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INSURANCE SERVICES

DEMYSTIFYING SELF-INSURANCE

WHY SELF INSURANCE?

A chain of Canadian casinos provides the ideal customer experience. From arrival to departure, guests are guaranteed satisfaction. Their rooms are well-serviced, table workers are briefed on etiquette, and the front desk and concierge are supremely helpful. Casino management has done everything to provide an exceptional stay for its clients, but it has been unable to prevent the slips, falls, twists, and thuds that create a high volume of low-severity insurance claims.

The casino's primary concern with these low-severity claims was the inevitable loss of control over the customer's experience. The casino reported all incidents to its insurance provider, who would then manage the claims until completion. The casino's customers were put in a situation that reflected on the casino's brand, but without the casino having any influence on the customer's treatment. Other times, casino employees suspected claims could be mitigated through a free night in its adjoining hotel or a dinner at its restaurant. But, because there was a standard procedure in place for all claims, the casino could not benefit from the judgement of its employees.

A lack of control meant the casino could not offer any insight into incidents it deemed suspicious. There were numerous claims that the casino's employees suspected to be fraudulent, but were paid out. Although the insurance company's adjusters were thorough in their information-gathering, they were not in as good a position to recognize fraudulent claims. The casino was left to think claims were settled based on economic decisions intended to avoid costs to the insurance company. Moreover, the casino believed the payout of fraudulent claims was resulting in unnecessarily high insurance premiums.

Ultimately, the casino felt it would benefit from increased input over the management of claims. Consequently, it was looking for an insurance solution that could deal with incidents and claims accurately, and with the casino's interests in mind. As a solution, the Canadian casino chain looked into the merits of self-insurance.

They identified that, as a large company dealing with a high volume of low severity claims, they were an ideal fit for self-insurance. With the help of a broker and Third

Party Administrator (TPA) the casino was able to self insure what their broker termed the "working layer" of their liability limit (i.e., the layer where the majority of their claims activity occurred). The organization first noticed the money they were able to save on premiums due to the significant credit obtained by retaining the risk for this working layer. The risk of large or catastrophic claims was transferred to the insurer to ensure they would be protected in the event of a major incident.

After a year of being self insured the casino was pleased with their ability to control their claims process. By personalizing their claims they were able to better reflect their customer service oriented brand. The insurance company had a different set of priorities and therefore was not always able to protect the casinos brand image. Now, because the casino controls the process, they have the opportunity to make life long customers by making the claims process a positive experience.

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WHAT IS SELF INSURANCE?

Self insurance is a risk management strategy that sees a company manage its own risk up to a set dollar value. The company creates and manages a fund from which they can pull resources to cover low severity, high frequency claims. By controlling the process, the self insuring company gains a transparent view of their claims, gains full control of their customer's experience, maintains and owns their loss experience information, and retains the interest created from their fund.

Understanding frequency and severity

A good candidate for self insurance will be involved in high frequency of low severity claims, while low frequency, high severity claims are almost always left to insurance companies.

High frequency, low severity

- These include small personal injuries, like slip and falls or a twisted ankle. The claim from these incidents will be low in severity and will require small amounts in compensation. If not dealt with efficiently the administrative costs can end up being greater than the payout.

Low frequency, high severity

- Significant bodily injuries or property damages are low frequency, high severity events. These claims are generally beyond the level of risk an organization is able to manage. However, when insurers only need to cover an organization's low frequency risk, premiums are significantly reduced.

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Where's the money?

The self insuring organization controls their money. To self insure, an organization will create a fund from which they are able to pay claims. The need to pay premiums to an insurer to cover the "working layer" is eliminated because the organization manages their low severity risk. So, if an incident becomes a claim, the organization will use the money in their fund to pay the claimant and resolve the issue.

To determine the size of fund needed, a retention analysis must be done. This process determines the appropriate amount per claim the organization will be comfortable retaining, and the amount that must be deposited in the claims fund. This analysis is typically undertaken by an actuarial consultant, who will review past loss history to analyze and assess risk, then suggest a sufficient amount to cover it.

Where's the management?

When an organization is responsible for their own risk it is important they understand their claims process. There are services to help, and many organizations choose to utilize a third party administrator. Third party administrators (TPA) understand claims services and risk management, and can professionally manage and control an organization's claims process.

Alternatively, some organizations manage the process on their own, creating a department capable of understanding the group's risk, customers, and claim needs.

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Where's the savings?

Under this program, companies benefit from cost-savings because the process of retaining risk, calculating risk, and paying resulting claims internally is cheaper than paying a commercial insurer. The frictional cost of an insurer handling a large number of low severity claims and processing incidents is greatly reduced. Furthermore, because the fund used to pay claims is controlled by the self insured company, any interest accrued will benefit the company.

Self insurance also gives the company full control of its risk. The organization exerts greater control over which claims are paid out, which are defended, and which are denied. By focusing on serious claims, or dealing with less serious claims in a creative way, an organization can save significantly. To help with this process, experienced third party administrators will work with clients to ensure claims are dealt with expediently, and less serious incidents do not eat up resources. The process becomes streamlined with the organization's goals in mind.

The Bottom Line

Organizations that self insure still use insurance companies to cover low frequency, high severity risk. The risk associated with a devastating liability claim is too great for an organization to cover on its own. By self insuring an organization raise the amount of risk they will retain to upwards of $50,000 per claim, and manages less expensive risk itself.

Organizations can manage how their customers are treated and can make critical decisions on setting reserves, investigations, and settlements.

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ARE YOU A CANDIDATE FOR SELF-INSURANCE?

Not every organization will benefit from self-insurance. Small companies, and companies not dealing with a large number of low severity claims, will not see sufficient benefits. Ideal candidates are large, commercial enterprises that have a high frequency of low severity claims.

First, the organization must have the finances to set up a fund that will cover their risk. Second, only large organizations see the high volume of claims that make the switch to self insurance beneficial.

Organizations with a large number of people moving through their establishments on a daily basis are best suited for this program. Examples of these include:

- Retail operations with multiple locations
  (e.g., Best Buy, Future Shop, Shaw, Sears, etc.)
- Hotels (e.g., Westin, Sheraton)
- Hospitality (e.g., Tim Hortons, Wendy's)
- Transportation (e.g., airports, airlines, trains)
- Resort hospitality
- Casinos

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Be sure

An organization might seem to fit the bill for self insurance, but the only way to be sure is to undergo a detailed cost-benefit analysis. This process involves:

Accurately understanding three prior years of loss history.

- This information should be available from your insurance company. The aid of a broker will often speed up the process.

Doing a total cost of risk analysis.

- It's important to understand how much money you will need to cover your risk.

Undergoing a retention analysis.

- The amount that needs to be set aside for a retention can be understood through actuarial science and the law of large numbers. There are services to help organizations through this process, and knowing the right amount to put away is important.

Know the market

Even if your organization is a perfect fit for self insurance, there are other factors to consider. During a soft market, when insurers are fighting for your business, premiums will be low and remaining under the wing of an insurance company might make the most financial sense. When the market is hard, and insurance premiums are high, self insurance becomes more attractive. Awareness of the insurance market will help you make an informed decision.

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How can I know?

Third party administrators, knowledgeable brokers, and educated risk managers, understand the benefits and risks that surround self insurance. Only after consulting with these experts can an organization understand whether a switch to self insurance is best.

BENEFITS OF SELF-INSURANCE

If an organization is a good candidate, self-insurance offers many benefits.

Tangible benefits

Cost savings

When an organization self insures it is responsible for managing its claims. Self management presents many benefits:

1) The adjuster can *deal with cases immediately.* Because adjusters have access to the organization's fund they can quickly write a cheque to a claimant without unnecessary and costly paperwork. Claims are solved faster because bureaucracy is avoided.

2) The organization is able to *collect accruing interest* instead of paying monthly premiums. The organization enjoys this benefit because their reserve fund is under their control.

3) *Commercial premiums are lower* because the company is self-insuring a portion of the risk. Because the insurance company only deals with claims over a certain amount, it charges the organization less premiums.

4) Insurance companies *appreciate organizations that self insure* because it cuts down on the administrative process and paper work involved with high frequency, low severity claims.

Cost savings are a huge and readily identifiable benefit of a well tailored self insurance plan, but it doesn't represent the only benefit. Increased control over the claims process offers organizations a number of benefits.

1) Self insured organizations *exert direct control over claims they wish to defend.* Insurance companies decide some claims based strictly on economic factors. While this is effective in most cases, certain times a company must draw a line in the sand to defend against becoming a target for questionable claims in the future. By controlling claims, corporations are empowered to spend what they see fit to protect themselves.

2) The company can *protect itself against fraudulent claims*. If a company employee is suspicious, or aware, of a fraudulent claim, they can quickly and easily initiate an investigation.

To better understand how added control can be of great benefit to an organization, consider the following example:

> *The store manager of a large restaurant chain is called to the front of the store where an individual is complaining about injuring himself in a slip and fall. The individual repeatedly, aggressively, demands to be compensated and the store manager has no real grounds to deny the claim. The incident is tracked and sent to the claims department, along with a note of suspicion from the manager. When the incident arrives at claims it shows that the restaurant has seen three previous claims from the same individual, all slip and falls. Because the organization is self insured and has access to all their previous claims data they can identify possible fraud easier. When fraud is suspected, they can then choose to fight the cases to prevent repeated claims in the future. The organization is even empowered to choose their own legal representation to defend their case.*

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Intangible benefits

While cost-savings are the obvious benefit to self insuring, companies will find it's the intangible benefits that can end up being most valuable.

1) *Protect risk to brand equity*. The brand that a company establishes can be destroyed by one negative customer experience. When self insuring, adjusters can be trained to interact with claimants in a way that is consistent with company messaging, providing a positive brand experience from your organization.

2) The claims process is an *opportunity for companies to win back the customer*. By making the claims process a positive experience, customers leave feeling respected and dignified. Claims processes can be customized for the company so claimants don't feel like a number.

3) When a company manages its claims, or has a third party administrator handle them, they enjoy *transparency around their outstanding claims*. Business owners will be aware of their exposures, and thus able to make informed business decisions. For example, if a company knows it has three large claims out, all of which will total $50,000, they can make wise decisions around accruing other, potentially costly, risks until their outstanding claims are dealt with. Third party administrators are proficient at communicating the exposures a company has at any given time.

The intangible benefits can be very rewarding for organizations. In the example of the Canadian casino chain, because they took over their claims services by self insuring, they now maintain a high level of customer service throughout their business. Furthermore, in cases where monetary compensation is not required, the owners can assuage customer concerns by providing alternate benefits.

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Sometimes an extra night of accommodations or a free meal at a restaurant is all it takes to appease a potential claimant.

Organizations work hard and spend significant resources on creating a positive, respected brand. By self insuring they control how that brand is treated.

LEARN MORE ABOUT SELF-INSURANCE

To learn more about self insurance get in touch with your broker or a third party administrator. SCM, a full service third party administrator, offers a host of experience to satisfy client needs. By utilizing SCM's full suite of services, ranging from risk management, digital claims collection systems, and full service claims support, companies can be confident that their self insurance program is in trusted hands.

More information about self-insurance is available on the following websites:

http://www.scm.ca/

http://www.scm.ca/SCM-SelfInsurance-CaseStudy.pdf

http://www.canadianunderwriter.ca/

SPECIAL THANKS TO:

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