

Alternatives to Financing Risk within Large Deductibles

Challenge

A major, privately held U.S. construction company with a proactive risk management philosophy and an excellent safety record took high deductibles on all of its casualty lines of business. Financial strength and safety focus put the company in a good position to reduce its commercial insurance purchases and use alternative risk financing solutions. Retention of risk with large deductibles often arises in response to the commercial insurance industry cycles that lead to periodic unavailability or unaffordability of liability coverage for developers and construction companies. Construction defect coverage is often retained because commercial insurance carriers often exclude this exposure from the general liability policy due to its unpredictability and potentially catastrophic loss nature.

Goal

The goal was to buy down current deductibles and provide construction defect coverage to protect the insured from the unpredictability of both the insurance industry cycles and their loss exposures.

Solution

The solution was to establish a captive insurance company with a “Beneficial Ownership” structure. The insured determined that a captive would be an efficient alternative risk vehicle to buy down its current deductibles. The objective of the captive was to provide protection from the variability in loss experience within their large deductibles. Then the captive issued a corporate reimbursement policy that included coverage for construction defect claims. In the first year of operation, the captive limited the amount of risk retained by placing a basket aggregate limit on its policy.

Benefits

- ✓ Fixed predictable premium
- ✓ Family ownership structure
- ✓ First year basket aggregate limit
- ✓ Potential future surplus distributions

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