

# SCCIA

## Fifth Annual Executive Educational Conference USING CAPTIVES FOR EMPLOYEE BENEFITS

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# Milliman

*Consultants and Actuaries*

# Session Overview

- **Why are employers using their captive for employee benefits?**
- **Who has done it so far?**
- **How have the existing transactions been structured?**
- **What are the primary issues that employers need to evaluate?**
- **How do you make it happen?**
- **What does the future hold?**



# Why Use A Captive for Employee Benefits

- **Reduced insurance expenses**
  - Commissions
  - Risk Charge
- **Cash flow management**
  - Investment Control
  - Rate of Return
- **More efficient use of capital**
  - Synergy with Other Risks in Captive
  - Generally Independent from Property and Casualty Risks
- **The ability to develop custom insurance programs not available in the commercial market**
- **Possible tax efficiencies**

(Same reasons for forming a captive in the first place)



# Sources of Savings

(relative to fully insured plans)

## ➤ **Savings:**

- Lower risk charges and capital charges
- Reduced margin on expected claim charges (Pricing margin)
- Lower expense charges
- Higher investment income (and control of reserves)
- Possibly lower premium taxes
- Possible income tax savings
- Self Insured – Accelerate deduction of reserves
- Broker commissions

## ➤ **Offset by:**

- Fronting fees
- Captive management fees
- Other captive operating costs
- Opportunity cost of capital



# Employee Benefits to Consider

- **Group Term Life (Basic Life Plan)**
- **AD&D (Often Linked with Basic Life)**
- **Supplemental/Optional Life (Dependent Life)**
- **Group Disability (LTD and STD)**
- **Retiree Medical**
- **Defined Benefit Pensions**
- **Group Medical Plan (Active Employees)**

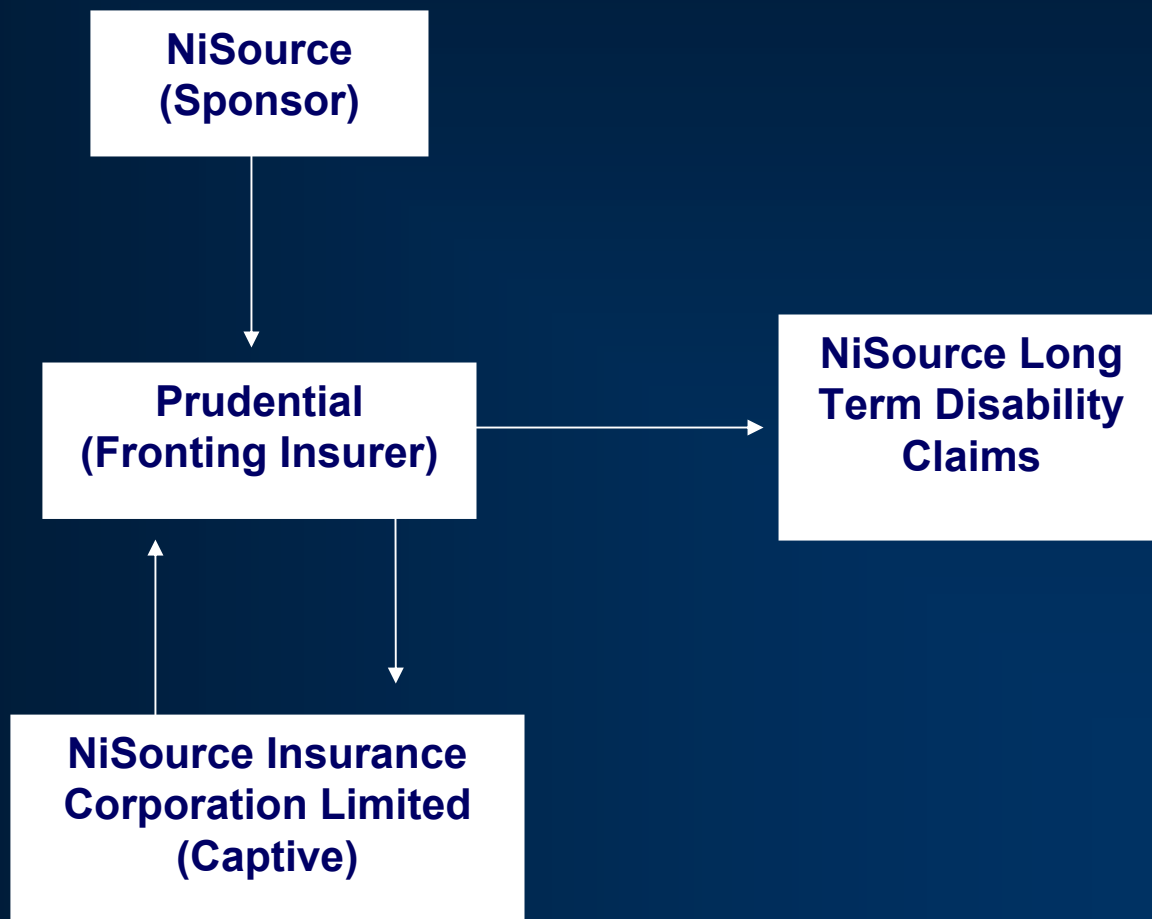


# Who has done it so far?

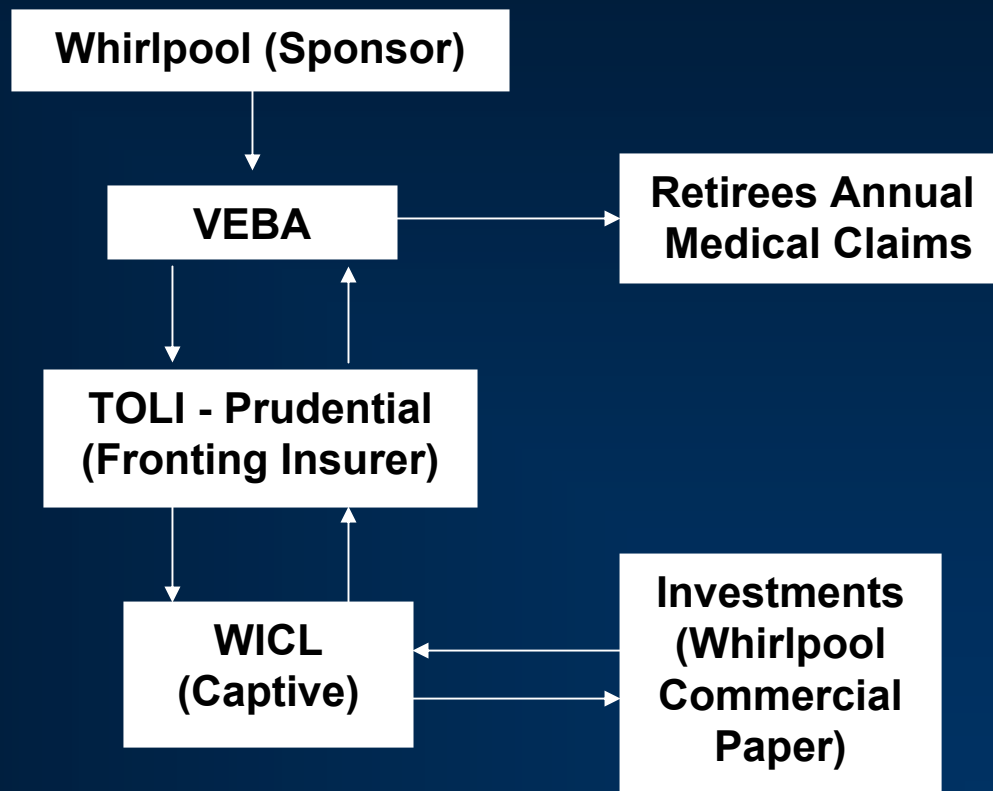
- **Columbia Energy (NiSource)**
  - Benefits Covered: LTD
  - Fronting Carrier: Prudential
- **Archer Daniels Midland (ADM)**
  - Benefits Covered: Basic and Supplemental Life
  - Fronting Carrier: Minnesota Life
- **International Paper**
  - Benefits Covered: Life and AD&D
  - Fronting Carrier: Met Life
- **SCA**
  - Benefits Covered: LTD, AD&D, Basic and Supplemental Life
  - Fronting Carrier: Aetna
- **Alcon**
  - Benefits Covered: Life and LTD
  - Fronting Carrier: Aetna
- **Alcoa**
  - Benefits Covered: Group Term Life
  - Fronting Carrier: Met Life



# Columbia Energy Structure of Transaction



# Whirlpool Structure of Transaction



**Whirlpool filed this approach with the DOL and then subsequently withdrew their filing**



# Making It Happen

- **Pre-feasibility study- Get support of internal parties such as Risk Management and HR**
- **Conduct a feasibility study (cost/benefit analysis)**
- **Discuss with captive manager (Engage a manager)**
- **Engage a lawyer**
- **Engage an independent fiduciary**
- **Get branch approved in US – domiciled jurisdiction if not a US captive (Meet with regulators)**
- **Negotiate contract with highly rated fronting insurance company**
- **File for PTE with the DOL and implement plan**



# What are the Requirements?

- **The DOL set the following requirements to protect the rights of the plan participants:**
  - **Requirements for the captive**
    - **“Party in interest”**
    - **Domestic license**
    - **Certificate of Authority (never revoked nor suspended)**
    - **Audit or financial examination**
    - **Reserves**
  - **Other Requirements**
    - **Reasonable premiums**
    - **No commissions**
    - **Enhanced benefits**
    - **Typical premium calculation methodology**
    - **Highly rated fronting insurer**
    - **Indemnity reinsurance only**



# What does the future hold?

- **More mainstream**
- **More examples for ExPro filings (different approaches being filed now)**
- **Continued pressure to lower benefit costs**
- **More efficient enterprise risk management**
- **Rules becoming clearer**
- **Less “radical” an approach**



# Have Questions?

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