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Should you consider a captive insurance firm?

By: Tony Martin

In light of the current economic trends, business owners are wise to consider all avenues of maintaining profitability. Over the past number of years, there has been a consistent increase in regulatory requirements, tax impact and price pressure on the majority of businesses in the marketplace. A Captive Insurance Company may be a good option that helps provide an offsetting positive impact in the right situation.

So what is a captive insurance company?

It is a special purpose insurance company formed primarily to underwrite the risks of a specific company and it is wholly owned by the parent company or its owners. A captive has very similar features to a traditional insurance company. It is a licensed insurance company that writes policies for the risks it chooses to underwrite, sets premiums for those policies, collects premium and pays out claims.

However, the main difference between a captive insurance company and a traditional insurance company is that a captive cannot sell insurance to the general public. Another benefit is they typically provide broader coverage and can be designed specifically to cover the exact needs of the insured.
There are multiple types of captive insurance companies including but not limited to group, association, single parent, and cell captives. Each captive is designed to cover a specific set of risks that may supplement the businesses existing risk management strategy or replace a part of it.

The best use of a captive should be evaluated to determine how to fit it in to the existing risk management program and the businesses strategy.

Captives are complex structures that are highly regulated by federal, state and insurance agencies. As such, they should be created and managed by experts. To properly evaluate, implement and manage a captive program requires a team approach including the captive manager, attorney, accountant and business adviser. If you already have a captive, a routine evaluation of its use and integration with the business to determine if the efficiency is being maximized is highly recommended.

Due to the potential benefits, a captive should be considered as part of a business's overall risk management strategy when the business begins generating revenue of $10 million a year or more. Of course, this marker is a suggestion and not a rule. Captives are not a fit for all businesses and should be carefully considered before implementation. However, when a captive is a fit the benefits to the business can be substantial.

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