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CASE STUDY

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Client Challenge

We were approached by the owner of an international consumer products company that offers cosmetics, health & beauty products, accessories, and costumes for children. The owner had significant concerns regarding their commercial insurance portfolio:

• The cost of their commercial policies had been rising over the years. Although minimal losses were incurred, their premiums were increasing to the point that they needed to consider self-insuring some of their risks in order to control their insurance expense outlay.

• Over the years, coverages that were once easily obtained and affordable commercially, had now been eliminated from the commercial marketplace and/or had become cost prohibitive due to the increased premiums.

• Current suppliers and third-party vendors were dictating certain additional coverages which they needed to obtain. They felt that these additional coverages were completely unnecessary and would negatively impact their bottom line. In addition, the coverages being requested contained onerous exclusions that would make placing and collecting on a claim difficult.

Recommendations:

We discussed the idea of using a private captive insurance company to coordinate with their commercial coverage. We felt this would make their overall risk management program more cost and benefit efficient. A feasibility study was performed examining their current coverage, including exclusions, costs, and a review of what coverages were in-line with industry standards. The study also addressed risks that were either self or uninsured. Our recommendations were as follows:

1. It was apparent that most of their coverages never had a claim attributed to it. We were able to transfer some of these lines to the private insurance company. The premiums that were paid on these coverages were paid on a tax-deductible basis to the private captive insurance company. This allowed them to re-capture underwriting profits and create future surplus in their private insurance company.

2. The owners were able to relieve their significant concerns about risks that were not insurable in the commercial market but which could adversely affect their company if a claim was to arise. These included risks such as loss of key customer, supply chain interruption, and business interruption coverage. By utilizing the private insurance company to address these risks, they could, most efficiently, address these issues by retaining any premiums that were not utilized for claims.

3. Since the parent company was a family-owned business, the private insurance company would become a conduit to help develop a business succession plan that allows the second generation to eventually buy out the founder.

Outcome:

Since the implementation of the private insurance company, the parent company has been able to utilize the surplus capital in the insurance company to address important business issues, such as:

1. Purchasing a new warehouse facility. This allowed them to efficiently obtain this new facility with lower financing costs.

2. To buy out a key vendor in their supply chain. The purchase added control, synergy, and profit to their business operations.

3. Dividends of surplus were paid from the captive insurance company to another commonly owned business on a tax favored basis. These funds are being utilized to help fund a multigenerational estate plan.

When the private insurance company was initiated, it was designed to address the singular purpose of reducing the current premium outlay and protecting more of their self-insured risks. As the private insurance company matured, it became an important, multifaceted tool for the parent corporation, its owners, and their overall business planning.

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