

CRM Risk Financing

Section 5

Alternative Financing Options

Dale Fenwick, CIC, CRM, ARM



Incurred Loss Retro

Calculation	Incurred Losses	Indicated Retro Premium	Premium Payments (Credits)
Deposit		2,050,000	2,050,000
1st	200,000	1,050,000	(1,000,000)
2nd	600,000	1,323,000	323,000
5th	1,000,000	1,835,000	462,000
Final	1,000,000	1,835,000	-
Total Payments			1,835,000

Red Slides

- Red Slides indicate information not in the notebook
- Created by me to help the learning process
- Available online at:

Sovereign.ky or DaleFenwick.com

Look for the “CRM” button.

Pooling Example #1

Planka Oslo



Monthly Pass Cost =	\$100
No Ticket Fine =	\$120
Monthly Pool Contribution =	\$40
First Year Membership =	30 Plankers

Source: Wall Street Journal – 3/29/2011

<http://online.wsj.com/article/SB10001424052748703580004576180383768578942.html>

Pooling Example #2

Healthcare Sharing Ministries

- A. Formed by people wanting to share healthcare costs amongst “like-minded” people.
- B. Not “Insurance”
- C. “Guidelines” determine what is “Shareable.”

Pooling Example #2

Healthcare Sharing Ministries

- A. Samaritan Ministries
- B. Christian Healthcare Ministries
- C. Christian Care Ministries (aka Medi-Share)
- D. Liberty HealthShare
- E. Altrua HealthShare

Pooling Example #2

Medi-Share Example

- A. Monthly Contribution (premium) based upon:
 - 1. Age
 - 2. Family Size
 - 3. Selected Household Portion (deductible)
 - a. \$1,000
 - b. \$2,500
 - c. \$5,000
 - d. \$10,000
 - 4. Plus Administrative Charge

“Court Orders Two Illinois Workers Comp Pools into Rehab”

December 1999

**“Trusts' failure costs companies
\$363 million”**

“11 NY WC Pools Have Failed”

Poughkeepsie Journal • July 13, 2008

“60 towns owe MIRMA \$9.5M”

New Haven Register - April 24, 2010

**“Insurance pool’s ‘savings’ now cost
town \$1 Million”**

Ridgefield Press – December 28, 2010

Municipal Interlocal Risk Management Agency (MIRMA)

“Surprising Deficits Ate Into Promise of Group Self-Insurance”

Poughkeepsie Journal • July 13, 2008

"I understood the basics of a trust," said Patrick Murphy, owner of Sucato Builders of Poughkeepsie and a member of Elite Contractors Trust of New York. Among them: "If the trust is underfunded, your liability for workers' compensation claims never ends."

“New York workers compensation shortfall surges toward \$1 billion”

Business Insurance • August 17, 2011

”

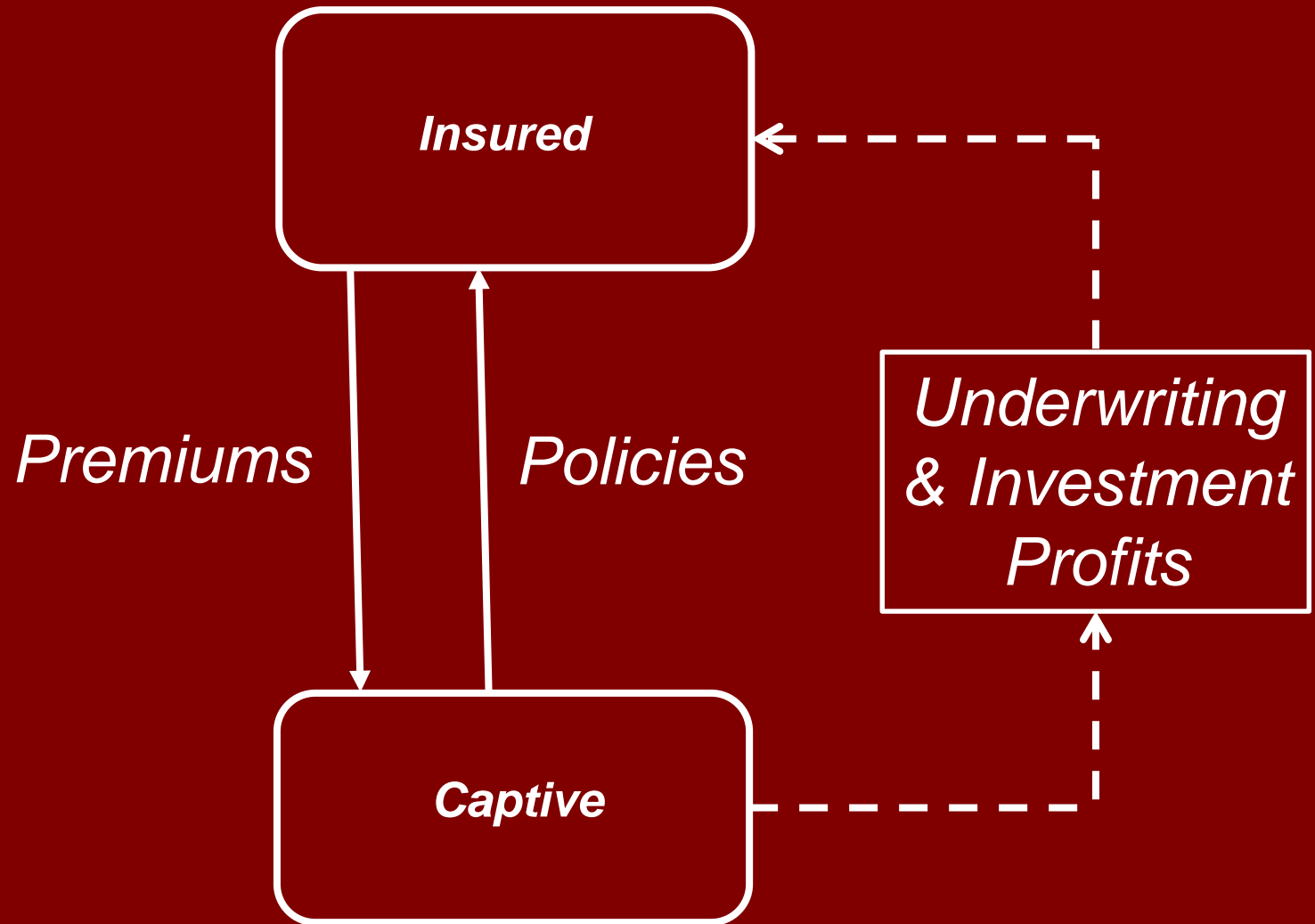
“I paid a premium to cover my company and now they're coming back and saying we owe \$925 million. It's insane.”

- Mark Teich, President of M&T Plumbing & Heating Co. Inc.

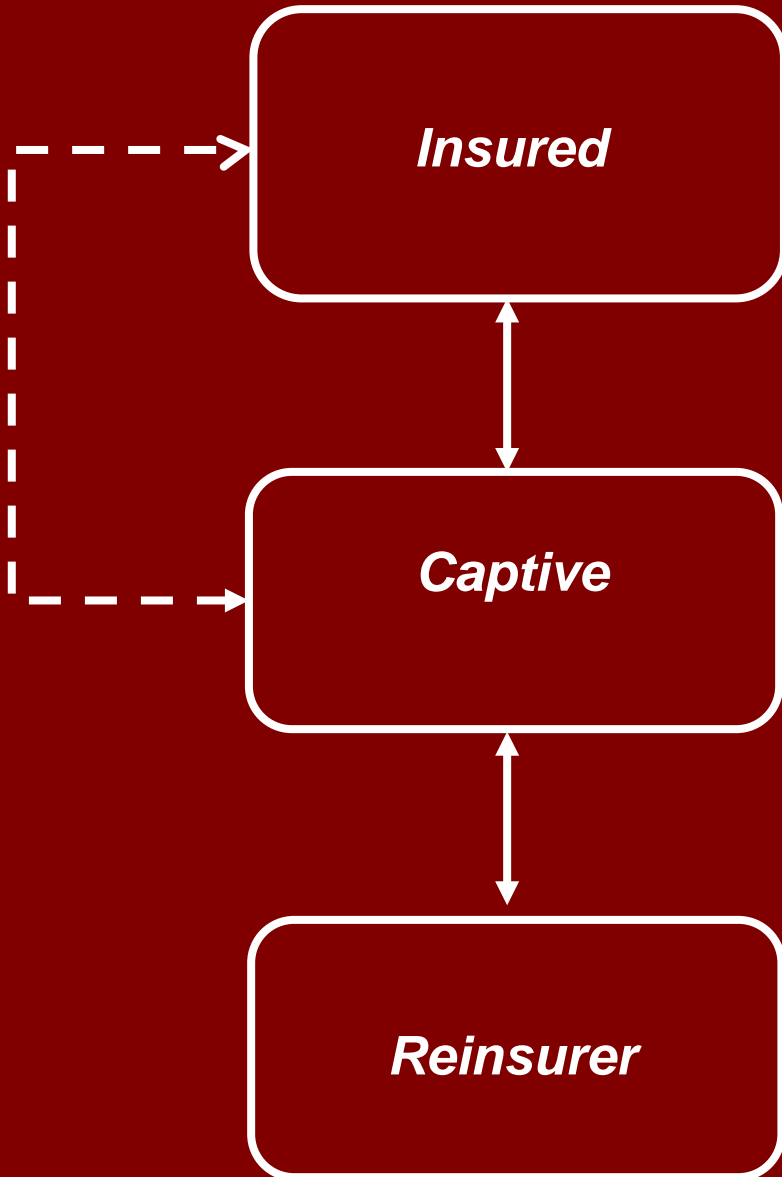
Why are these insurance companies called “captives?”

- Fred Reiss
- Ohio -1950s
- Youngstown Steel & Tube Company
- Mining operations called “captive” mines
- The insurance subsidiary became another form of “captive” operation.
- “The policyholder owns the insurance company; therefore, the insurer is captive to the policyholder.” – Fred Reiss

“Pure” Captive (Single Owner)



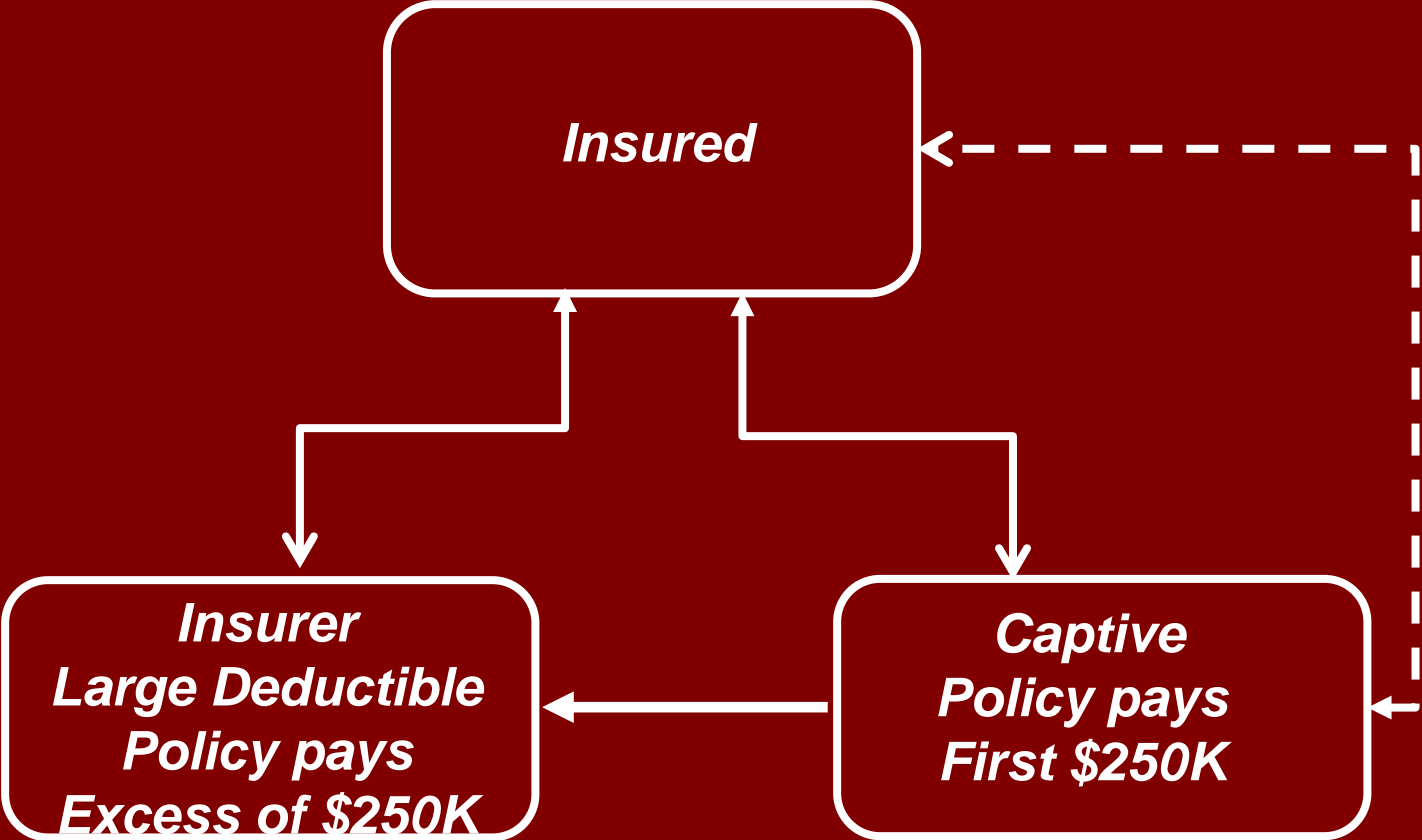
Direct-Write Captive Program



Issues Policy
Example: \$1 Million Limit
Retains Primary Layer
Example: First \$250,000 of each claim

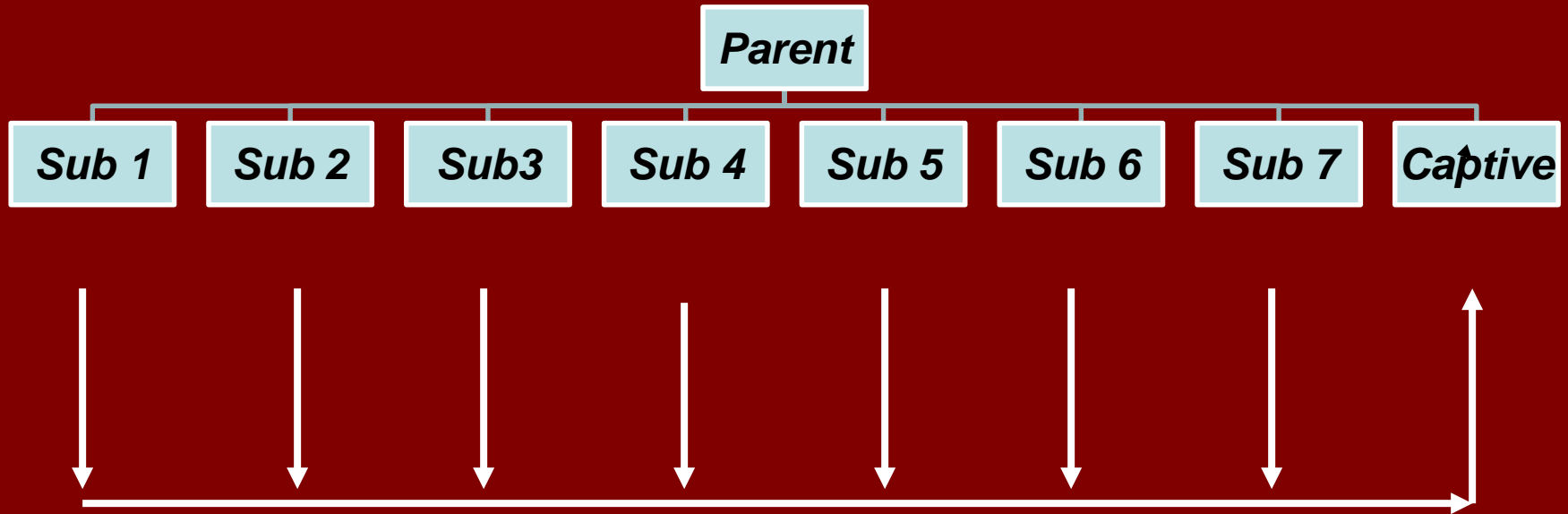
Provides Excess Reinsurance
Example: 750,000 x 250,000

Deductible Reimbursement Captive Program



Captive Provides Collateral

Single Parent Captive With Multiple Entities



Pools vs Captives

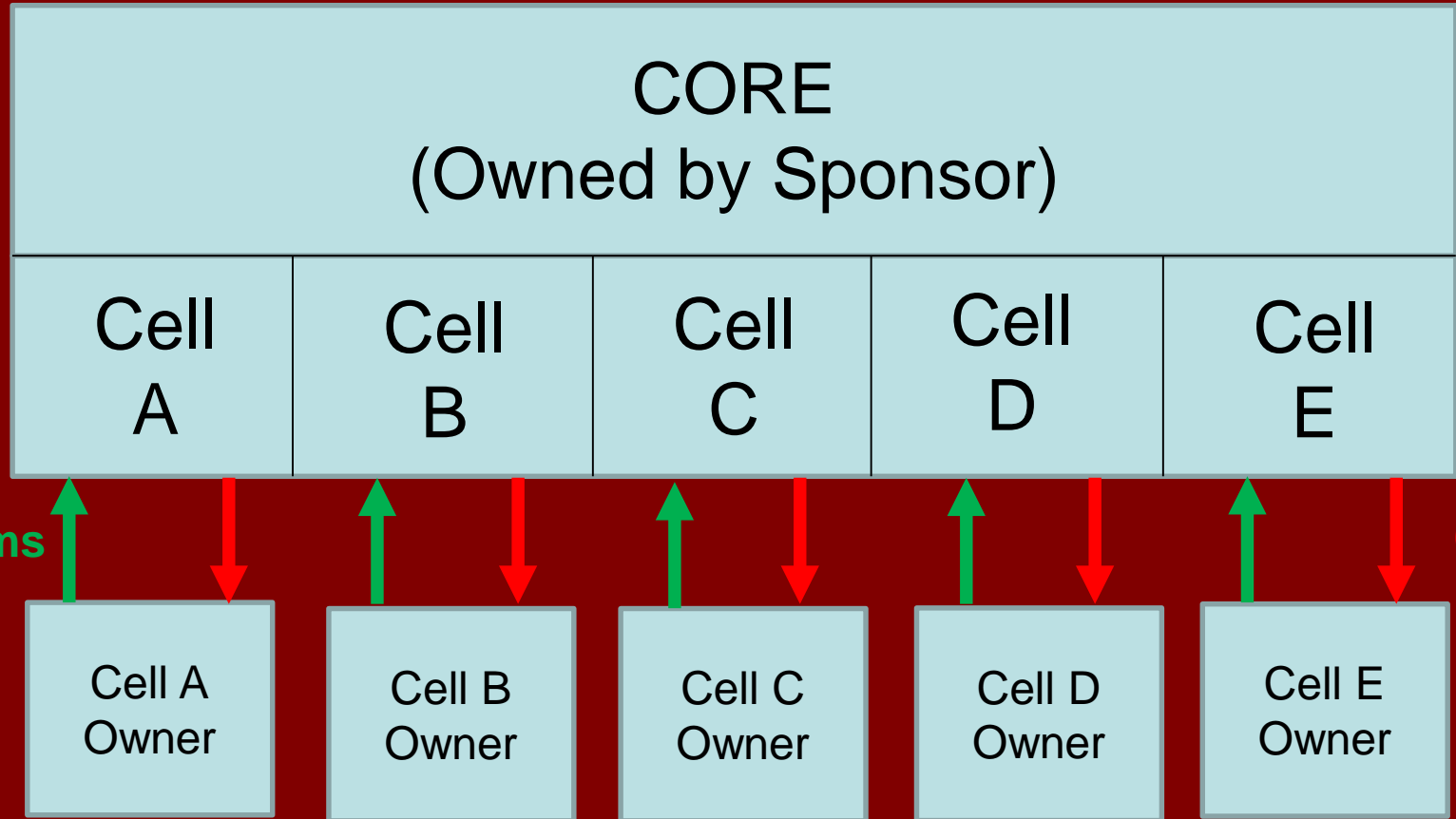
Pools (Regulated)

1. Operate only in the state of domicile
2. Limited coverage offerings
 - a. Private Employers (WC)
 - b. Public Employers (WC, GL, AL, Prop., etc...)
3. Front not required – Considered “Authorized”

Group Captives

1. Usually operate outside their domicile
2. Unlimited coverage offerings
3. Unauthorized unless front involved

Segregated Cell Rent-A-Captive

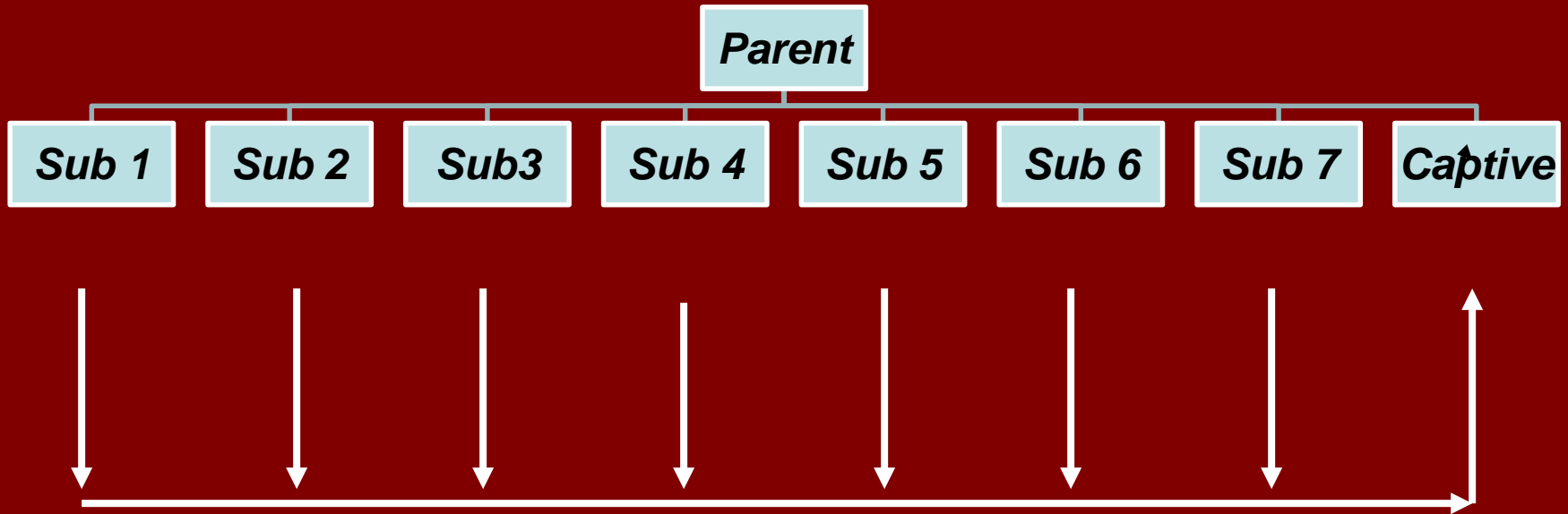


A Cell Captive is Like A Condominium...

- You control the inside (your cell), but...
- No ownership or control outside your 4 walls
- Limits on what you can do in your unit
 - Condo Bylaws = Participation Agreement
- Dues (RAC Fees), for your share of upkeep (Core Operations), and access to Common Elements (Core Capital and/or License)

Risk Distribution: The 15% Rule

(Rev. Rul. 2002-90)



***No one policy should represent
more than 15% of Premiums***

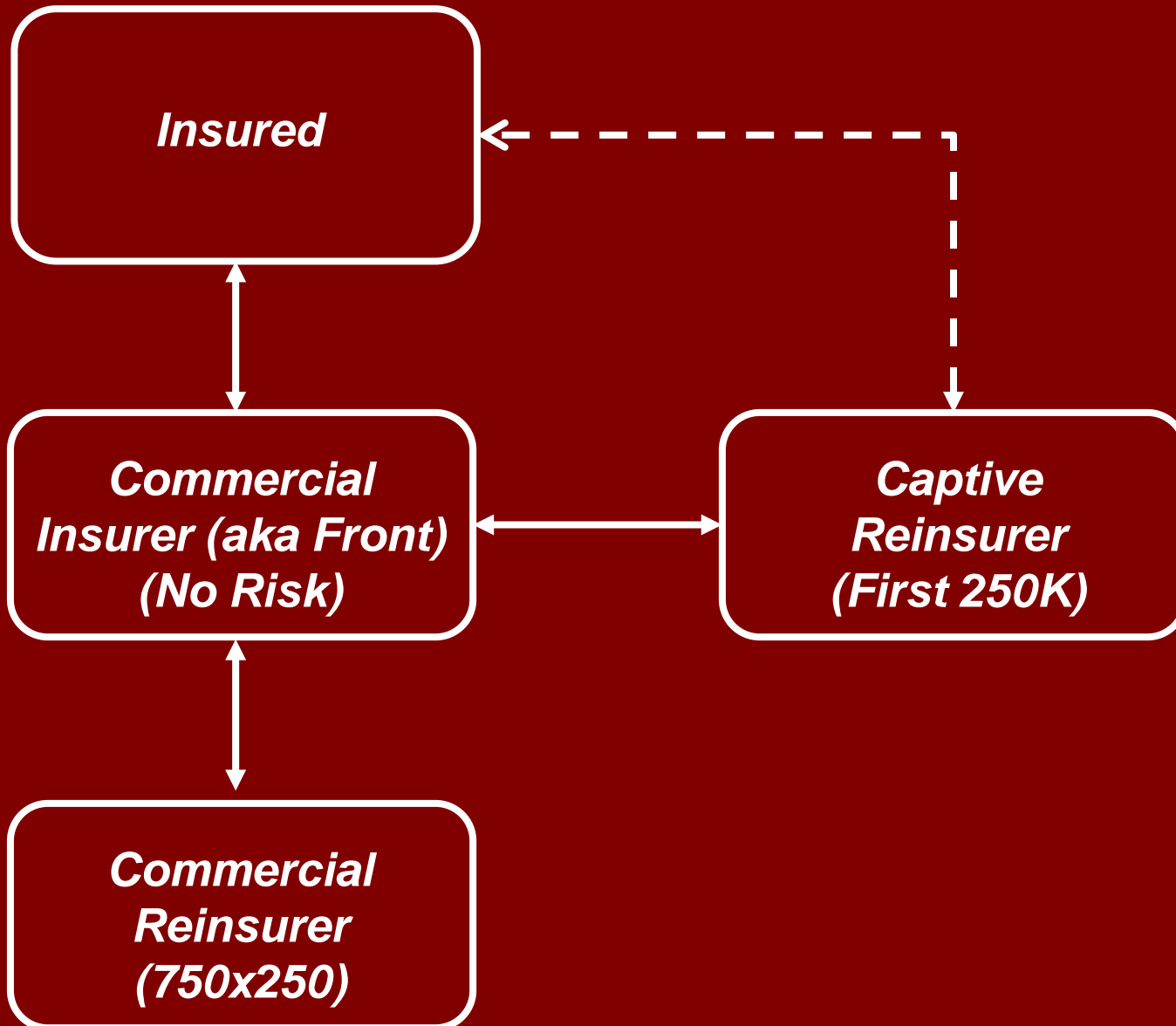
Federal Income Tax Comparison

	831(a)	831(b)
Premium	1,100,000	1,100,000
Administrative Expenses	100,000	100,000
Losses	-	-
Underwriting Profit	1,000,000	1,000,000
Investment Income	100,000	100,000
Net Income	1,100,000	1,100,000
Taxable Income	1,100,000	100,000
Taxes	(374,000)	(34,000)
After Tax Income	726,000	1,066,000

Captive Premium Tax Rates

Domicile	Direct Procurement	Captive Premium	Minimum
Arizona	3.00%	0.00%	\$5,000
Utah	4.25%	0.00%	\$5,000
Oklahoma	6.00%	0.20%	\$5,000
Delaware	2.00%	0.20%	\$5,000
District of Columbia	0.00%	0.25%	\$7,500
Hawaii	4.68%	0.25%	-
Missouri	5.00%	0.38%	\$7,500
Vermont	3.00%	0.38%	\$7,500
Montana	2.75%	0.40%	\$5,000
South Carolina	0.00%	0.40%	\$5,000
Tennessee	0.00%	0.40%	\$5,000
Nevada	3.50%	0.40%	\$5,000
Kentucky	2.00%	0.40%	\$5,000
Texas	4.85%	0.50%	\$7,500

Fronted Captive Program



Authorized vs Unauthorized

A. Authorized Insurance

1. Licensed / Admitted

a. State Approvals

1) Rates

2) Forms

b. Certificate of Authority

2. Surplus Lines

B. Unauthorized Insurance

1. Not Illegal – Just Not Regulated by the State

2. Direct Captive Policies

C. “Allowed” Insurance – Risk Retention Groups

Florida Division of Financial Services

The Division protects the public and insurance industry by timely and accurately licensing competent individuals and entities, and by fairly investigating alleged violations of the Florida Insurance Code and Administrative Rules.

Source: www.myfloridacfo.com

Iowa DOI Mission Statement

Our Mission:

The Iowa Insurance Division shall protect consumers through consumer education and by effectively and efficiently providing a fair, flexible and positive regulatory environment.

Source: <http://www.iid.state.ia.us>

Cayman DOI Mission Statement

Role of the Insurance Division

The Insurance Division monitors licensed insurance entities to ensure that they are operating in a satisfactory manner and remain solvent.

Source: <http://www.cimoney.com.ky>

Legacy Domiciles

2014 Captive Activity

Domicile	Jan	New	Closed	Dec	Growth
Bermuda	841	16	16	841	0%
Cayman	758	22	21	759	0%
Vermont	588	16	17	587	0%
Utah	343	106	25	424	24%
Delaware	298	87	52	333	12%
Hawaii	184	15	5	194	5%
Montana	150	34	7	177	18%
Nevada	148	26	9	165	11%
South Carolina	145	20	5	160	10%
Kentucky	128	-	6	122	-5%
DC	126	5	6	125	-1%
Arizona	106	13	5	114	8%

Emerging Domiciles

2014 Captive Activity

Domicile	Jan	New	Closed	Dec	Growth
North Carolina	4	49	0	53	1,225%
Tennessee	29	43	0	72	148%
Oklahoma	10	37	0	47	370%
Missouri	35	12	0	47	34%
Texas	0	12	0	12	NM
Connecticut	4	3	0	7	75%
New Jersey	14	3	0	17	21%
Total	96	159	0	255	166%

November 21, 1980



MGM Grand Fire

- 11/21/1980
- 84 Deaths / 400 Injured
- \$30 Million in Liability Coverage
- Was this enough?

MGM Grand Fire

In 1981 MGM Bought the Following:

Premium	Limits	Carrier
\$25 Million	35M X 30M	Union International
\$7 Million	35M X 65M	12 Insurers
\$2 Million	25M X 100M	8 Insurers
\$1 Million	75M X 125M	20 Insurers

MGM Grand Fire

- Why did the Insurers do this?
- Interest Rates in 1981
 - Prime Rate Averaged 18%
 - CD Rates were 9% to 12%.
 - At only 10%...
 - \$25 Million becomes \$37 Million in 4 years

MGM Grand Fire

- Union reinsured their \$35-million exposure
- Premium of \$20.2 million
- The reinsurance contract provided for no payments until 1984 and spread payments through 1991 (8 years).

MGM Grand Fire

In 1983 MGM settled all remaining claims for \$69 M

Insurers refused to reimburse

MGM sues insurers

April 1985 Settlement - \$76 Million

\$65 Million from MGM's insurers

\$11 Million from Del Webb