

RIMS 31ST ANNUAL RIMS CONFERENCE

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Speaker's Name(s): FRANCIS A. ASCOLILLOSession Number: FN Session Name: PROFIT CENTER CAPTIVES.
203Date: MONDAY - April Time: 2:00 - 4:00 PM

Profit Center Captives

1993 RIMS Conference

Orlando, Florida

Session FN 203

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What is a Captive?

- Insurance Company owned by Non-Insurance Parent
- Exists for the Risk Management Needs of the Parent Company
- Is Not Necessarily a Profit Center

Typical Captive Programs

- Primary Casualty (Workers' Comp., General Liability, Automobile Liability)
- Professional Liability
- Environmental Impairment Liability
- Property Quota Share Programs

Why Form a Captive? *The "Soft" Reasons*

- Funding Predictable Losses
- Coverage in Problem Areas
- Meet Legal Coverage Requirements
- Program Consolidation and Rationalization
- Strategic Investment Reasons



Why Form A Captive? *The Money Reasons*

- Access to Underwriting Profits
- Cash Flow Benefits
- Allocability of Insurance Expenses to Clients
- Potential Tax Advantages
- Potential Fixed Cost Savings
- Encourage Loss Control Improvements at Subsidiary Level



Why Form A Captive? *The Money Reasons*

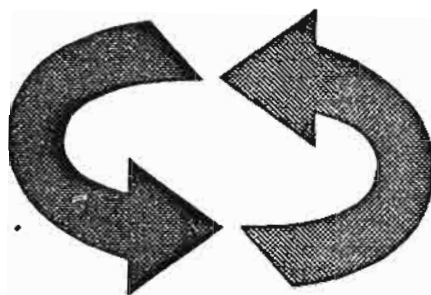
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Can a Captive Really Be a Profit Center?

*"Show Me a Profitable Captive,
and I'll Show You. . ."*

- A Large Parent Insurance Budget
- An Empire Builder



Innocent Capacity!

- Writing Facultative Reinsurance
- Accepting Quota Shares of Reinsurance Treaties
- Markets of Last Resort
- Entrepreneurial Ventures



The Horror Stories

- Walton
- ODECO
- Bad Treaties



The Lessons



- ◆ Captive Business is Still the Best Business
- ◆ Don't Be the Market of Last Resort
- ◆ Do Be the Market of First or Only Resort

Why the Renewed Interest in Profit Center Captives?

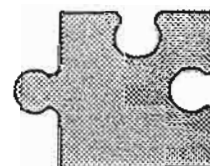
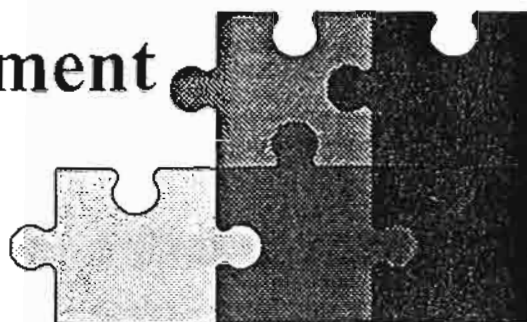
- Recent Tax Decisions
 - ✓ Harper Group
 - ✓ Amerco
 - ✓ ODECO
 - ✓ Revenue Ruling 92-93
- Product Enhancements
- Market Efficiencies

IRS Revenue Ruling 92-93

- Life/Health/Accident Business Considered Non-Parent Business
- Parent Can Insure These Coverages with Subsidiary and Take Tax Deductions
- Opportunity for "Safe" Outside Business

Product Enhancement Opportunities

- Credit Life Insurance
- Product Warranty
- Extended Service Contract
- Travel Related Coverages
- Property Coverages



Success Stories

- RLI (Replacement Lens)
- American Road Insurance Co.
- Burlington Industries
- Wang Laboratories



Criteria

Need Must Be Present

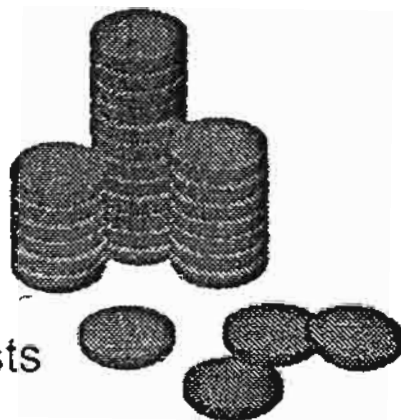
- Revenue
- Savings
- Special Purpose



Revenue

Insure Directly Associated Risks Unique to Parent

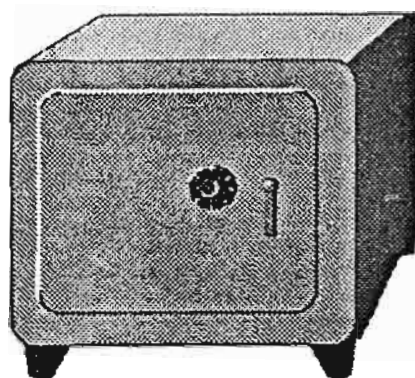
- Customer Need
- Alternative to Insurance
- Use Sunk or Contingency Costs
- Incremental Revenue/Sales



Savings

Alternative to Commercial Insurance in Areas of Expertise

- Technology
- Preserve Accrual
- Fund Risk
- Access Revenue



Special Purpose

Areas Not Adequately Addressed by Commercial Insurance

- Cash Flow . . . Employee Benefits
- Tax . . . Credit Insurance
- Liquidity . . . Bonds

Criteria

Basis Must Be Real

- Insurer Relationship
- Cost vs. Returns
- Examples

Transit

Workers' Comp

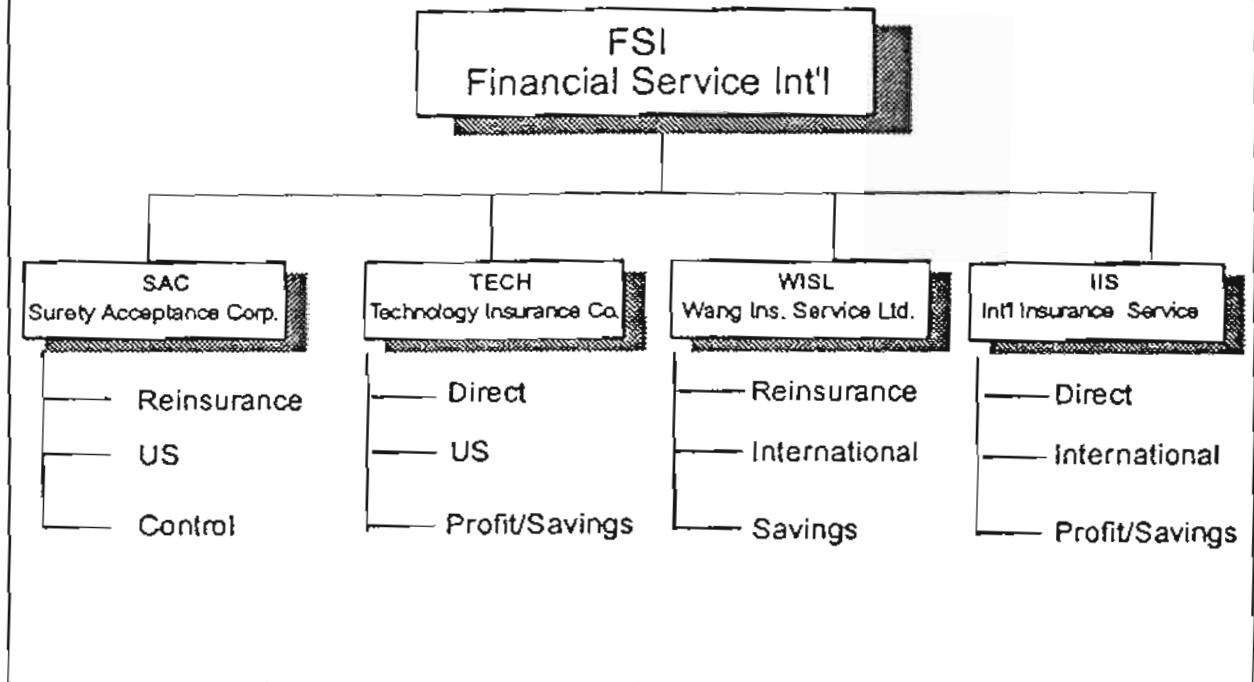
Credit

Property

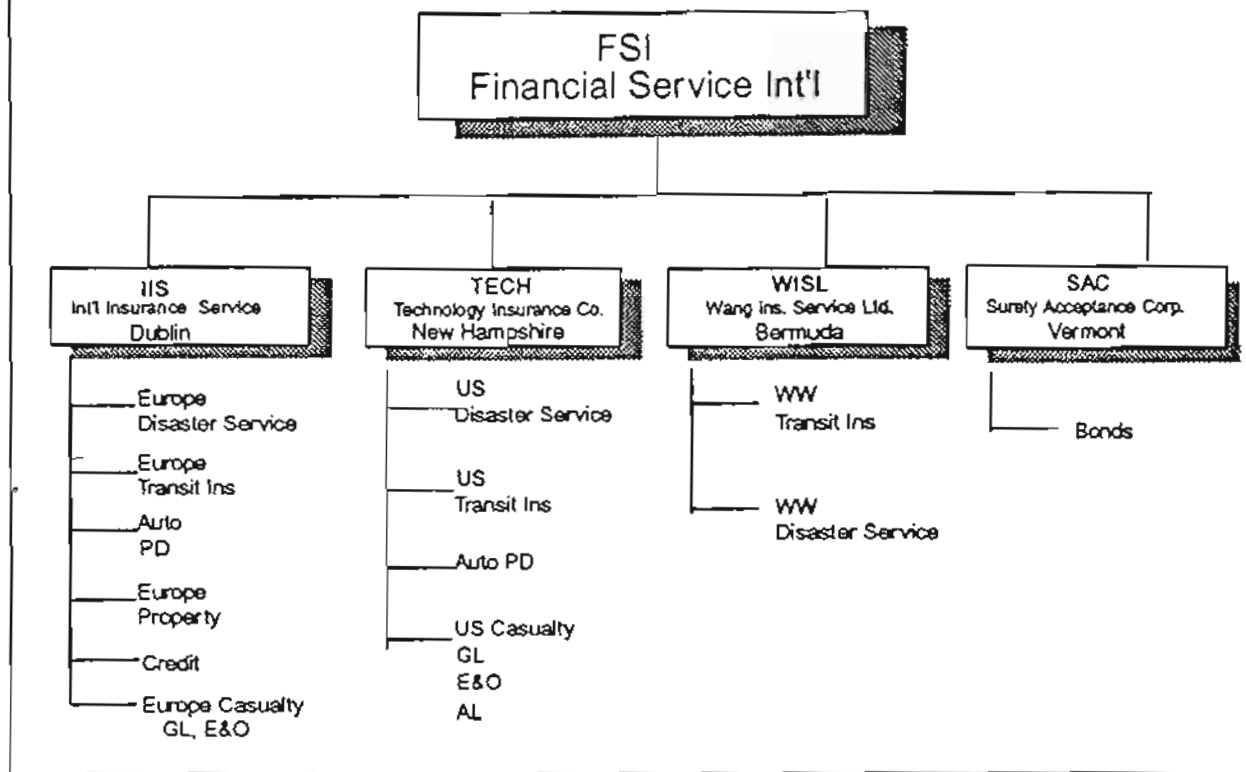
Auto

E&O

Case History



Case History



Key Factors for Success

- Existing Relationship with Insureds
- Be the Market of First Resort
- Knowledge of Insurance Product
- Awareness of Relevant Regulations, both insurance and non-insurance
- Good Working Relationship with Insurers

