THE PREFERRED PROVIDER TO THE MOST TRUSTED ADVISOR

National Network of Accountants, 6900 Jericho Turnpike, Syosset, NY 11791
www.nnaplan.com E-mail address: rroth@nnaplan.com
Offices located in Connecticut, Florida, New York, and Israel

Making a "Case" for Captive Insurance

By Ronald M. Roth, Senior Vice President
National Network of Accountants

Every day, business owners ask about the benefits of utilizing captive insurance as part of their risk management program.
Our first step is to take them through an overview of:

- how captives are operated
- how they integrate with commercial insurance coverage
- how they can help make a more efficient risk management program

With these thoughts in mind, we decided this month to present an actual case study to help answer these questions and show the positive effect a captive can have on the bottom line of a business.
The following is one of our current clients who has had a captive insurance

Client/Challenge:

The owner of an international consumer products company offering cosmetics, health and beauty products and accessories, approached us due to significant concerns about 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 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 this coverage was 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* in coordination with commercial coverage. This would make their overall risk management program more cost and benefit efficient. A feasibility study was performed that examined 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 coverage, that they were paying premiums on, had never had a claim attributed to them. We were able to transfer some of these lines to the private (captive) insurance company. The premiums that were paid on this coverage were paid on a tax-deductible basis to the private captive insurance company. This allowed them to *recapture* underwriting profits and to create future surplus in their private insurance company.
2. The owners were able to relieve their significant concerns about risks not insurable in the commercial market that 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 the 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 has become a conduit to help develop a business succession plan that will allow 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 the new facility with lower financing costs.

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

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

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 a multifaceted and important tool for the parent corporation, its owners, and their overall business planning.

"There's a better way to do it – find it."

Thomas Edison

THE NATIONAL NETWORK OF ACCOUNTANTS, INC.

Ron Roth
Phone: 516-629-9063
E-mail: rroth@nnaplan.com
National Network of Accountants
6900 Jericho Turnpike, STE. 300
Syosset, NY 11791
www.nnaplan.com