A Convert to ART Entrepreneurship

By Dick Goff

This is our first anniversary ART Gallery article. It's not likely I'll be cutting myself a slice of cake (all those carbs!) but that doesn't mean I won't celebrate. Consider yourselves all invited (must be a million or so including all the pass-along readers).

I know one person who'll join the party. He's successful entrepreneur Keith Sullivan, who built up a mega-TPA, sold it to a financial services giant and then had the luxury of deciding what he really wanted to do with his career. His answer is to follow in the pioneering path of alternative risk transfer (ART).

I have in past months extolled the virtues and benefits of industry service providers in getting on board the ART express and leading their clients to both solving their risk management challenges and profitably participating in ART risk management vehicles.

Now a significant player has decided to do exactly that and I feel like Elmer Gantry, the fictional evangelist played so well by Burt Lancaster (Classic Films for Old Fogeys cable channel). Elmer knew his first follower would be one of many.

Sullivan's conversion includes a complex business model that he believes will serve the interests of all parties in an ART structure, whether it may involve self-insurance, a captive insurance company, a risk retention group or innovative uses of reinsurance.

First, a little background: Sullivan is a career insurance professional who rode the TPA elevator on its way to the penthouse in the 80s and 90s. Keith formed Performax, a Baltimore administrator that grew to manage a $500 million portfolio of client employee benefits. After selling the company to Legg Mason Inc. Keith vowed to find the "next big thing."

Now he's back in business as founder and CEO of Armada Corporation with a three-legged approach: broker/consultant to mid-to-large employers; specialty benefits product provider and risk taker through ART vehicles. By the latter avenue, Sullivan will have his own "skin in the game" in addition to earning fees for services.

Sullivan has a rock-ribbed strategic reason for trying to change the nature of benefits structures. He believes the nation's employee benefits universe will implode upon itself as unsustainable costs become too great to finance. That day may not be too far off.

Consultant and actuarial firm Milliman, Inc. stated that medical spending for the "typical American family of four" will be $12,214 this year, up an average annual increase of 9.8 percent for the period 2001-2005. Any kid with a calculator can forecast that an increase of that level over the next five years will push the average family's costs to $19,151. Another five years and the cost trend line gets steeper: $30,563. Where's the limit?

Another study by Wells Fargo found that the weighted average increase in employers' healthcare costs was 12 percent from 2003 to 2004.

"Employers are like the proverbial lobsters in a pot," Sullivan says. "They don't really feel the temperature go up until they're cooked. If fundamental changes aren't made in how healthcare and risk management costs are structured, we'll all be cooked."

Sullivan believes that ART can help control costs as the interests of all parties converge in a cooperative model rather than each taking its own direction in its own interests.

"ART changes the character of the relationship between the service provider and the customer," Sullivan says. "Traditionally, service providers have been transaction-oriented: 'how many of this can we sell, how many of those can we provide.' ART takes the service provider out of the commodity mode to become a long-term strategic partner."

As examples, Sullivan provides diagrams (I've always said yes when someone asked if they had to draw me a picture). Diagram #1 Diagram #2

In the current industry dynamic, employers, brokers and TPAs follow their own divergent interests. Of course, these are greatly simplified example lists, but it makes the point that each player naturally follows the path of self-interest.

In a future with ART structures, interests naturally converge: TPAs focus on elements that help mitigate costs and risks. Brokers are advisors in analyzing risks and sourcing markets to better manage outcomes. Employers reduce their immediate costs by 10 to 15 percent and participate in long-term returns. All of the tactical elements of the "current dynamic" are still accommodated, but they are subsumed by the new strategic approach.

The difference is this: in ART the rewards of risk-taking accrue to the partners of each project rather than to giant insurance companies. The insurance companies still get their fair share through stop-loss, fronting or reinsurance but they're not the economic locomotive. Their position is several cars back on the train, closer to the caboose.

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