
Federal Home Loan Bank System, 303
Federal Home Loan Mortgage Corporation (FHLMC), 368
Federal National Mortgage Association (FNMA, FannieMae), 303, 368, 521
Federal Reserve, 298, 301
Fidelity and surety insurance, 214
FIFA (Federation Internationale de Football Association), business interruption insurance, 513–515
example of, 547–550, 568–573
funded vs. unfunded, 556–558, 565–566
legitimate transactions, 563–573
multiyear contracts, 553
premiums, 578
principles of, 573–576
retroactive cover, 564–565, 568
prospective vs. retrospective policies, 554–556
structures, 550–563
termination provisions, 568
Fire insurance, 140–141, 150, 157, 159, 162, 166
Firm size, significance of, 88
FirstBoston, 370
First Energy, 604
First-loss exposure, 293
First-order condition, 55
Fitch, 382, 430, 439, 690, 710–711
Fixed coupon rates, 314
Fixed debt, 299
Fixed-for-floating interest rate swaps, 233
Fixed liabilities, 355
Fixed-rate:
assets, 371
coupon bond, 308–309, 316, 318
coupons, 366
debt, 310
Flashpoint UK Ltd., 217
Floating-rate:
debt, 371
financing, 310
interest, 233, 310, 312, 366, 371
loans, 27
Floating-rate note (FRN), 308–310, 416–417, 461
Flood insurance, 140
Flood-related loss, 598
Flows of funds, 11–12
Flows of securities issued, 12
Ford Motor Credit Corporation, 317
Forecasting, 85–86, 101–102
Foreign currency, 316–317
Foreign exchange (FX), generally:
depreciation, 300
forwards, 530, 795
options, 530
rate, 300
risk, 578, 795
swaps, 530
Formosa Re (Central Re), 698–699, 704, 706, 708, 710, 712, 723, 726, 731
For-profit corporations, 167
Forward contracts, 38, 109, 216, 226–230, 478, 530, 744
Forward delivery contracts, 228, 231
Forward-looking insurance rates, 610
Forward transactions, 226
Franchise deductibles, 160–161
Fraternity row, see Greeks
Fraud, 26, 50–51, 565, 655–656
Freddie Mac, 368, 508–511
Free cash flows, agency costs, 44–45, 51
Frontier Insurance Company, 571–572
Fronting credit protection provider, 400–401
Fronting insurer, single-parent captive with, 531, 542
Fronting reinsurer, 197
Fujiyama (Nissay Dowa), 702, 704, 706, 708, 731
Full consolidation, 349
Full indemnity contract, 140, 493–494
Full prefunded reinsurance program, 326
Fully funded SCDOs, 391–395
Fund-raising, 70–71, 449
Funded retention, 32–33, 122
Funded risk transfer, 38–39, 278
Funding gap, CDO, 386–387, 409
Funding risk management, 24, 539
Future cash flows, 7, 24, 106
Future flow securitization, 274, 281, 444, 462–473
Future free cash flows, 45
Future net cash flows, 5
Futures contracts, 38, 109, 230–231, 744
Gamma, 24
Gearing, defined, 424
Gemini Re, 615–617
General contractors, 205, 446
General Electric (GE), 103–104
General ledger, 86
General Motors, 524
General partners (GPs), 421–422
General partnerships, 8
Generally accepted accounting principles (GAAP), 350, 483, 564, 663, 666, 670–671
George Re, 497–498
Georgetown Re, 730
Gerling Credit Insurance Group (GCIG), 499–500
Gerling-Konzern Globale Rückversicherungs AG, 499
Gerling-Konzern Speziale Kreditversicherungs AG, 499
Global macro funds, 421
Global structured credit market, defined, 340
Go/no go decision, see Project selection methodologies
Going long, 36
Gold Eagle, 730
Golden Goal Finance Ltd., 513
Golden Goal transaction, 727–728, 731, 742
Gold forward purchase agreement, 229–230
Goldman Sachs, 734–737
Goldman Sachs Mitsui Marine Derivatives Products LP, 499, 508
Gold warrants, 318
Good faith, in insurance contracts, 146–148
Government agencies, project finance, 448
Government National Mortgage Association (GNMA), 368
Government-sponsored enterprises (GSEs), 303, 368–369
Grammercy Place Insurance Ltd., 507, 510, 730
Grantor trusts, 284
Great Bay Power Corp. (GBPC), 605
Greeks, 24, 237–238
Greenspan, Alan, 672
Gresham’s law, 64
Gross domestic product (GDP), 335, 598
Gross payoff, indemnity insurance, 141
Gross present value, 96
Growth firms, equity issues, 68
G-10 countries, 698
Guaranteed investment certificates (GICs), 291, 514
Guaranteed investment contracts (GICs), 291, 514
Guarantees, 256–257, 358, 430–433, 455, 482
Guaranties, 117–119, 211, 213–222
Guarantor, 72, 118, 120, 203, 358
Haircuts, debt securities, 794–797
Haitink, 197–198
Hedge funds, 249, 279, 374, 419–421, 424–426
Hedge-to-arrive contracts, 246
Hicks, John, 226
Hidden action, 155
Hidden information, 155
Higher-quality investments, 75
High-yield debt instruments, 291
HIH Casualty & General Insurance, 217–218
Hill, J. J., 298
Hiscox, 703, 705, 707, 709
Holdback, 355–357, 366, 383
Holding period return, 82–83
Holding periods, 421
Hollywood Funding, 217–220, 473
Homeowner’s insurance, 140–141, 150, 156–157, 159, 161
Honeywell, 577, 586
Hong Kong Securities Clearing Corporation, 221
Horace Mann Educators Corp., 330, 332
Horizontally layered reinsurance programs, 196–197
Hospital Insurance and Equity Protection Multiline Double-Trigger Program, 605–607
Household insurance, 169
Human hazards, 28
Hurdle rate, 3, 83, 90, 100, 102, 820–824
Hybrid debt-equity securities, 66
Hybrid financing, trust preferred stock (TruPS), 297, 301
Hybrid securities, 65, 295–296. See also Structured synthetic hybrids
I/C (interest coverage) ratio, 383
Idiosyncratic risk, 35, 37, 92–93, 110, 113
IFC Latin America and Asia Loan Trust, 696
Illiquid options, 431
In-the-money options, 141, 242, 305–306, 317, 339, 352
Incurred but not reported (IBNR), 493, 538, 559
Indebtedness, leverage ratio and, 59
Indemnity contracts, 38, 140, 155. See also Insurance contracts
Index-amortizing notes (IAN), 315
Index-amortizing rate (IAR) swap, 315
Individual insurance, 169
Industrial production, 88
Industry loss warranties (ILWs), 607–608, 723, 728
Inflation, 88
Information technology (IT), 85, 447
Infrastructure, 85, 443, 447
Initial investment, 80
Input switching, 98–99
Insiders, corporate, 69–70
Insolvency, 27, 45–51, 213
Institutional investors, 11, 421, 426
INSTRAT, 331
Insurance, see specific types of insurance
adverse selection costs, 112–113, 162–168
ambiguity rule, 149
Basel II applications, 653–661
characteristics of, 642–643
claims, see Insurance claims
classification process, 163
coi-insurance, 161–162
companies, see Insurance companies
contracts, see Insurance contracts
credit derivatives compared with, 683–686
defined, 224
documentation, 647–648
financial guaranties and, 213
moral hazard, 156–158
policy, see Insurance policy limits
pools, 195
premiums, 34, 121
pricing, 150–156
risk and disclosure audit, 573
risk transfer strategies, 109, 113–114
securitization, see Insurance securitization
synthetic CDOs, 409–410
taxation, 651
underinvestment mitigation, 111–112
unfunded, 39
Insurance agent, functions of, 171
Insurance broker, functions of, 171, 534
Insurance claims, 139–140, 143, 154, 172, 183, 211, 213
Insurance companies, 71–72, 168–178, 283, 386, 447–448, 797–800
Insurance contracts, 22, 38, 137–150, 156–168, 554–555, 364, 685
Insurance industry, 63, 324
Insurance-linked notes (ILNs), 487–522, 615–617
Insurance policy limits, 156–157
Insurance securitization, 358, 698–743
Insurance Services Office (ISO), 516–519
Intangible assets, 7, 73, 131
Intangible residual claim, 13
Integrated risk and capital management:
adverse selection and corporate financing decisions, 62–75
capital budgeting, project selection, and performance evaluation, 76–107
leverage, 40–61
real and financial capital, 3–21
risk and risk management, 22–39
risk finance, 122–134
risk transfer, 108–121
Integrated risk management (IRM), 577
Intellectual property, 7, 443, 463, 638
Inter-American Development Bank, 448
Interactive growth option, 100
Interest, 9, 19, 125–126, 139–140, 145, 254, 256, 360, 362
Interest coverage (I/C), securitization process, 360–362, 383, 388
Interest rate, 38, 95, 209, 326, 354, 366
Interest-rate-indexed notes, 308–315
Interest rate risk, 24, 366, 369–371, 441, 795
Interest rate swaps, 139, 231–233, 308, 310, 315, 404
Internal borrowing, 539
Internal cash flow, 66
Internal credit enhancement (C/E), 355–358, 366–367, 447, 455, 470
Internal finance, 66
Internal rate of return (IRR), 83–84, 107
Internal Revenue Service (IRS), 532, 770
Internal risk transfer, 290
International Accounting Standards Board (IASB), SIC-12, 671
International Air Transport Association, 542
International Finance Corporation (IFC), 448, 457, 696
International Monetary Fund (IMF), 448, 687
International Organisation of Securities Commissions (IOSCO), 797
Internet commerce, 28–29
Interpolis Re, 502
In-the-money options, 141
Intrinsic value, 52, 237, 241, 315
Inverse floating-rate notes (FRNs), 310–312
Investment(s), influential factors, 6, 60, 74, 88, 96, 106, 538
Investment banks, as collateral manager, 386
Investment risk, 182–183, 279, 551
Investment trust, 284
Investor(s), 82, 279, 283, 447
Iron Mountain Copper Mine, 569
Issuer(s), 270, 281, 298
IT Corp., 569–570
Japan, equalization reserves, 177
Jardine Lloyd Thompson (JLT), 220
J-curve, 422, 431, 434
JP Morgan:
  Broad Index Secured Trust Offering (BISTRO), 396
  investments, generally, 434
JPMorgan Chase (JPMC), 215–216, 479–481, 483–484
Junior creditors, 16, 71–72
Junior debenture, 297
Junior debt, 10, 18, 296, 333
Junior tranche, 11
Junio, 730
Kelvin, 703, 705, 730
Key employee(s), overdependency, 28
Kidnap and ransom (K&R) insurance, 171
Kirchoffer, Art, 593
Knock-in option, 240–241
Knock-out option, 240
K3, 731
Kuwait Investment Authority, 802
Labor income, 88
Ladder bonds, 315
Ladder options, 243–244
LAE sharing, 192
Lane Financial (LFC), 491, 728–729, 735, 737
Large-line capacity, 184
Large-scale project financing, 283
Latent assets, 7, 73, 443, 456
Laurie-Walker, Alastair, 221
Law Debenture Trust Corp. (Channel Islands), Ltd., 220
Law firms, securitization process, 348
Lead underwriter, 169, 197
Lease bonds, 214
Least squares regression, 88
Leeson, Nick, 30
Legal fees, 47
Legal issues, structured finance, 281
Legal perils, 28
Legal risk, 26–27
Legislation:
  Commodity Exchange Act (CEA), 641–642
  Employee Retirement Income Security Act (ERISA), 692
  patent law, 621–624
  tax laws, 650–651
  Terrorism Risk Insurance Act of 2002 (TRIA), 584–585
U.S. Investment Company Act, 692
Lehman, 703, 705, 707, 709, 711, 723, 735–737
Lehman Re, 705
Lemons problem, 63–66, 72
Lenders, project finance, 447
Letters of credit (LOC or L/C), 132, 207–208, 210, 212–213, 325, 359, 363–364, 366, 373, 475, 484
Leverage/leveraging, 40–61, 82, 93–94, 132, 274, 425, 455
Leveraged buyouts (LBOs), 376
Leveraged firms, 36
Leverage ratio, 11, 41, 55–61, 67
Levered FRNs, 312
Liabilities, 24, 28, 37, 86, 270–271
Liability insurance, 169
Liability risk, 143, 546
Liberty Mutual, 216, 540
Life insurance, 169, 501–502
Life Insurance and Life Annuities-backed Charity Securities (LILACS), 728, 731
Liquidity risk, 24, 30, 359–360, 371, 401
Liquid marketable securities, 101
Liquid securities, 66
Liquid yield option notes (LYONs), 300–301
Liquidity support, securitization process, 354, 359–364, 373, 440–441
Litigation, 145, 220
Lloyd, Edward, 171
Lloyd’s, 169–171, 800
Loan(s):
  bank, 67–68
  default, 116, 118, 120
documentation, 404
  insurance, 121
  renewal, 71
  riskless, 53, 121
  short-term, 204
  unsecured senior, 71
  Loan-loss reserves, 334
Lockout periods, 421
Lockup tests, 361
London Clearing House, 221
London Stock Exchange, 221
Long call option, 18, 53
Long forward, 317
Long put option, 16, 157
Long/short funds, 421
Long stock position, 301
Lookback options, 243
Loss(es), generally:
  distribution, 290–294, 395–396
  equity put, 328
  insurance program, 325
  mitigation products (LMPs), 771–772
  portfolio transfer (LPT), 558–559, 569–571
  reserves, 132, 178, 183, 525–526
Low-risk debt, 65–66, 74
Low-risk securities, 66, 73
  McGarret transactions, 352–353
  Magma Copper Company, 318
  Magma copper-indexed notes, 318
  Mahonia Limited, 480–482
  Mahonia XII, 482–483
  Malpractice liability insurance, 154
  Man Glenwood Alternative Strategies I (MAST 1), 434–435
  Management buyouts, 296
  Managerial control, 12–13
  Managerial decisions, influential factors, 54
  Managerial risk aversion, mitigation of, 112
  Mandatory reinstatement, 567–568
  March, Michael, 221–222
  Margin calls, 222
  Marginal cash outflow, 86
  Marginal cost, 55
Marine insurance, 149, 169, 186
Marketable securities, risk finance, 125–126
Market capital structure, 39
“Market for Lemons, The” (Akerlof), 63–64, 66
Marketing, 210, 686
Market intelligence, 186
Market liquidity risk, 24–25
Market neutral investing, 420
Market return on investment (ROI), 82–83
Market risk, 23–24, 30, 96, 401, 465, 467, 791
Market timing, 421
Mark-to-market, 14, 19, 231
Markup, on insurance, 151
Marsh Ltd, 221, 528, 592, 734–736
Martinair Insurance, 538
MascoTech, 301
Massachusetts Mutual, 540
Master CDO, 409
Master swap agreement, 516, 647–648, 676
Master trust, 284, 344
Matched book, 35
Material adverse change (MAC) clauses, 132
Material risk transfer, 551–552
Maturity/maturity date, 9, 18, 20, 97, 127, 157, 237–239, 241–246, 286, 339, 361, 491
MBIA Insurance Company (MBIA), 206, 331–332, 731
MCI, 301
Mead Corp., 591
Mechanical hazards, 28
Mediterranean Re (AGF), 704, 708, 730
Medium-term notes (MTNs), 303, 699, 715, 742–743
Mellon Bank, 312
Mergers and acquisitions (M&A), 36, 100, 336, 443, 463, 470, 764
Merrill Lynch, 433, 461, 636–637, 735–736
Met-Max Penoles S.A. de C.V., 464–465
Metallgesellschaft AG (MG AG), 802
Mexican peso, 37
Mezzanine, generally:
  debt, 66
  financing, 296
  interest, 434, 438
  tranche, 405–407
MG Refining & Marketing (MGRM), 24, 802
Michelin, 334–335, 731
Multifactor models, expected asset returns, 88
Multilateral agencies, project finance, 448
Multiline insurance companies, 216
Multiline integrated risk transfer:
  benefits of, 582–585
  blended rs. integrated cover, 578–581
  cost savings, 585–586
  example of, 587–591
  features of, 581–582
  structures, examples of, 591–597
Multiline issuers, guaranties, 211–212, 221
Multiline programs, 612–613
Multinationals, 279, 532
Multiparent captives, 542
Multirisk insurance programs, 583
Multiseller asset-backed commercial paper conduit, 372
Multitrigger integrated risk management (IRM), 598–608
Multiyear coverage, 611–612
Munich-American Risk Partners, 591
Munich Re, 705, 707, 709
Municipal bonds, 207
Mutual insurance companies, 170, 526
Mutuals, 540–545
Namazu, 730
Namur Re SA, 499
National Association of Insurance Commissioners (NAIC), 645–647, 798
National Cat options, 518–519
National Indemnity, 571
National Provident Institution (NPI), 501–502
National Westminster Bank PLC, 378, 381
Natural disasters, economic impact of, 490, 493, 503, 606–608, 611
Natural gas prices, 99
Natural resource extraction, 98
Negative cash flow, 79
Negative net present value, 44
Negative stock prices, 67
NeHi (Vesta), 703, 705, 730
Net asset insurance, 807–808
Net asset value (NAV), 18, 429–430, 523, 525
Net cash flow:
  deficit, 66
  implications of, 5–6, 8, 12, 17, 74
  from operations, 101–102
  preloss financing and, 128
  surplus, 66
  volatility of, 111–112
Net earnings management, 115–116
Net operating cash flows, 59
Net operating income, 80–81
Net operating profits after taxes (NOPAT), 102–103
Net payoff, 16
Net present value (NPV), 3, 6, 24, 44, 48, 52–53, 111, 132, 281, 381, 453, 558, 813–814
Net present value (NPV) rule, in capital budgeting, 86–100
Net reinsurance premiums written (NRPW), 180, 182
Netting agreement, 26–27
Net working capital, 86
New drug approval process, 338
New equity issue, 786–787
New Hampshire Insurance, 218
New York:
fidelity and surety insurance, 214–215
guaranties, 214–217
State Insurance Department (NYID), 215, 644, 685
terrorist attack (9/11), 192–193
New York Mercantile Exchange (NYMEX), 222, 481
Nexus of contracts, 3–4
Nissay Dowa, 702, 704, 706, 708
No-claims bonus B-M system, 166
Nobel Prize winners (2001), 63
Noncapital assets, 4
Nonconvertible debt, 67
Noncore business risks, 114, 575
Noncore risks, 30–31, 112
Noncredit structured financing, 341
Nonfinancial corporations, 80, 249, 802
Nonfinancial risk, 35
Nonlife insurance products, 169
Nonprofit organizations, 13
Normal distribution, 163
Note(s) issue, short-term, 285. See also specific types of notes
Notional principal amount (NPA), 232–233
Notional principal contracts (NPCs), 648–649
Nth aggregate limit cover, 614–615

Off-balance-sheet items, 19, 81, 271, 789–791
Offer and acceptance principle, in insurance contract, 148
Offsetting contracts, 25
Offtake leg, 475
Oil Insurance Limited (OIL), 544–545
Oil price(s), 57, 578
OM Gruppen AB, 221
On-balance-sheet credit risks, 789
One-touch digital options, 242
Open corporations, 12–13
Operating cash flow, 13, 74
Operating scale option, alteration of, 98
Operational costs, captives, 537
Operational perils, 27, 29–30
Operational risk, 303, 654–657
Operation and maintenance risk, 452
Operator, project finance, 446
Opportunity costs, 86
Optimal capital structure, 40–41, 55–61, 66
Optimal exercise behavior, 60
Optimal leverage ratio, 59
Optimal risk capital, 817–818
Optimal risk packaging, 37
Optional limit acceleration, 614
Optional reinstatement, 613
Options, see specific types of options
capital-protected notes and, 431
characteristics of, 234–235, 478, 530
coupon-protected notes, 425–426
exercising, 236, 240
Greeks, 237–238
intrinsic value, 237, 244
put-call parity, 239
strike price, 235–237, 243–244
time theory, 14–19
time value, 237
type of, overview, 239–246
Option writer, functions of, 129
Oral contract formation, 26
Organization for Economic Cooperation and Development (OECD), 399–401
Oriental Land Co., 504–506, 702, 704, 706, 708
Original equipment manufacturer (OEM), 595, 596–597
Outperformance option, 245
Output purchasers, project finance, 447
Output switching, 99
Over-the-counter derivatives, 303, 795
Over-the-counter options, 795
Overhead expenditures, 85
Overinvestment, 74
Overpriced stock, 65
Overstructuring, 285
Ownership, title transfer, 286
Owner trusts, 284
Pacific Re, 734
Paid-in capital, 323, 325, 815–817, 826
Palm Capital (Swiss Re), 706, 708, 710, 712, 720–721, 724, 731
Palmer, Paul, 221
Parametric contracts, risk transfer, 38
Parametric Re (Tokio), 496–497, 515, 702, 704, 706, 708, 730
Parametric triggers, 494, 504
Parametric Units (Zurich Re), 703, 705, 707, 709
Parent/parental guarantees, 324–325, 355
Paribas Capital Markets, 313–314
Partially funded finite programs, 565–566, 572
Partial risk transfer, 552
Participation rate, 305, 424, 426
Partners Group, 430, 433
Partnership, equity in, 13
Pass-through certificates, 284
Pass-through mortgage-backed security, 368–369
Pass-through securities, 284
Patent law:
  case illustration, 625–630
  emergence of, 621–623
  examples of risk finance patents, 630–635
  financial patents, evolution of, 635–638
  patentability, 623–624
  treatment of, 443, 463, 473
Pay-fixed/receive-floating interest rate swap, 310
Pay-floating swap, 310
Payoffs, 8–9, 16–18, 141–142, 156–158, 239, 241–245
PCS options, 519–521
Pearl Holding Ltd., 432
Pecking order theory, 67–70, 73–74
Pedro Domecq Group, 336
Pegasus Gold Corporation, 318
Pension plans, 279, 421
Per-period cash flows, 73, 282
  See also Performance measurement, accounting metrics
Performance measurement, accounting metrics, 78–83, 107
Perils, types of, 27–28
Perpetual capital, 8
Perpetual preferred stock, 332
Personal income, 43
Personal insurance, 171
Personal taxation, 42–43
Pharmaceutical industry, 473
Philip Morris Credit Corporation, 316
Phoenix Quake Wind Ltd./Phoenix Quake Ltd./Phoenix Quake Wind II Ltd. (Swiss Re), 702, 704, 706, 708, 710, 712, 726, 731
Physical asset risks, 112
Physical perils, 28
Physically settled credit default swaps, 252, 256
Pine Street, 435
Pioneer Series (Swiss Re), 702–711, 713, 715–719, 722, 731
Planned risk retention, 31–32
Political perils, 28
Political risk, 404
Poor-quality goods, 63
Portfolio credit default swap (PCDS), 257–260
Portfolio diversification, see Diversification
Portfolio securitization, 458–460
Positive EVA spread, 104
Positive net cash flow, 46
Positive net earnings, 42
Positive net present value (NPV), 44, 48, 51, 60–61, 71, 111–112, 132–134
Postloss financing/funding, postloss funded retention, postloss funded risk capital, 33, 122, 128–130, 132, 324, 333
Postloss risk financing, 77, 122–126
Posttax discounting, 92
Power market protection, case illustrations, 604–606
Preferred equity redemption cumulative stock (PERCS), 301, 338
Preferred redeemable increased dividend equity securities (PRIDES), 301–302
Preferred stock, 8, 10, 67, 70, 296, 298, 321, 328, 333, 439
Preloss financing/funding, 33, 73, 133–134, 322, 549
Preloss funded retention, 127–128
Preloss funded risk capital, 324
Preloss risk finance, 77, 122–126, 276, 527
Premium(s), 34, 88–89, 121, 146, 150–155, 165, 175–176, 180, 182–185, 201, 208, 558
Premium-in-arrears insurance program, 214
Premium protection options, 609–612
Prepaids, 216, 226–227, 474–475, 479–480
Prepayment risk, 369–370
Present value, 5–6, 41–42, 45, 56–59, 83, 90, 228, 424. See also Adjusted present value (APV) rule; Net present value (NPV)
Presettlement risk, 25–26
Pretax discounting, 92
Price, 703, 705
Price risk, 303
Pricing strategies, insurance policies, 150–156, 166–168
Pricing theory, trend review, 728–729
Primary beneficiary (PB), 354, 446, 687, 669–671
Prime contractor, 446
Prime Edge Capital PLC, 433–435
PRIME (Munich Re), 703, 705, 707, 709, 730
Princess Private Equity Holding Ltd., 430–431
Principal exchange rate linked securities (PERLS), 316–317
Principal finance, 443, 456, 467–473
Private equity, 279. See also Private equity funds
Private equity funds, 419–423, 433
Private Equity Investment Notes (PEI Notes), 436, 438, 440
Private Finance Initiative (PFI), 460–461
Private placement, 131, 323, 328, 453
Pro rata temporis calculation method, unearned premium reserve, 177
Probability density function, 48
Production perils, 27–29
Product issuer, securitized, 343
Product liability, 34, 134, 148, 170, 524, 578, 581, 584, 596
Professional indemnity (PI) insurance, 170, 578, 581
Professional liability, 138, 294
Profitability, 78–81
Profit margin, 103
Profit maximization, 64, 167
Project advisers, functions of, 448–449
Project completion risk, 450–452
Project finance:
collateralized debt obligations (CDOs), 689–697
defined, 443
future flow securitization, 462–473
implications of, 785–786
phases of projects, 449–450
project loan securitization, 456–462
project risks, 450–452
securitization, 456–462
structured, benefits of, 452–456
structures of, 444–456
synthetic commodity-based, 473–484
types of projects, 443
Project managers, 281
Project risk, 90–91
Project selection methodologies, 76–77, 82–84, 94–107
Promissory warranty, 147
Property, insurable interest in, 138
Property Claim Services (PCS), 494–495, 607, 723
Property damage (PD) insurance, 170, 506, 578. See also Property insurance
Property insurance, 140, 143–144, 146, 157–159, 162, 169, 194, 203, 219
Proportional reinsurance treaties, 187–189
Proprietorship, 12
Prospective insurance, 142–145
Protected bull note, 306–307
Protected cell companies (PCCs), 523, 533–535
Pseudo-self-insurance, 525
PubCos, 469
Public investors, 11
Public Private Partnership (PPP), 460–461
Public relations management, 29
Public securities offerings, 74, 114
Pub securitization, 469
Punch Tavern Finance PLC, 470–471
Pure financial guaranties, 202–204
Pure premium, 151–153, 165, 176, 182
Pure risk, 744. See also Pure risk finance
Pure risk finance, 363, 523, 527
Put options, 16, 54, 97, 128, 157, 235–246, 278, 301, 319, 326, 328, 330, 359, 464
Puttable bonds, 300
Puttable debt, 9
Pylon Ltd. (Elec de Fr), 699, 707, 709, 711, 713, 726–727, 731
Qatar General Petroleum Corp. (QGPC), 466–467
Quadrant Capital, 220
Qualified SPE (QSPE), 351, 386
Quota share treaties (QSTs), 187–189, 332, 561–562
Rabobank, 502
Radian, 222
Rainbow bonds, 307–308
Rainbow options, 245
Rainer Marc Frey (RMF), 433
Ramp-up period, 287, 385, 429, 431, 438
Range notes, 313–314
Rate making, 137
Rate on line (ROL), insurance premiums, 150
Rating agencies, as information resource, 72, 114, 297, 347–348, 360, 362, 373, 382–383, 388–389, 423, 693, 697
Ratings arbitrage, 383
Rattle, 197–198
RBC, 731
Real assets, 4, 58–61
Real capital, 4–7, 78
Real estate development, 98
Real estate investment trusts (REITs), 12, 284, 497
Real estate mortgage investment conduit (REMIC), 284, 369
Real options, 7, 73. See also Real options strategic net present value
Real options strategic net present value, 94–97, 99
Rebound notes, 416–418
Receivables, 79, 285, 372–373
Recovery rates, 292, 382
Recovery right, credit default swaps, 254
Redemption, at par, 337
Redwood Capital, 731
Redwood II/III/IV (Lehman), 703, 705, 707, 709, 711, 723
Reference level, 429
Reference rate, 315
Reference set of securities, 729–734, 742–743
Refinancing, 456–457
Regression analysis, 88, 91
Regulated investment company, 284
Regulatory agencies, 348–349, 788–800
Regulatory issues, structured finance, 281
Reinstatement, 158, 195, 567–568
Reinsurers, capital regulations, 797–800
Reinvestment, 12, 78
Reinvestment period, 385–386, 439
Relative spread option, 245
Reliance I/II/III/IV, 330–331, 615, 730
Reliance National, 330–331
Rent-a-captives, 533–536
Renting the balance sheet, 184
Repackaging, 409, 420
Repos, 488
Representations and warranties (R&W) insurance, 765, 767–770, 772
Repurchase agreements (repos), 326
Reputation risk, 29, 36–37
Research and development (R&D) investment, 52–53, 88, 443
Reserve management, 442, 538. See also Reserve management at insurance companies
Reserve management at insurance companies, 174–175
Reserves, 73, 175, 362–363
Residential mortgage-backed securities (RMBSs), 376, 407
Residential property insurance, 165–166. See also Fire insurance; Homeowner’s insurance; Property insurance
Residential Re (USAA), 497, 699, 701, 703, 705, 707, 709, 711, 714–715, 730–731
Residual(s), 8, 11, 17–18, 75, 101, 103–104, 106, 507–508
Residual risk, 35
Restart decisions, 98
Restricted core capital, 298
Retail sales contracts, 226
Retained earnings, 21, 41, 123, 126, 133, 786
Retained risks, 288
Retention, in risk finance, 31, 122, 130–134
Retroactive cover, finite risk and, 564–565
Retroactive insurance contracts, 142–145
Retrocedant, 180, 184–185
Retrocession, 179–180, 183, 198, 324, 490–491, 499–501, 615
Retrocessionaire, 180, 184, 537
Retro premium payment bonds, 214
Retrospective aggregate loss (RAL), 560–561
Retrospective excess of loss (RAL), 559
Index

Retrospective insurance, 142–145
Return on assets (ROA), 80–81
Return on equity (ROE), 81–82, 381–382, 399
Return on investment (ROI), 80–81, 282
Revenue(s), 37, 59
Reverse cherry-picking, 72, 380
Reverse convertibles, 337–338
Reverse PERLS, 317
Revised International Capital Standards, see Basel Accord(s), Basel II
Rho, 24
Rhythms NetConnections, Inc., 45
Ring-fencing, 274–277, 569–571
Risk(s), see specific types of risk
aversion, 112
budget, 809–810
consolidation, 34
core vs. noncore, 30–31
defined, 22
diversification, 8
exposure, 25, 34–35, 37, 111, 543, 751–752
financial vs. nonfinancial, 23–30
identification, 584
management of, see Risk management;
Risk management alternatives
measurement, 657–658
mitigation, 54, 111
neutralization, 33–34, 109, 334
profile, 35, 62, 70, 163, 165
project vs. firm, 89–91
protection strategies, 38–39, 283
reduction strategies, 33–34, 541
reserve, 128
retentions, 31–33
securitization, defined, 487
sharing, 197, 447
swaps, 515–516
tolerance, 35, 186
transfer, see Risk transfer trigger, 132
Risk-adjusted discount rate, 86–87, 91
Risk-adjusted expected returns, 87, 92
Risk-adjusted return on capital (RAROC), 820–821, 823–824
Risk-adjusted returns, 3, 87, 92
Risk-averse management, 51
Risk capital, 3, 37, 77, 118, 184, 356, 801–826
Risk finance, 31–32, 122–134, 278, 349
Risk-free assets, 183
Risk-free interest rate, 26, 30, 87–88, 95, 117, 183
Riskless debt, 53, 65–66, 245
Riskless discounted net cash flow, 133
Riskless loans, 53, 121
Riskless note, 120
Riskless rate, 183
Riskless returns, 287
Risk management, 30, 73, 77, 79, 108–110, 155–156, 173, 303. See also specific types of risk
Risk management alternatives, 31–39
Risk Management Association (RMA), 29
Risk/return profiles, 678
Risk transfer, 34–39, 77, 108–121, 404
Risky assets, 72
Risky debt, 65
RLI Corporation, 328, 330
Rogue trader, 656
Rolled-over loans, 71
Rolls-Royce, 730
Rose Funding, 378–379, 381
Royal Bank of Canada (RBC), CLOCs, 333–335
Royal Bank of Canada Insurance Co., 222
Rule 144A, 682
Runoff solution, 276, 571–572
Saab, 730
Safir-Simpson scale, 494
St. Agatha Re (Hiscox), 703, 705, 707, 709, 731
St. Paul Companies/Georgetown Re, 497–498
St. Paul Fire and Marine, 216
Sakura Capital (Swiss Re), 705, 707, 709, 713, 720–721, 724
Sakura Ltd., 731
Sallie Mae, 303, 310, 312, 317
Sarbanes-Oxley provisions, 579
SBC Warburg, 339
Schuldscheine, 461
SCOR, 702, 704, 705–706, 708
SCS Alternative Fund (SCSAF), 429–430
Secondary market, 47, 116
Secured export notes (SENs), 463–465
Secured liabilities, 272
Secured liquidity notes, 362
Securities, see specific types of securities as capital, 3
design, structured finance, 284–285
issuance, 65–66, 68, 133
Securities and Exchange Commission (SEC), net capital rule, 794–797
Securitization:
collateralized debt obligations (CDOs), 368–374
consolidation, 349–354
credit enhancement, 354–359
as credit risk reinsurance, 366–368
currency risk, 366
defined, 340
interest rate, 366
liquidity support, 359–365
participants in, 341–349
process overview, 341–354
project loan, 456–462
technology, 217
Securitized product, 341
Security offering, 67
Sedgewick Lane Financial, 331
Seed capital, 296
Seismic, 730
Self-insurance, 524–526, 542
Semimonthly calculation method, 176
Senior basket swap, 258–259
Senior creditors, 16, 290
Senior debt, 15–16, 18, 66, 287, 296, 357, 366–367
Senior expenses, 282
Senior loans, unsecured, 71
Senior management, functions of, 47–48, 77
Sequoia Capital (Swiss Re), 707, 709, 713, 720–721, 724, 731
Servicer, securitization process, 346
Settlement date, 232, 520
Settlement process, financial guaranties, 204
Settlement risk, 25–26
Shareholder(s), 21, 77–78, 81, 100, 130, 575
Shareholder value added (SVA), 100–103, 105–106, 821, 825
Sharpe ratio, 822
Shock loss, 595
Short volatility position, 54
Short-term assets, 86
Shout options, 244–245
Sigma index, 607
Signal-to-noise ratio, risk transfer, 114–115
Signaling theories, adverse selection costs, 74
Silo-by-silo insurance, 578, 584
Silver Leaf, 435
Single-capital-structure products, 286, 302
Single-currency asset swaps, 366
Single-loan securitization, 457
Single-loss securitization, 457
Single-name credit default swaps (CDSs), 251–257
Single-parent captives, 527–533
Single-tranche capital-protected notes, 423–442
Single-tranche CDO, 384
Single-tranche SCDOs (STSCDOs), 405–406, 416
Single-trigger deals, 330
Small-batch production, 99
Snow, Temperature, or Rain Management (STORM) program, 591
Social perils, 27
Société Générale (SocGen), 222, 334–335, 735, 737
Soft call protection, 298
Soft capital, 324–325
Soft claims, 10
Solti, 197–198
Sonatrach oil-indexed notes, 318–319
South East Water Holdings Ltd. (SEWHL), 472
Sovereign debt, 386
Sovereign risk, 404
Specialist, risk transfer, 35–36
Special purpose company (SPC), 284, 344, 346
Special purpose entities (SPEs):
capital-protected notes (CPNs), 423–427, 430, 436
cat bonds, 493–494
characteristics of, 72, 217, 278, 283–284, 326–327, 335–360
classification of, 662–671
collateralized debt obligations, 375, 381, 389, 667, 678–679, 681–682
contingent ILNs, 615–616
credit risk securitizations, 487
finite risk, 563
FIN46R, 353–354, 662–671
insurance-linked notes (ILNs), 488
principal finance, 469, 473, 475, 477
project finance, 445–446, 461, 668–669
qualified (QSPE), 351, 386, 665
synthetic CDOs, 391–393, 396–397, 400, 406, 678–681
variable interests (VIs), 665–666, 670
Special purpose trust, 326
Special purpose vehicle (SPV), 283, 343
Specific risk transfer, 303
Speculators, 35
Spence, Michael, 63
Spot purchase, 227
Spread, in credit default swaps, 252, 257
Spread bond, 307–308
Spread loss treaty (SLT), 562–563
Spread risk, 25
SPV Mutual Securitisation PLC, 501
ST-CDO², 407–409
Stand-alone derivatives, 586
Stand-alone projects, 82
Standard & Poor’s 500 Indexed Subordinated Note (SPIN), 307
Standard & Poor’s Risk Solutions, 693
Standard & Poor’s (S&P):
as information resource, 219–220, 306, 327, 382, 439, 606, 690, 695
rating, 710–711
Start-up expenses, 443
Statistical inference, 541
Stauffer Management Co., 569–570
Step-up bonds, 314
Stern Stewart & Company, 104
Sticky dividend policies, 66
Stiglitz, Joseph, 63
Stock Exchange of Singapore, 221
Stockholder wealth, 55
Stock Index Growth Notes (SIGNs), 306
Stock insurance companies, 170
Stock investments, see specific types of stock
Stock prices, influential factors, 75
Stock repurchase, 44–45, 51, 67
Storm and hail insurance, 178
Straddles, 315
Straight deductibles, 159–160
Strategic opportunities, 77
Strike price, 18, 48, 52, 97, 128, 314, 317, 321–322, 330
Structured corporate securities, see Convertibles; Hybrid securities; Structured notes
Structured debt, 278
Structured finance:
cash collateralized debt obligations, 375–389
characteristics of, generally, 70, 72
collateralized debt obligations (CDOs), 376
contingent capital, 320–339
convertibles, 295–302
finance, project and principal, 443–484
hedge funds, securitizing, 419–442
hybrids, 295–302
private equity funds, securitizing, 419–442
securitization, 340–374
structured notes, 302–319
structured synthetic hybrids, 411–418
structuring process, 269–294
synthetic collateralized debt obligations, 390–410
Structured financial solutions, types of, 269–279
Structured financing, 452–453
Structured insurance, alternative risk transfer:
captives, 527–540, 549
contingent cover, 609–618
dual-trigger insurance, 608
finite risk, 546–576
insurance-linked notes, 487–522
multiline integrated risk transfer, 577–598
mutltitrigger structures, 577, 598–608
mutuals, 540–549
Structured notes, 302–319
Structured synthetic hybrids, 412, 414–418
Structuring agent, 282–283, 284, 286, 347, 448–449
Structuring process:
components of, 280
economic motivation, 280–281
enhancements, credit and liquidity, 286
execution, 286
institutional features, design of, 283–284
investor interest, 283
preliminary cash flow model, 281, 286
ramp-up, 286
securities, design of, 284–286
structuring agent, appointment of, 282–283
subordination, 286–294
target ratings, 286
tranching, 286–294
Studio Re (Vivendi), 506, 703, 705, 707, 709, 731
Suboptimal investment program, 134
Suboptimal leverage ratio, 59
Subordinated basket swap, 258
Subordinated creditors, 289
Subordinated debenture, 297
Subordinated debt, 11, 16, 19, 66, 70, 296, 321, 332, 357, 359, 366–367, 371, 386
Suboptimal investment program, 134
Suboptimal leverage ratio, 59
Subordinated basket swap, 258
Subordinated creditors, 289
Subordinated debenture, 297
Subordinated debt, 11, 16, 19, 66, 70, 296, 321, 332, 357, 359, 366–367, 371, 386
Subordinated expenses, 282
Subordination, 9–10, 72, 286–294
Subrogation, 149–150, 203
Subsidiaries, ring-fencing assets, 274
Sub-trust, 328
Sun Microsystems, 591
Sunk costs, 81, 86
Super-senior CDS, 396–399
Supplier(s), 70, 447, 595, 597–598
Supply and demand, 285
Supply chain, 28–29
Surety bonds, 204, 208, 210, 213–217
Surplus, defined, 184
Surplus notes, contingent, 325–327
Surplus share treaties (SSTs), 189
SVG Diamond Holdings PLC, 435–442
Swap dealer, 365, 401, 490, 426, 529
Swaps, 38, 72, 109, 139, 216, 231–234, 444, 478, 515–516, 530, 744. See also specific types of swaps
Swiss Exchange, 222
Swiss franc, 36, 153–154, 316
Switching option, 98–100
Switching trigger, 599
Sydney Futures Exchange, 221
Symmetric information, 46, 62, 109, 153, 779
Syndicates, defined, 12–13
Syndication, reinsurance programs, 197–198
Synthetic, defined, 287
Time value, 237
Timing risk, 183, 551
Title transfer, 287
Tokio Marine, 496–497, 515–516, 702, 704, 706, 708, 730
Tokyo Disneyland, 503–506
Total return swap (TRS), 262–263, 353, 675–677
Toyota Motor Credit Corporation (TMCC),
residual value ILNs, 507–510
Trade credit insurance, 79, 199–202
Trade credit receivables, 373
Trade credit retrocession, 499–501
Trade date, 226
Trade-off theory, 40–41, 55–56, 66, 68
TradePoint, Virt-x, 222
Trade secret law, 638
Trading level, 429
Traditional QST, 561
Traditional risk transfer:
credit derivatives, 247–265
credit insurance, 199–213
credit-linked notes, 247–265
derivatives, 223–246
guaranties, 213–222
insurance, 137–178
reinsurance, 179–198
Transaction costs, 58, 109
Transcational insurance products (TIPs), 765–767, 772–776
Transferee, securitization process, 343
Transferor, securitization program, 342–343, 355
Transmission and distribution (T&D) asset insurance, 511–512
Transparency, 274, 539, 574, 687
Travelers Casualty & Surety, 216
Treasuries, 73, 326, 399–400, 424–425, 427–428, 488
Treaty reinsurance, 186–187
Trigger events, credit default swaps, 254–255
Trinity I/Trinity II, 730
Trinom Ltd. (Zurich Re), 703, 705, 707, 709, 731
Trombone convertibles, 336–337
True sale, 349–350, 403, 478–479
Trust collateral accounts, 507–508
Trustee, securitization process, 281, 345–346, 357, 363
Trust preferred stock (TruPS), 279, 297–298, 301, 338, 388
Trusts, collateral held in, 39
Turner & Newall, 570–571
Uberimae fidei, 146
Uncertainty, 96–97, 213
Undepreciated assets, 80–81
Underlying assets, 97, 157, 227–228, 235, 239, 286–287
Underlying collateral, 361, 365, 367, 370, 374
Underpricing, 75
Underwriter(s), 283, 345, 347
Unearned premium reserve (UPR), 176–177, 183, 185
Unfunded finite programs, 565–566
Unfunded retention, 32–33, 122, 127, 130
Unfunded risk finance, 572
Unfunded risk transfer solution, 39
Unilateral insurance contracts, 149
Union Carbide, 591
United Grain Growers (UGG), 594
United States Automobile Association (USAA), Residential Re, 497, 699, 701, 703, 705, 707, 709, 711, 714–715
U.S. Commercial Fire Rating Schedule, 166
U.S. dollar, 316–317, 442
U.S. Export-Import (EXIM) Bank, 465
U.S. Investment Company Act, 692
U.S. Overseas Private Investment Corporation (OPIC), 448
United States Patent and Trademark Office, 622–623
Universal Studios, 506–507
Unplanned risk retention, 32
Unprotected bull note, 305
Unsecured debt, 73, 276, 278
Unsecured loans, 71
Unsecured securities, 11, 70, 280
Up/down B-M (bonus-malus) system, 166
Valdez oil disaster, 29
Valuation, 29, 272
Value at risk (VaR), 804, 814
Value-based management (VBM), defined, 77
Valued contract, 140–142
Variable interest entities (VIEs), 353–354, 386, 436, 446, 666–670
Variable interests (VIs), 665–666, 670
Variable trigger, 599
Vega, 24, 238
Venture capital, 277–278
Vertically layered XOL reinsurance program, 191–192, 195–197
Vertical spread, 520–521
Vesta, 703, 705
Virt-x, 222
Vita Capital (Swiss Re), 502, 698, 707, 709, 713, 727, 731
Vivendi Universal, 506–507, 703, 705, 707, 709
Volatile demand production, 99
Volatility, 24–25, 53–54, 97, 114, 134, 167, 185, 195

Warrants, 299, 318, 323, 352
Warranty, 146–147, 219–220
Waste Management, 301
Wauters, Diego, 221
Wealth creation and maximization strategies, 100–101
Weather derivatives, 641–651
Weather risk, case illustration, 756–758
Weighted average cost of capital (WACC), 3, 40, 59, 80, 83–84, 89–93, 103, 107, 272, 276, 289, 303, 317, 380–381, 404, 457, 523, 590, 781–784, 822–824
Weighted average rating factor (WARF), 382
West Landesbank, 482–484
West LB, 730
Westdeutsche Landesbank, 222
Western Capital, 730
Whipsaw rules, 650
Whole asset securitization, 404
Whole business securitization, 281, 467, 470, 472
Willis Risk Solutions, 755–756, 761–762
WinCat coupons, 498
Wind Class (Swiss Re), 703, 705, 707, 709, 724, 730
Winterthur (Credit Suisse), 335, 730
Winterthur Hail bonds, 498
Woo, Gordon, 727, 742
Woolwich, 502
Worker’s compensation, 214, 506
Working capital, 78, 86, 125, 539, 561
World Bank, 448
WorldCom, 672
Wraps, 208, 210–211, 358
Writing insurance, risks of, 182–183
Writing options, 301

XL Capital, 435, 586–591
XL Mid-Ocean, 730

Year-end gross asset value, 288
Yen, U.S. dollar exchange rate, 317
Yield, convertible bonds, 299
Yield curve, 96, 310, 313

Zero coupon, generally:
  bonds, 306–307, 314
debr, 358
senior debt, 15
subordinated debt, 17
Treasuries, 427

Zero net supply assets, 229, 231
Zürich Corporate Solutions (ZCS), 572, 592–596, 606–608
Zürich Financial Services Group, 222, 528, 591–592, 606
Zurich Re, 703, 705, 707, 709, 727, 735, 737