4. (2 points)

   Consider the following companies seeking insurance coverage. For each scenario, recommend the optimal way to manage the insurance risk and describe the rationale.

   a. (1 point)

      Company A is a large corporation seeking to reduce its insurance costs. It has a dedicated risk manager and can be described as a large, stable insurance risk. It has loss carry-forwards from prior tax years.

   b. (1 point)

      Company B has been in operation for two years and currently operates in several states. It is having difficulty obtaining liability insurance coverage and is interested in partnering with companies with similar operations.

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| QUESTION 4 | |
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| **TOTAL POINT VALUE: 2** | **LEARNING OBJECTIVE: A3** |
| **SAMPLE ANSWERS** | |
| **Part a:** 1 point | |
| Optimal solution:<br>• Company A should take on more insurance risk (or move towards self-insuring) and maintain a high retention or fronting.<br>• One of (or combination of) the following:<br>  • Company A should start a captive with relatively high retained limits/Reinsurance<br>  • Company A should use Surplus/Non-admitted lines at relatively high retained limits<br>  • Company A should use General Insurer with relatively high retained limits<br>  • Company A should seek large deductible plan/high excess reinsurance and insurance will protect company against catastrophic claims.<br>Rationale (any one of the following):<br>• Company A will gain tax benefits from a captive and will be able to manage the risk better and can avoid needing to pay profit load and other expenses to an insurer.<br>• Company A can save cost through captive's favorable tax benefits and significant reduction of insurer's profit load and expenses (commissions, brokerage, marketing costs etc.)<br>• Company A saves cost through effective risk management plans such as claims control/safety program and avoid paying profit loads and expenses to insurer<br>• Large and stable company will result in predictable losses and hence can determine where to attach the high retention limit. A dedicated risk manager can put in place effective risk controls and there will be no need to pay profit loads for retained exposure. | |
| **Part b:** 1 point | |
| Optimal solution:<br>• It should start or join an RRG with companies having similar operations OR heterogeneous companies are not allowed in RRGs<br>• Company B joins RRG and pool or spread like or liability risks with other companies<br>Rationale (any one of the following):<br>• Company B won't meet seasoning requirements, so likely won't be able to form a captive<br>• RRG provides liability coverage and allows Company B to be licensed in the domiciled states but operate in multiple registered states<br>• RRG allows affordable and available liability coverage. Pool members will obtain tailored coverage, have incentive to control cost and have adequate pricing/reserves due to lack of guaranty funds and will avoid paying profit loads and other expenses to third party insurers<br>• RRG was purposely established to solve liability coverage problems and eliminates contradictory and redundancy of licensing in every state while providing the ability to operate in multiple states | |
| **EXAMINER'S REPORT** | |
| Candidates were expected to identify key insurance issues within the question and suggest logical insurance solutions that were supported with reasonable rationales. | |
| **Part a** | |
| Candidates were expected to demonstrate a plan for which the company assumes significant risk | |

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| and seek insurance at a high limit. Common errors included:<br>• Mentioning they will insure through captives/surplus lines/insurer without stating the extent of risk the company will assume and how the company will be protected from catastrophic losses<br>• Listing the benefits of the proposed plans without explanation<br>• Not explaining how the plan will lead to significant reductions of profit load and other expenses<br>• Leaving out part of the plan dealing with insuring excess losses at high limit to cover catastrophic losses<br>• Not explaining how Company A's risk manager will help with cost savings<br>• Not mentioning how the reduced insurance cost will be attained<br>• Not explaining where the cost savings from the plan was coming from |
| **Part b** |
| Most candidates provided a logical plan with reasonable support. Candidates were expected to describe a reasonable plan that is suitable for the outlined conditions (very young company, operations in multiple states, difficulty finding liability coverage). Common errors included:<br>• Stating that the company can pool risks without explaining the type of pooling<br>• Confusing captives and RRGs or not demonstrating knowledge of which might be the best fit for this situation<br>• Not describing how liability coverage or availability will be improved<br>• Failing to discuss simplified regulatory requirements |