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What is a Captive?

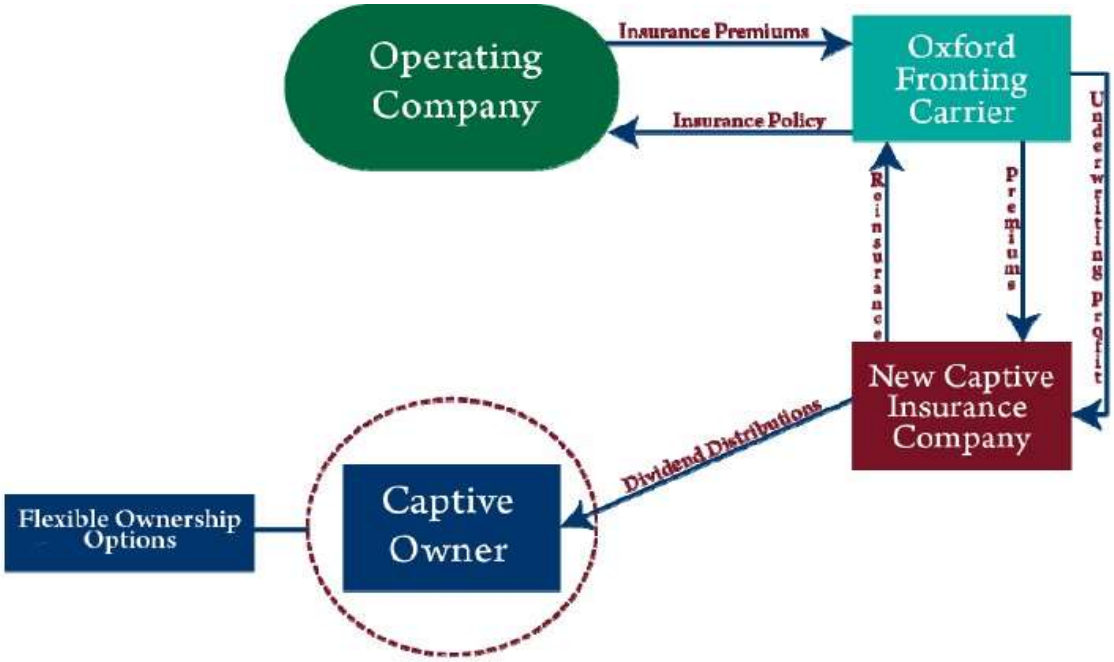
A captive insurance company is a property and casualty insurance company that is established to provide coverage primarily to a Parent Operating Company. Captives are an effective risk management strategy to insure against risks for which commercial insurance is not available or may be too expensive. Examples of exposures often incorporated in captive insurance arrangements include enterprise risks such as business interruption resulting in loss of income due to: breach/release of data, deductible reimbursement, defense cost reimbursement, loss of licensure, legislative and regulatory changes, loss of franchise, reputational risk, supplier/supply chain interruption, etc. Many operating companies face losses from these low frequency/high liability risks, which can be better managed through coverage from a captive insurance company rather than self-insuring. A policy issued by the captive insurance company will have the features and coverages drafted to meet the specific risks unique to your business.

Are Captives New?

Captive insurance companies are not new. In fact, most Fortune 500 companies have their own captives, organized and regulated in various domestic and offshore domiciles. Today, the majority of domestic domiciles offer specialized statutes for captive planning, which thousands of small to mid-size companies have utilized to more effectively manage corporate risks. Congress passed laws dating back to 2001 and the Internal Revenue Service has issued guidelines for captive insurance companies dating back to 2002. The captive insurance company must be properly organized, operate for bona fide business purpose and demonstrate both risk shifting and risk distribution in order for the arrangement to meet the requirements to qualify as insurance in the commonly accepted sense. Adherence to all known guidance is essential in order for this risk management tool to commence business with predictable results and maintain Federal, State and Insurance regulatory compliance.

How Do They Work?

There are different types of captive insurance arrangements in the marketplace today. Small to mid-size companies often elect to have their captive insurance company taxed according to IRC Section 831(b). This code section states that captive insurance companies are taxed only on their investment income, and do not pay income taxes on the premiums they collect, provided premiums to the captive do not exceed $2.3M per year starting 2017. This important provision aids the captive in the ability to quickly build up insurance company profits (called surplus) year to year increasing the capacity to pay claims.



Over the years, as the captive generates profit, after adjustment for expenses and claims, those dollars belong to the captive, not a third party insurance company. The profit and surplus may be invested in a reasonable manner, often accumulating excess reserves over time. Subject to regulatory approval, distributions to the owner(s) of the captive insurance company are generally treated as qualifying dividends. Upon liquidation or sale of a captive insurance company, distributions may qualify as long- term capital gains.

It is important for the captive to maintain appropriate liquid reserves in order to pay expenses and meet potential claims liabilities. Therefore, captive insurance companies need to have a well-designed, disciplined investment policy statement in order to maintain sufficient liquidity and long term growth objectives as a regulated entity.

How do I set up a Captive?

Establishing a captive involves many steps that must be orchestrated to achieve a successful result. During your initial consultation with U.S. Captive, we will work with you and your advisors to determine if a captive insurance program is appropriate based on your business economics and risk liability circumstance. U.S. Captive does not charge for this initial analysis.

Upon engagement, U.S. Captive will work with you to perform a more in-depth review of your unique fact pattern to determine risks appropriate for your company. Our underwriting team will conduct a review of your existing property and casualty policies and consult with your existing insurance broker to uncover additional lines of coverage which may be insured through the captive insurance company. This thorough review process will often include consultation with an independent risk management advisory firm and engagement of an independent actuarial firm to perform additional critical analysis and underwriting.

The U.S. Captive team will then manage all aspects of the process, including selection of the domicile best suited for your insurance structure, submission to the insurance regulatory team in that jurisdiction, final approval and ongoing management.