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SOCIAL VALUES AND THE CAPTIVE INSURANCE INDUSTRY



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By William York, VP Marketing

It is a known fact that business development and business growth drive the economic engine in the United States. Businesses generate income that assist both the Federal and State governments. In turn, the State and Federal governments provide services to the people such as police protection, fire protection, road maintenance, mail service, etc.

The growth of business is also responsible for an increase in employment. A strong workforce is the backbone of the American economy. A stable business environment is essential to national security and the wellbeing of each citizen.

Business owners were seeking solutions to problems that could potentially devastate their businesses. These potential problems (such as the Covid 19 pandemic) would threaten to close their doors, terminate employees and, therefore, the business would stop paying taxes. This was the principal reason behind the creation of the Captive Insurance industry.

As previously stated, business failure is not good for the general economic strength of the United States. Over the years, Department of Labor statistics have shown that the lack of adequate insurance coverage is a major contributing factor to business failures.

Two major factors have further exacerbated this issue over the last ten years:

- We live in a litigious society
- Natural disasters, (such as the recent pandemic, hurricanes, etc.) have caused many P&C insurance carriers to reassess their exposures and to limit the type of coverages offered.

Businesses are exposed to a variety of risks on a daily basis such as:

- Coverage for loss of computer data, loss of a key customer, international terrorism, copyright infringement, currency risk, judicial and administrative delay, lender failure, change of circumstance in an industry, pandemics and other natural disasters. **The list goes on and on.**

As early as 1957, legislation was established to permit "Special Purpose Insurance Companies," commonly known today as Captive Insurance companies. This legislation was designed to help businesses, employees and the general public.

Through the use of this selective legislation, Congress aimed at leveling the playing field between those businesses that chose to self-insure certain risk, and those businesses who chose to use third-party insurance. While it was widely understood that businesses have a multitude of risks, it was also an issue of paying

exorbitant premiums to cover these risks. Historically, risk protection insurance could be obtained by paying tax-deductible premiums to a third-party insurance company, while self-insurance had to be provided with after tax dollars.

In the passage of the 1957 legislation, Congress intended to incentivize businesses that currently do not purchase insurance from a third party (due to cost or other considerations) and who fail to create a reserve for these risks. The legislation allows for business to reserve against risks in a tax efficient manner.

Currently there are 36 states, the District of Columbia and the U.S. Virgin Islands that have enacted laws that regulate these company sponsored insurance companies. Today, these companies comprise 20% of the worldwide corporate P&C coverage. Additionally, they comprise between \$55 - \$60 billion in annual premiums. All 30 companies comprising the Dow Jones Industrials have their own Captive Insurance companies and over 90% of the Fortune 500 companies utilize captives.

The growth of this industry has had an enormously positive effect on local state governments, the federal government and business in general. Most certainly the growth of this industry has had a positive effect on the workers in America. Every state, through their economic development programs and insurance departments, have increased employment as a direct result of this program.

In addition to the increased employment, states are experiencing a growth in income caused by an increase in premium revenue. As an example, in recent years the State of Connecticut has established itself as one of the leading domiciles in the captive insurance industry. Our firm, the National Network of Accountants, through an initiative called "Reimagining Business Insurance" has been responsible for attracting new captives to the state, including 12 formed by out-of-state companies.

IN CONCLUSION

- Captive insurance legislation has aided in stabilizing business and this certainty has caused increased employment and greater profit margins.
- Captive legislation is good for job growth both on the State level and the individual corporate level. Throughout the United States it is estimated that this growth has actually increased retail sales, home building and provided greater security for the workforce.
- Captive legislation is good for the Federal government because less business failures have occurred which translates to lower unemployment costs and increased tax revenue.

Recent studies conducted among captive owners have revealed that increased reserves and surplus with captives has created a 'war chest' for businesses in difficult times. They have created true asset protection for business owners and helped to retain employees. Captives are drivers of employment, employee benefits, healthcare and employee security. Captives offer and add greater social value! A true win/win.

"We build too many walls and not enough bridges".
– Isaac Newton



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