PREMIUM SAVINGS NOW, CAN COST YOU LATER

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In these difficult economic times, many companies have acted to reduce their insurance costs by participating in trade association programs or self-insuring in ways intended to achieve premium savings. These savings, however, can sometimes be difficult to verify. Moreover, the insurance arrangements are not always free from risk, and premium savings can rapidly dissipate if litigation or other problems ensue.

Trade groups often form relationships with insurers and brokers in an effort to provide a benefit to their members. These relationships are very common, and they can be a valuable asset to the group's members. For instance, the trade group's members might receive a discount if they participate in, and purchase insurance through, the group's program. The concept is straightforward, but the reality can become quite complex.

A business should take a close look at the premium savings that will realistically be achieved from participating in such programs. In many instances, the complexity of the programs obscure whether premium savings will occur. For instance, insurers commonly market programs based on the dividends that will be paid to participants. These dividends are paid at the discretion of the insurer, and the savings are therefore subject to debate. It is also common for insurers to impose restrictions on the dividends that may be paid, and the restrictions may be "buried" beneath several layers of documentation. A business should carefully examine the program documentation and consider whether the potential savings justify participation.

Risk retention groups ("RRGs") are another mechanism for achieving premium savings and other benefits. Essentially, an RRG is a form of self-insurance in which a group of companies provide their own insurance by establishing their own premiums and reserves. RRGs work well, and they are certainly an option for many companies. They are not, however, a cure-all. In the event of a serious claim, an RRG member will likely pay more than a business insured through a traditional insurer. RRG members need to closely monitor who they admit to the group and carefully scrutinize the members' claims histories. It is important for a company to be actively involved. If a business cannot (or will not) be actively involved, then an RRG may not be a good option.

RRGs have also begun to act more like traditional insurers in that they market their products to non-members through a trade association or other outlet. These non-members have no control over the RRG's decision-making or operations. While an RRG may be a great choice for its members, the RRG may not be such a great option for non-members. A non-member will not have control over the admission of new members or setting of premiums. It may, therefore, suffer adverse consequences because of decisions made by others.

RRGs differ from traditional insurers in many ways. For example, a company purchasing insurance through a traditional carrier will be covered by the state's guaranty association in the event the insurer becomes insolvent. A company purchasing insurance through an RRG will not be covered by the guaranty association. The policy forms issued by a traditional insurer will also be scrutinized by the state's insurance department. The policy forms issued by an RRG, on the other hand, are often not subject to such scrutiny. These may be perfectly acceptable trade-offs for an RRG member. For a non-member, the calculus may be different.

Insurance is a highly regulated field, and the complexity of alternative insurance arrangements can create problems for companies seeking premium savings. For example, a company or trade association may expect to receive some sort of benefit or payment which is not fully evident from a review of the program's literature. However, Pennsylvania law prohibits the payment of undisclosed "rebates" of any kind and provides for severe sanctions. Rebates include all manner of inducements or benefits. It is therefore important that any rebate, discount, or other benefit be clearly disclosed in the policies issued. The search for premium savings may also lead a company or trade group to engage in activities resembling those of an insurance broker. Generally, a company can perform many insurance related functions without obtaining a broker license. However, a good broker can bring real value to a transaction and should not be overlooked. Furthermore, if a company or trade group receives a fee or other benefit tied to the sale of insurance, then it is potentially acting as an unlicensed broker or "producer." It will therefore need to obtain a producer license, and failure to obtain the required license can result in criminal penalties.

Alternative insurance arrangements can result in substantial savings, but businesses and their trade groups need to have realistic expectations. They should be as informed as possible about the actual benefits to be achieved through these arrangements. The promises of substantial savings may not bear out under close scrutiny. Moreover, the sale of insurance is a highly regulated activity. If a business or its trade group is unaware of the regulatory hurdles, then the expected premium savings may rapidly dissipate in a cloud of litigation, fines, and penalties.