

## GRAHAM PROMOTES THREE NEW VICE PRESIDENTS

### DAWN A. HOUPT CPCU, AIC, ARM



Dawn joined The Graham Company in 1988. Prior to her joining the Technical Development Department, Dawn handled various levels of multi-line claims and was a claims supervisor at The Graham Company. While still a member of the Technical Development Department, Dawn has also been promoted to Claims Manager of the Claims Services Department. In this role she is responsible for directing claims consultants in providing the highest level of claims services for our clients.

### KEVIN D. SMITH CPCU, ARM



Kevin joined The Graham Company in 1999. Kevin acts as a technical resource for the development and training of new producers, participates in continuing education seminars and performs audits for new business quality assurance. He is involved in the development of The Graham Company's Group Captive, is active in the risk assessment practice group and is the practice group leader for the international practice group.

### G. MARTIN IRONS CPCU, CIC, ARM



With The Graham Company for over 18 years, Marty is the Team Leader for the Technical Resource supporting the account management units and is responsible for account management unit training, continuous improvement and quality assurance. He is also active in The Graham Company's practice groups for construction, mergers & acquisitions and environmental coverage.

## COMMENTS FROM THE CEO

A Captive Insurance Company is one of several strategies you can use to take control over your insurance program. Captives provide a way for you to



enjoy the benefits of owning an insurance company, including keeping the underwriting profit (premiums minus expenses and losses) and investment income involved with insuring the risks of your organization. Like most strategies we recommend at The Graham Company, success with a Captive Insurance Company is ultimately driven by working safely. Companies with world-class safety will reap the biggest rewards. We can help you get there.

We first started seriously researching captives in the 1990s. We talked with our clients and found that many of them wanted a way to take control of their insurance program and find a way to enjoy the savings they deserved by running a safe organization. Clients asked us, "If our losses are significantly less than the premiums we paid, why should the insurance company get to keep all of our money?"

After a thorough search, we partnered with Innovative Captive Strategies (ICS), a leading captive consulting firm, to help us enter the captive insurance marketplace. In 2001, we launched The Graham Company Group Captive, and today it insures the risks of 15 different businesses. This newsletter is designed to give you a snapshot of Captive Insurance Company options and help you to understand how you can turn premiums into profits using these structures. We'd love to hear your thoughts; please send an email to [feedback@grahamco.com](mailto:feedback@grahamco.com).

Best regards,

WILLIAM A. GRAHAM, IV, CPCU, CLU  
CEO

## FREEDOM IN CAPTIVITY: UTILIZING GROUP CAPTIVE INSURANCE

By BILL SELMAN, VICE PRESIDENT, THE GRAHAM COMPANY

Control. For most business owners and CFOs, it's not a word that comes to mind when insurance is the topic. For Gary Nolan, President and Founder of Brother's Inc., a family-owned and operated electrical contracting business in the Philadelphia tri-state region with annual revenue of \$32 million, control is exactly what Nolan now has over his business' insurance program—in fact, he operates his own insurance company through The Graham Company's Group Captive.

"In 1981, I started my business out of a pickup truck with four employees. As my business continued to grow throughout the years, I remained committed to managing every aspect of the company's success, working diligently to forge meaningful relationships with builders and managing my contractors," said Nolan. "But one item I never controlled was my insurance costs – I never questioned steadily rising insurance premiums because I thought there was no alternative," recalled Nolan.



As a result of his superior safety culture, Gary Nolan, President and Founder of Brother's Inc., has accrued over \$2 million offshore. Photo credit: Brother's Inc.

MANAGE THE X-FACTOR

Mike Mitchell, CPA, CPCU, Executive Vice President of The Graham Company, said, "We recommended our Group Captive insurance program, not because it's a quick-fix alternative, but because Nolan demonstrated a real commitment to strengthening his company's safety culture." The Graham Company Group Captive is a member-owned group captive operated by companies in various industries, from construction and distribution to manufacturing and financial services. While the Captive is designed for companies that

pay premiums of \$500,000 or more, it is paramount that the company maintains a commitment to safety and loss control. "Most business owners are under the misconception that captives are an instant money-saver; the reality for Nolan, and all other members of The Graham Company's Group Captive, is that your safety culture and commitment to upholding world-class safety standards is the x-factor when it comes to captive insurance and cost savings," continued Mitchell.

GET IN THE DRIVER'S SEAT

Captives provide business owners with the unique alternative of owning their own insurance company. For members of The Graham Company's Group Captive, this has translated to control over claims handling, professional partners, stabilization and reduction of the cost of risk, risk management and loss control and ultimately, control over underwriting profits and investment income.

Having partnered with Brother's Inc. since 2002 on its P&C program, The Graham Company recognized the limitations Nolan faced with traditional insurance and therefore recommended its Group Captive. This strategic proactive approach put Nolan in the driver's seat of his business' profitability.

In a group captive, business owners assume a portion of their risk by taking large deductibles, as much as \$300,000 per occurrence. Unlike traditional insurance, where business owners pay a premium and let the carrier pay for the claim, members of the group captive are shareholders and are required to fund a large portion of the claim. "This is why it is critical that captive members operate as safely as possible – you have a vested interest to raise your safety standards and elevate your risk management game to a new level," added Mitchell.

MAKE IT A PROFIT CENTER

In a traditional insurance program, a full dollar is given to your carrier, regardless of how few claims you file. In a captive, approximately 40 cents of every dollar is put towards reinsurance costs and fixed expenses, while an impressive 60 cents of that dollar is invested offshore,

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# CAPTIVE 101: CONTROLLING YOUR DESTINY

BY ROGER LADDA, ASSISTANT VICE PRESIDENT  
INNOVATIVE CAPTIVE STRATEGIES, INC. (ICS)

## WHAT IS CAPTIVE INSURANCE?

A captive is an insurance company created with the specific objective of financing the risks of its owners/insureds.

## TYPES OF CAPTIVES

There are many types of captive insurance companies, including:

**Single Parent Captive** – This type of captive insures the risks of a single company. As a rule of thumb, single parent captives need to have at least \$2 million of premium to be viable.

**Rental Captive** – In a rental captive structure, participants “rent” a “cell,” or a portion of a captive, for their own use. Rental captives allow companies with eligible premiums of \$1 million or more to participate in a captive structure without having to set up their own.

**Group Captives** – When you don’t have enough premiums or separate sources of risk to qualify for a single parent or a rental captive, then group captives can be a good alternative. These captives are collectively owned by a group of companies, either homogenous (from the same industry) or heterogeneous (from a variety of industries). In this structure, members of the captive band together to provide primarily three types of insurance coverage: workers’ compensation, general liability and business automobile.

## CHARACTERISTICS OF CAPTIVE OWNERS/INSUREDS

Regardless of the size of their organization, captive owners/insureds should have:

- An entrepreneurial spirit
- A desire to take control
- Financial ability to take risk – at least \$250,000 per occurrence
- Commitment to loss control and safety improvement

## THE BENEFITS OF A CAPTIVE

### Greater control

- Professional partners are hand-selected by captive owners.
- Captive members control how their specific claims are managed.
- Loss control services are customized to meet members’ needs and reduce risk.

### Reduced overall costs

- Contributions are based on your company’s expected losses.
- Premiums are likely to be more stable from year to year.
- Members have the ability to retain investment earnings and underwriting profit.

### Improved stability

- Captives offer enhanced coverage, marketability and cost control.
- They provide a forum for the exchange of ideas, and members can learn from fellow members’ experiences.
- There are no surprises in the renewal process and there is no bidding upheaval.

## GROUP CAPTIVE STRUCTURE

The goal of a group captive is for each member to fund for expected losses to the greatest extent possible and to reinsure for the rare catastrophic loss. Losses falling within the captive retention, usually \$300,000 per occurrence, will be paid from the member’s funds from an actuarially established allowance for projected losses. Large losses exceeding the captive’s retention levels will be offset through the purchase of A-rated reinsurance and umbrella coverage.

In the event a member’s cumulative losses exceed their total loss allowances, these losses will be shared with other captive members by a pre-determined distribution methodology. Overall financial support is also provided by an A-rated insurance carrier that the captive will select to “front” the overall program.

## RETURNING PROFITS

Profits from a group captive are returned to the owners after a period of at least three years from inception of the insurance policy, which allows enough time for most claims to have been resolved. While owners are waiting for their profits, they are earning investment income on their premiums that have not been used to pay for losses. Not only do owners receive returns when their actual losses are less than the premiums paid to their loss funds, but they also earn investment income on those dollars. **G**

Roger Ladda, Assistant Vice President at ICS, can be reached by contacting Bill Selman, Vice President at The Graham Company, at 215-701-5233 or bselman@grahamco.com.

# ASK THE EXPERT

## KEVIN SMITH ON MAXIMIZING THE BENEFIT OF CAPTIVE INSURANCE

**Q:** How does participating in a captive insurance program affect my insurance coverage?



**A:** Oftentimes the traditional insurance market is not willing to

provide coverage for certain exposures related to your business. By participating in a captive, the insured takes on all or a significant part of the risks and uses reinsurance to supplement or provide excess coverage. For example, if you have an exposure to liability arising from mold or fungus, traditional markets might balk at providing coverage. In a single parent captive, you can decide to fund for the exposure in your captive. Group captives may allow for flexibility in including certain coverages that are common to all members.

**Q:** How can I protect my captive from multiple losses from a single event?

**A:** In any insurance program where you are insuring multiple lines of coverage, there is an exposure to one event causing a loss to more than one line of coverage, i.e., insuring workers’ compensation, general liability and automobile liability in the same captive program.

To illustrate, if one of your employees were involved in an automobile accident where they caused injuries to a third party and were also injured, there would likely be an automobile liability claim as well as a workers’ compensation claim. If you were retaining the first \$250,000 of each occurrence by line of coverage, you could be exposed to a loss of \$500,000 for this one event. Agreements with a reinsurance company can be structured with a “clash” deductible that would cap your exposure to claims under multiple lines of coverage to a more acceptable level. In this example, a clash deductible of \$300,000 would reduce the exposure to both a \$250,000 automobile deductible and a \$250,000 workers’ compensation deductible resulting from the same occurrence.

**About the Expert:** Kevin D. Smith, CPCU, ARM is a Vice President in the Technical Development Department and was involved in the formation of The Graham Company Group Captive. He can be reached at 215-701-5233 or ksmith@grahamco.com.

## FREEDOM IN CAPTIVITY CONTINUED

where it accrues over time and can be used to pay claims under your control. So if claims can be nearly eliminated, captive members get their underwriting profit back in the form of a dividend. In the meantime, the member gets a tax deduction for the full dollar in each policy year. “Now you’ve transformed insurance from one of your business’ most significant expenses to a profit center,” said Mitchell.

Nolan, who has been part of the Captive for seven years and has accrued over \$2 million offshore, said, “This money does not belong to the insurance company; it’s Gary Nolan’s money. I earned it so I’m going to control it.” While Nolan’s success is noteworthy, he admitted, “Insurance didn’t become a profit center overnight for me – this is the result of years of safety diligence.” Regardless of how safely you operate, Mitchell advised, “Joining a group captive is still a long-term decision. It runs in cycles and you can’t simply bail out in a soft market and jump back in when it hardens; but if you remain committed to your safety culture over the long term, your business will prosper.”

## RELY ON THE GROUP

“At the heart of Brother’s Inc., you’ll find that I’m just a hard-working contractor, not a savvy CFO, so while the Captive’s notion of control through superior risk management was appealing, I must admit that the responsibility of owning my own insurance company was initially overwhelming,” recalled Nolan. “But then I met the other members – CFOs, CEOs and entrepreneurs from diverse industries – that’s when it hit me; we’re not just members, we’re partners,” continued Nolan. As an adviser to The Graham Company’s Group Captive, Mitchell said, “There is an underwriting committee, a finance committee and a safety leadership committee within the Captive – all working together for the benefit of the group. But I believe the entrepreneurial spirit and the respect and information sharing between members is the most significant benefit to members.” Nolan wholeheartedly agreed, saying, “We don’t just share insurance insights; we share the same vision and passion for safety and other business practices. That’s what unifies us and makes us stronger.”

## EMBRACE EXCLUSIVITY

The financial success shared by members of The Graham Company’s Group Captive is attributed to the exclusivity of the group. Each new prospective member must pass The Graham Company’s rigorous underwriting criteria before the members will be presented to the Captive’s Underwriting Committee and then to the Captive’s Board of Directors for approval. Like each member, The Graham Company is also a stockholder in the Captive. “We share in the risk too and we only get one vote like every other member, so it’s in our best interest to select only the safest companies. Our members like knowing that we, as the ‘gate-keeper,’ have ‘skin in the game.’ That means we are all aligned,” said Mitchell.

Because the Captive is a real insurance company, and in order for members to get a full tax deduction for premiums paid into the Captive, there must be risk shifting and sharing. “Part of any group captive formula requires members to share in other members’ losses. But at the end of the day, you need to limit that as much as possible, so you need to keep it exclusive to members who share in your same safety culture. Otherwise, the captive

won’t be successful and profitable for its members,” explained Mitchell. As a result of its commitment to exclusivity, The Graham Company’s Group Captive has averaged less than one percent of risk sharing per year over the past nine years. So if you are paying \$1 million into the Captive, only \$5,000 is committed to risk sharing. In comparison, captives that have hundreds of members often have five to 15 percent of risk sharing per year. “Uncontrolled risk sharing like that can blow you out of the water, even if it’s not your loss,” warned Mitchell.

“As a founding member of the Captive, I can tell you that the mantra is ‘bigger is not better.’ We’re not going to allow a new member to join just because they meet the premium requirements; rather, a new member must make the collective group stronger,” said Nolan. “We are exclusive by design; the intimacy of the group allows each member to maintain control.” **G**

**If you have questions regarding how you can make a group captive work to your advantage, please contact Bill Selman, Vice President at The Graham Company, at 215-701-5233 or bselman@grahamco.com.**

**WE ARE EXCLUSIVE BY DESIGN; THE INTIMACY OF THE GROUP ALLOWS EACH MEMBER TO MAINTAIN CONTROL.**

life and disability coverage because the coverage has a low claim frequency and premiums are “reserved” until a claim needs to be paid. Today, most employee benefits captives are used by very large employers.

Although captives might not make sense for small to mid-size employers, they do have other options when it comes to financing their employee benefits risks. Employers can consider self-insurance, minimum premium

# GRAHAM SIGHTINGS

## EXPERTS IN THE NEWS

DAVE MERKER AND  
NASON CONSTRUCTION

• *Construction Executive:*  
January issue

MICHAEL MITCHELL  
AND BROTHER’S INC.

• *GBCA Construction Today:* Spring issue



## GRAHAM GIVES BACK

- The Graham Company started the first Corporate Kiwanis Club in the club’s 95-year history! Kiwanis is an organization that serves the needs of over 10 million underprivileged children around the world through community projects and leadership training.
- Employees of The Graham Company donated 38 coats to “Feel the Warmth,” a Philadelphia-based non-profit that provides winter jackets to families across the city.
- Over 120 gifts were donated by Graham Company employees to 30 children at The Red Cross shelter in Levittown, Pa.



## MOVERS & SHAKERS

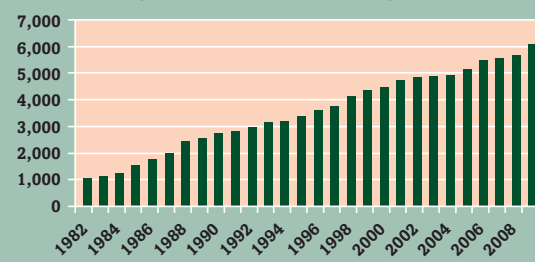
- The Graham Company placed 4th in the *Central Penn Business Journal’s* 2009 Best Places to Work in Pennsylvania, a competition that included over 15,000 businesses across the state. This is a significant distinction because it shows The Graham Company’s ongoing commitment to empowering employees and an unwavering dedication to the well-being and happiness of all employees.
- The Graham Company was awarded the PAR Excellence Award for 2009 from Assurex Global in recognition of its outstanding Quality Management achievements. It is the 16th time the firm has won this prestigious award!

and participating contracts. Many of these alternative funding methods are a better fit for managing benefits risks, but can provide some of the same advantages of a benefits captive, including sharing in a favorable experience and improved cash flow.

**If you have questions regarding benefits captives or other alternative methods to finance benefits, please contact Joseph McGinty, Vice President at The Graham Company, at 215-701-5292 or jmcginty@grahamco.com.**

# STAGGERING STATISTICS

Captive insurance has been around for nearly 60 years, and its growth over that time period is a striking indication of just how successful this non-traditional approach can be. There were 1,000 captives in 1982 and today over 6,000 exist. Captives have continued to prove the test of time, growing in both hard and soft insurance markets and through economic cycles. There are a total of 70 worldwide domiciles that authorize/regulate the formation of captives.



Source: Captive Insurance Company Directory

# BENEFITS BRIEF

Captives can be used for employee benefit plans, too! In 2000, the Department of Labor (DOL) ruled to allow the formation of employee benefits captives. In order to get them up and running, employers must meet the requirements of state insurance regulators and get approval from the DOL. The most common benefit plans put into a captive are