For decades, large corporations around the world have enjoyed the many benefits of operating their own captive insurance company. Most were established to provide coverage where insurance was unavailable or unreasonably priced. These insurance subsidiaries or affiliates were often domiciled offshore, especially in Bermuda or the Cayman Islands. The risk management benefits of these captives were primary, but their efficient tax and operating advantages were also important.

In recent years, mid-sized, closely held businesses have also learned that the captive insurance entities can provide them significant benefits. These include the attractive risk management elements long appreciated by the larger companies, as well as some attractive opportunities. A properly structured and managed captive insurance company is all about control and, properly structured for the right reasons, could provide the following benefits:

- Retain premiums otherwise paid for commercial insurance
- Design coverage for gaps and/or egregious terms typically found in commercial policies (i.e. property retentions; wage/hour coverage; product recall)
- Direct access to the lower-cost reinsurance market
- Use higher retentions to drive market pricing (reduce dependence on commercial market)
- Ability to manage claims yourself, not rely on the insurance company's incentives to settle claims
- Keep underwriting profits and investment income on funds held
- Profit center to manage customer risk (provide warranties, weather insurance; guarantees)
- Use equity for dividend potential (or invest in expansion of your business, shareholders)
- Efficient tax treatment of underwriting profits, when it makes sense
- A vehicle to manage compliance and risk appetite across the organization

There are many types of captives for a multitude of purposes. For example, these include "pure captives," where the insurance company only insures the risks of the owner and related entities; "group captives," where the captive insures the risks of the shareholder/members of the captive; and "agency captives," where the captive is owned and operated by one group (insurance agents) to insure the risks of their related clients.

IDEAL CANDIDATES FOR CAPTIVES

Single parent captive should be considered for entities that meet the following criteria:

- Entrepreneurial business entities seeking control over their insurance future
- Historically favorable loss experience (loss ratio less than 50% of premiums paid over 5-years)
- Businesses with diverse risk exposures or high risk needing customized solutions
- Commercial insurance premiums typically exceed $1MM annually
- Owners who can commit to a long-term strategic play
- Management is committed to safety, risk management, and loss control
- Business with a problem to solve: extended warranties; customer billings; high retentions

INSURANCE REQUIREMENTS

There are some captive promoters that historically "sold" captives exclusively for the tax benefits alone. The IRS will not tolerate this structure and mandates that the captive must be established for legitimate insurance purposes. We are risk management and insurance-focused, not tax, so while being tax efficient is important, it's not the focus of a captive and never should be.

Sufficient for this paper is to state that for a captive to qualify as a valid insurance company, it must at least insure legitimate business risks, operate in way that insurance companies would generally operate, and have the elements of risk shifting and risk distribution. We are happy to continue the discussion, but if "tax benefit" is the first objective on your list of captive benefits, we are likely not the right fit as your consultant.

FORMATION OF A CAPTIVE

The formation of a captive insurance company is a detailed process including feasibility studies, financial projections, determining domicile, and, finally, preparing and submitting the application for an insurance license.

The need for a qualified captive manager on the planning team is very important, particularly in the formative stages.

One critical function to be performed during the formative stages is the identification of the risks to be insured by the captive. We call this process, "CORE™ Review" (Coordinated Overview of Risk and Exposure). We identify your current gaps and operational exposures, then blend them with outside actuary and risk management recommendations. The operating company is presently paying premiums to one or more commercial insurance companies to protect it from specific risks, some of which could be catastrophic if they were to occur without such insurance. The goal of a captive would be to maintain the transfer of the catastrophic risks to the commercial carriers, but to assume the underwriting and premiums associated with more "manageable" risks.

The policies that are written need to be for "real" insurance risks, not ones that will never occur. Should the captive see a need to protect itself in the case of a higher-risk policy, it may be able to buy reinsurance at premiums that are less than the premiums that it has charged the parent company.

One of the key risk management benefits that the captive will provide is the flexibility to opt for higher deductible levels on the existing property and casualty (or health) insurance policies. This obviously helps drive deep discounts in your commercial premium.

Another area for consideration is the requirement for adequate initial capitalization. This will be dependent in part on the level of risk projected to be assumed by the captive and the requirements of the respective domicile chosen. In some cases, this initial capitalization can be accomplished using irrevocable letters of credit.

OPERATION OF THE CAPTIVE

The use of an experienced and capable Captive Manager is an essential element of the normal operations of a regulated and board governed entity. If a fronting carrier is necessary to pass the premiums along to the captive, then a Program Manager will be key to structuring and maintaining this relationship. Elevate serves both as a Captive Manager and Program Manager.

The need for annual actuarial reviews, annual financial statement audits, continuing governance compliance oversight, claims management, and other regulatory compliance needs puts the day-to-day management of a captive insurance company beyond the skills of most general businesspeople. Likewise, the oversight of the management company in the investment activities of the captive is essential from a planning perspective to assure that the captive's liquidity needs are met.

SUMMARY

You no longer must solely rely on commercial insurance to fund for risk and uncertainty. By creating and owning your own captive, you can finally take the ultimate control in your own risk-financing destiny and enjoy the benefits that the vast majority of the Fortune 500 companies have been taking advantage of for decades.

Benefits	Savings	Cautions
Greater control of insurance Manuscript insurance terms Less dependence on insurance mkt. Experienced claims managers Leverage buy excess limits Share knowledge Improved cash flow	Pay only your group's losses Lower administrative expenses Keep profits & investment income Receive dividends Lower claim payouts with experienced adjusters	Long-term commitment Capital outlay at the start Sharing results of members Finding like-minded business owners

Elevate provides turn-key design/build solutions, and operates your captive insurance company, with full transparency and accountable to you. We are captive insurance experts, so you don't have to be.

For more Information, please contact:

Ryan Ralston
President
Elevate Risk Solutions
11500 E Turtle Creek Circle
Wichita, KS 67226
ryan@elevaterisk.solutions

Direct: 316.746.7277 Mobile: 316-239-4588

Ryan is an experienced industry leader in risk management and insurance. He is a past Director of Risk Management at Whirlpool Corporation and as Risk Manager at Koch Industries, The Boeing Company. Ryan has lead organizations to develop and implement global risk management strategies, including the placement of insurance, negotiation and interpretation of coverage, self-insurance analysis, enterprise risk management process, claim management, actuarial reserve analysis and accounting impact, captive set-up and management, and broker relations. Ryan has participated on due diligence teams and with the integration of major acquisitions. He has been a frequent speaker at RIMS and CICA for risk management, captives, and leadership topics.