Moreton & Company

Property & Casualty Newsletter

July 2018: Captives

Taking Control of your Insurance Costs with Group Captives

Year after year many insurance buyers say to themselves, "I pay a premium to my insurer every year, I have no claims, and I rarely, if ever, get a decrease in my cost. What is that insurer doing with the money I give them?"

While insurers rightly say they use premiums collected to pay claims and operating expenses, the reality is that they are a business and have a profit need for share/stakeholders. Unfortunately, many buyers with a consistently good claims history often feel like they're not being rewarded properly–receiving no credit for running a safe business and keeping claims as few and low as possible

While companies that have an insurance premium spend over $1M and a manageable claims history have always been able to reduce their insurance costs by entering into large deductible plans for workers compensation, general liability, and/or auto (and now employee healthcare plans), the insurance community generally doesn't offer similar options to middle-market clients. This failing of commercial insurers to reward middle-sized insurance buyers has led to the explosive growth of the "group captive" insurance industry over the last two decades.

In a group captive program, a buyer arranges a typical, licensed, A-rated insurance contract with a standard commercial insurer, usually for workers compensation, general liability, and auto. That insurer then cedes a primary (or first) layer of coverage to the group captive via a reinsurance agreement. The group captive deducts a fixed expense fee from the identified premium to cover various fringe costs (usually about 40% of the money ceded), and the leftover balance is used to pay claims for that buyer's "account" as per the terms of the reinsurance agreement.

Behind-the-scenes, the same insurance buyer is also a part-owner of the group captive reinsurer. This means that if the portion of the ceded premium allocated to the buyer's "account" doesn't pay-out any claims, the buyer gets that money back–plus investment income–as a distribution from the group captive. This usually happens after a 3-5 year period, when almost all of the workers compensation, general liability, and auto claims have settled and paid (usually much quicker with employee healthcare plans).

(Continued on page 2)

These programs are called group captives because many like-minded insurance buyers make up the owners of the reinsurance entity, each with their own "account" and all with the same desire to recoup underwriting income from their own good claims experience that otherwise stays with an insurer. There is always some element of risk sharing amongst the group captive owners, and because these programs mimic deductible plans there is the risk of paying more than a standard-rated premium; nevertheless, the idea of controlling your own premium through good claims experience is very attractive to mid-market buyers.

Many group captives have formed since the early 2000s from a few specialty providers, with, according to some estimates, close to $3 billion in premiums annually funneling into group captives. Groups can be heterogeneous (many different buyer industries) or homogeneous (all participants of the same type, such as general contractors, truckers, medical services, temp agencies, etc.), and there are pros and cons for each type.

Moreton & Company has relationships with most of these providers and can explain these plans to you and help you choose the one that fits you best. Any one of our sales staff would love to explain how a group captive can give you more control over your insurance costs.

Please contact your Moreton & Company consultant with any questions.

Please visit www.moreton.com/news-events/ for more information and to view other newsletters. For additional questions, please contact your Moreton & Company representative.

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