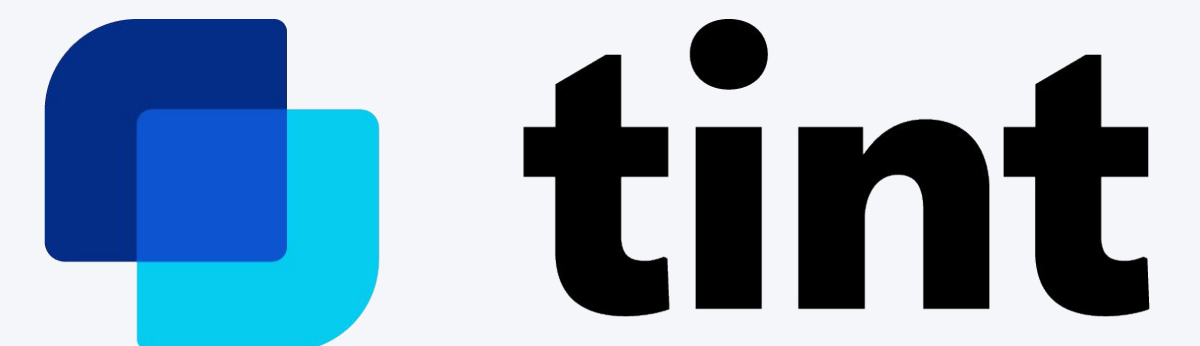


# **The Financial and Operational Implications of Captive Insurance: Everything You Need to Know**





# Introduction

Understanding the meaning of captive insurance can't be done with a simple definition. Captive insurance is a powerful financial tool for your business that can be deployed in a variety of ways, including to protect your users from the risks they face while transacting with you.

Captive insurance has been around for roughly 100 years. During that time, an evolution has occurred transforming how it has been deployed by some of the top brands in the world.

In this guide, we will cover the financial and operational implications of captive insurance and how its full potential can be realized when used in combination with technology that reduces the burdens placed on your organization.



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# Diving Into the Pros and Cons of Captive Insurance

Captive insurance isn't something that anyone creates on a whim. There are real financial and operational implications that need to be considered. Some of these are **significant pros for your business, like tax benefits**. However, the pros aren't limited to your corporate insurance needs; **captive insurance can also be used to protect your customers while they do business with you**. Additionally, there are other considerations that could be considered cons, like the plethora of administrative tasks required to effectively and compliantly manage your captive.

We will take you on a deeper dive of these pros and cons to help you assess whether a captive is right for your business.



# Financial Implications: The Pros

There are several positive outcomes you can expect from captive insurance. When we consider the financial implications, there are a few that stand out above all others. Risk reduction, favorable pricing, and tax benefits.

## **Risk Reduction**

A captive insurance company can be used to help take control by offering the ability to tailor coverage for hard to insure risks. Captive insurers have greater control over their coverage than those who purchase insurance from a traditional commercial insurer. This provides more flexibility in addition to the ability to cover risks that matter to your business, but may not be attractive to a traditional insurer.

## **Favorable Pricing and Tax Benefits**

The cost of purchasing insurance through traditional markets typically has baked in costs, like marketing expenses, broker commissions, administrative costs, and overhead. When you opt to self-insure through a captive, those expenses are eliminated. Furthermore, you are now in control over the cost of claims handling and the stabilization of prices from one year to the next..



# Financial Implications: The Cons

There are also several negative outcomes that coincide with self-insuring through a captive. These include the upfront and ongoing expenses needed to create and fund a captive and annual audits.

## High Start-Up Fees and Capitalization

The process of starting and funding a captive insurance company is an expensive one. Not only are there administrative costs such as claim administration, loss control, and underwriting; there are also high levels of capital required to fund the captive to pay out any potential losses. The amount will vary from company to company, but if you plan to create a single-parent captive the cost could be in the millions to hundreds of millions.

## Required Annual Audits

Captive insurance companies are required by their home state's department of insurance to have annual audits completed each year. This ensures the captive is abiding by the state's regulations. Annual audits can be time consuming, complex, and expensive if you do not have experienced employees handling them.



# Operational Implications: The Pros

Aside from the financial benefits of a captive, there are operational “pros” that can provide you more flexibility and autonomy. If you are creating a captive insurance company you can expect to own much more of how your program will be run than when you work with a traditional insurer.

## **Owning Your Process**

When creating a captive you’re able to reap many internal benefits for efficiency. First and foremost, you aren’t beholden to third parties so you can work on your own timetable. Real-time reporting can help guide financial decisions such as pricing. This allows changes to be made in a faster and more efficient manner, resulting in better overall outcomes.

## **Flexibility with Claims Management**

A captive allows your team(s) to adjudicate and pay claims without going through a lengthy payout process. This model has considerable benefits from an end-user satisfaction and internal perspective. In many cases, speed to claims payments can be crucial to maintain good relationships with customers / users. Owning this process allows you to achieve speed and quality, which are equally important to a well-run program.





# Operational Implications: The Cons

The challenges with captive insurance typically come in the form of needing dedicated resources to create but even more importantly, to maintain your captive insurance. When you add shifting regulations on top of that, the risk of getting it wrong is too great for many companies.

## High Administrative Burden

Although owning your own process can be beneficial, it's hard to gauge the administrative capital needed to maintain a complex captive and full insurance program. Over or under staffing can have a significant impact on the program's overall success. Without proper management, your program is set up for failure.

## Shifting Regulatory Complexity

Rules and regulations surrounding captive insurance companies are still growing and evolving. This is a highly regulated and complex subsection of the insurance industry, and it requires subject matter experts to ensure that your captive program is in compliance with all regulations. Not to mention the downstream impacts, including the potential need to hire outside counsel or consultants to help maintain compliance.

## Required Annual Audits

Annual audits can vary depending on the size and complexity of your program. However, dedicated resources are needed each year to work with auditors. This either distracts employees from their normal duties or requires full-time employees dedicated to the task for several months.



## Pros

- Risk Reduction
- Pricing & Tax Benefits
- Ownership
- Flexibility

## Cons

- Expenses
- Annual Audits
- Administrative Burden
- Regulatory Complexity

## Key Takeaways:

To determine if a traditional single-parent captive insurance company is right for your business, you have to weigh the pros and cons. Most businesses will take pains to understand the impact it will have on the corporate insurance structure, but the most innovative businesses are also going a step beyond and evaluating whether end-users could be positively impacted with the risk mitigation captives provide.

If it doesn't make sense financially or operationally to create a single parent captive, there are still other options available to you that can protect your core business and end-users. Options that make sense for companies of nearly any size, in any industry.

# Leveraging Captive Insurance As a Non-Fortune 500 Company

Creative captive insurance relies on a solid foundation. Many companies are tempted to strategize internally, determine what elements they feel comfortable taking on themselves, and then hire an outside captive manager to handle everything else. We'd recommend taking a more holistic approach that includes thinking outside the box. Captives are a great tool for your corporate insurance needs but they can be an even better tool to protect your customers from the risks inherent in your business.

**1. Set your goals.** What are you hoping to achieve? Evaluate potential financial goals, risk management goals, and operational goals. To elevate your goals, consider whether there are risks your customers face that could be monetized.

**2. Research.** Understand the types of captives available to you and the limitations of each. Look at what types of captive managers might make sense and what roles you'd like to play as a company.

**3. Consult with experts.** Innovations are happening all the time in how captives are deployed (and for what reasons). We'd recommend that you speak with professionals who can help you hone your strategy and creatively brainstorm ways to achieve your goals.

**4. Look at the overall picture and deploy resources wisely.** Depending on your company size, financial resources, and priorities you may find that although the benefits of captive insurance are alluring the real-world implications are too much for you to take on. However, that doesn't mean you need to give up on captive insurance as a tool - you need a strong partner who can help you from start to finish.

**If you are considering captive insurance and want to speak with a professional who can help you turn your goals into a well-executed strategy without huge overhead costs, high administrative burden, and don't want shifting regulations to become a roadblock, let us know. We'd be happy to talk with you about your goals and see if captive insurance could help.**

TALK WITH THE TINT TEAM

# WORK WITH THE EXPERTS



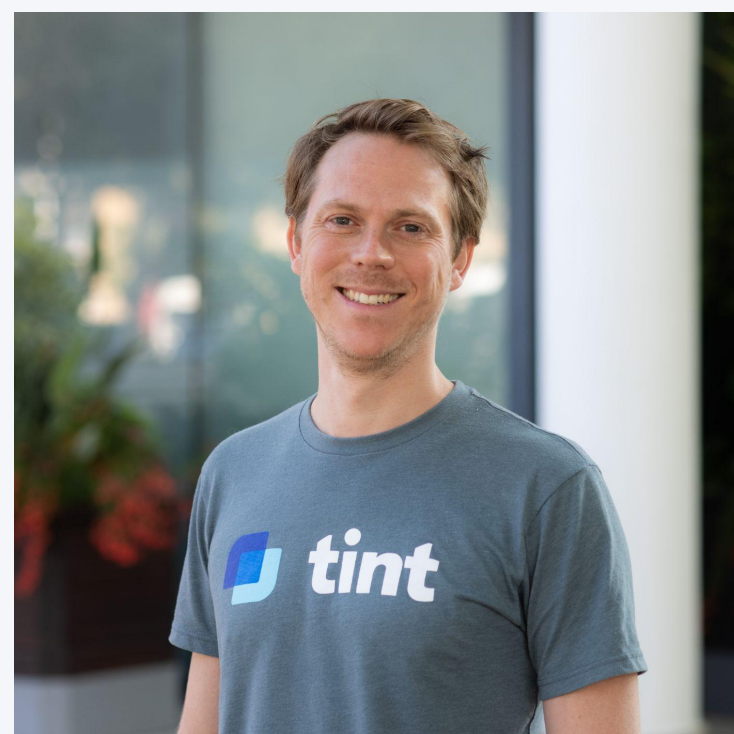
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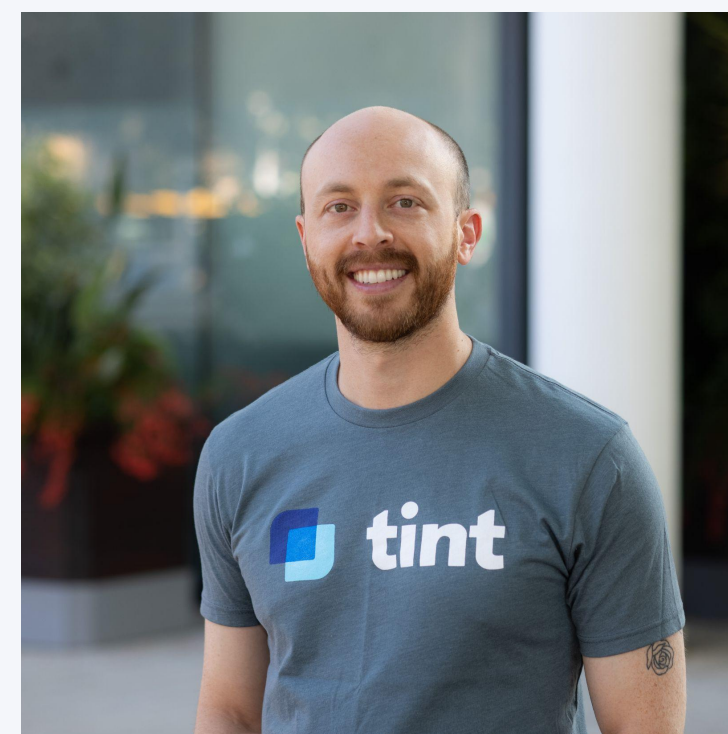
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# Thank You!

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