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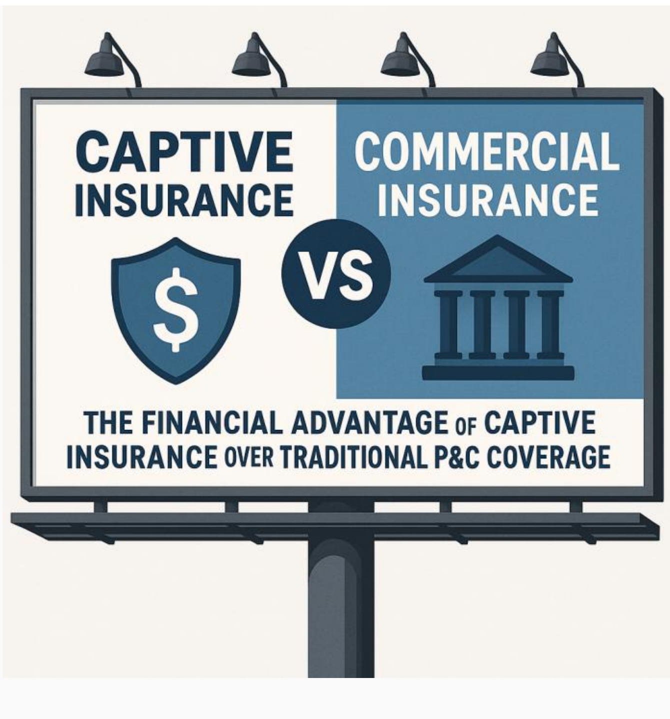
The Financial Advantage of Captive Insurance Over Traditional P&C Coverage



By Joseph W Tucciarone, CEO National Network of Accountants

For decades, business owners have turned to commercial property and casualty (P&C) insurance carriers as their default risk-management solution. These policies provide security but come with rising premiums, shrinking coverage, and limited flexibility.

In today's climate—marked by inflation, unpredictable risks, and a hardened insurance market—more companies are exploring an alternative: forming their own captive insurance company. By shifting from being just an insurance buyer to also becoming an insurance owner, businesses gain control, stability, and the ability to transform insurance costs into a financial advantage.

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1. Turning a Cost Center Into a Profit Center

With commercial P&C insurance, premiums are paid year after year with little chance of return unless a claim is filed. Even then, one or two claims often trigger higher future premiums or reduced coverage. In most cases, premiums are simply sunk costs.

Captives change that dynamic. When a company owns a captive, premiums paid become retained capital. If claims are low, underwriting profits remain in the captive and can be invested, compounding over time. Instead of enriching outside shareholders, the business keeps the financial benefit.

For example, a company paying $2 million annually in premiums spends $20 million over 10 years—closer to $40 million when factoring lost investment opportunity. With a captive, those same dollars fund the company's own insurance vehicle, converting expenses into assets.

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2. Stability in a Volatile Market

The commercial insurance marketplace is cyclical. After natural disasters, pandemics, or industry losses, rates spike across the board—even for businesses with clean claims histories. Exclusions increase, deductibles rise, and terms tighten.

Captives insulate businesses from this volatility. Premiums are set according to the company's actual risk profile, not industry averages. While reinsurance is still needed for catastrophic protection, day-to-day pricing and coverage terms are under company control. This stability provides executives the ability to budget long-term without being at the mercy of market swings.

3. Tailored Coverage for Real Business Needs

Commercial carriers often deliver one-size-fits-all policies that leave critical gaps. Emerging risks such as cyber liability, supply chain disruption, or reputational damage are frequently excluded or inadequately covered.

A captive can be designed to insure these exact exposures. By tailoring policies to the company's needs, businesses achieve broader and more relevant protection. For example, during COVID-19 many firms learned their business interruption policies excluded pandemic-related losses. A well-structured captive could have covered such risks, ensuring continuity when it mattered most.

4. Tax Efficiency and Cash Flow Advantages

Captives also offer potential tax benefits. Under U.S. tax law—including Section 831(b) for small insurance companies—premiums paid to the captive may be deductible as a business expense, while the captive may receive favorable tax treatment on underwriting income if structured properly.

Beyond tax efficiency, captives create cash-flow flexibility. Instead of premiums leaving the business entirely, they remain in the captive and may be invested or loaned back to the parent company under regulatory rules. This allows businesses to unlock liquidity in ways unavailable with traditional carriers.

5. Alignment of Interests and Better Risk Management

With a captive, the insured and the insurer are essentially the same entity. This alignment incentivizes proactive risk management. Companies with captives tend to invest more in safety programs, loss prevention, and claims oversight because every dollar saved benefits them directly.

The result is not only fewer claims but also stronger long-term financial health and operational resilience. Captives cultivate a culture where risk management is not just compliance—it is profit protection.

Conclusion

Commercial P&C insurance remains necessary in many contexts, but its limitations are increasingly clear: rising costs, reduced coverage, and little financial return. Captive insurance offers a compelling alternative, turning premiums into retained capital, stabilizing costs, tailoring coverage, providing tax and cash-flow advantages, and aligning incentives for better risk management.

For companies seeking greater control and long-term financial strength, the shift from insurance buyer to insurance owner is more than risk management—it's a strategic move toward lasting value.

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