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Employee benefits & people risk:

A growing role for risk managers

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CONTENTS

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Introduction	3
Benefits trends	4
Ditching the silos	5
Changing roles	7
Risk financing	9
Funding benefits	10
Client needs	14
Global programmes	15
Case studies	17

EMPLOYEE BENEFITS AND PEOPLE RISK: A GROWING ROLE FOR RISK MANAGERS

AWARENESS OF PEOPLE RISKS IS INCREASING. WHETHER IT IS THE loss of top talent, a poor safety culture or corporate misconduct, such risks can be as devastating to a business as a large fire or a flood. Yet the management of people risk is arguably a far less developed discipline than it is for property/casualty exposures.

But this is likely to change. People are becoming recognised as a critical asset in today's knowledge-based economy, while there has been growing interest in the role of behavioural and cultural risks in company failures. And as companies seek efficiencies, and with the implementation of enterprise risk management (ERM), many are now taking a more holistic view risk, including people.

This all points to an opportunity for risk managers, who can lend their skills to human resources, identifying risks and cooperating with human resources (HR) to use employee benefits, insurance and HR tools—like wellness programmes—to manage people risks.

One area where risk managers are already making a difference, and forging relationships with HR, is in the area of insured employee benefits. Unlike property/casualty insurance, benefits are traditionally managed and placed locally, but rising costs have seen many multinational companies look to centralise their employee benefits programmes, increasing control and finding efficiencies.

Risk managers are being asked to collaborate with HR on new employee benefits financing solutions, and many have found significant cost savings through programme rationalisation, consolidated purchasing and the use of captives.

Although numbers remain relatively small, there is growing interest in using captives to self-insure employee benefits; and insurers, networks and brokers are having to respond with an improved offering. The latest development being the launch of global employee benefits programmes—a key area to watch in coming years.

Employee benefits and people risk are emerging areas for risk managers, but they are areas where they can add value. The profession and vendors are at the start of what might be a long journey. But there is a definite direction of travel.

**Stuart Collins,
Report Author**

BENEFIT TRENDS: Rising costs drive new risk financing approaches

EMPLOYEE BENEFITS ARE KEY to managing risks such as talent and the ageing workforce, yet the costs of insured benefits is rising, forcing multinational companies to seek new solutions.

Insured employee benefits, such as life, disability and medical insurance are a significant cost for multinational and large organisations, but they are also a useful tool for attracting and retaining talent.

Employee benefits are becoming of much greater importance for corporates, according to Wendy Liu, head of Zurich Global Employee Benefits Solutions at Zurich Insurance Company.

"Organisations are increasingly concerned with the acquisition and retention of talent. At the same time, we are also seeing a widening of the income protection gap, with the responsibility for providing benefits and managing the gap moving from government to corporations," she says.

While there are a number of trends shaping employee benefits strategies, rising costs are a recurring theme. A company with more than 50,000 employees can easily spend some $50m a year on insured employee benefits, and as much as $100m if a large number of employees are based in the US, according to Willis Towers Watson.

And the cost of benefits is increasing. Medical inflation is running at an annual average of about 8% globally, and as high as 40%-50% in some Latin American countries, according to the broker and consultant.

"In recent years there has been increased awareness at an executive level of the cost of pension benefits. Now we see an emerging awareness of the significant costs associated with other benefits, in particular medical benefits and long-term disability," says Roger Beech, senior consultant at Willis Towers Watson.

"Rising medical inflation—which can be seen in programmes in Singapore, China and Russia—is being combined with more savvy consumers. Employees are more aware of benefits and know how to use them, for example, to access branded drugs or better treatments," he adds.

In addition to rising medical costs, long-term disability is an increasing issue for companies. If a young employee suffers a severe disability, a company disability plan could face 40 years or more of significant cost.

"Long-term disability is a massive tail risk with much uncertainty. As a result, some companies are looking to cap benefits to a maximum number of years and then pay a lump sum," says Mr Beech.

Centralisation

The role of benefits in the 'war for talent', and the growing cost of providing insured benefits, is coinciding with another trend in human resources and employee benefits.

Recent years have seen a general rationalisation of corporate operations, as companies look for efficiencies and improved governance. As a result, most companies have centralised key internal functions and services.

HR, which has historically been largely locally focused, is increasingly being drawn into the corporate centre. And as costs have risen, many companies have looked to gain more central oversight and control over employee benefits.

"While historically employee benefits have been controlled locally, many companies now want to have a central overview of employee benefits being purchased around the world. They are looking for more uniformed offerings, better reporting and a greater understanding of the global benefits picture," says Ms Liu.

Regulation is also an important growing trend in the employee benefits area, according to Ms Liu. As organisations become more global, their employee benefits needs become more complex, given the large variations in local tax, insurance and employee benefits environments, she explains.

"Regulation requirement has been increasing for employee benefits, requiring companies to take a proactive approach to make sure that their benefits offerings are in line with local regulatory and tax requirements and kept up to date with any regulatory changes," says Ms Liu.

Funding

Rising costs and the centralisation of employee benefits are also driving changes in the way companies fund and place insured benefits.

Large international organisations are increasingly focusing on the management and financing of employee benefits, according to Holger Kraus, head of risk finance and strategy at Siemens Financial Services. The company began funding benefits risks through its captive in 2013.

"Organisations are looking at new ways to manage benefits—a significant expense for all corporates, and a cost that has been largely sidelined as it is usually in the domain of local HR. Now large companies are looking to integrate HR and finance and get the best out of their benefits," he says.

DITCHING THE SILOS: Taking an holistic view of people risk

THE INCREASING relevance of human capital is likely to drive a more holistic approach to people risk in the future.

Take a look at any risk register or survey of risk professionals and people-related risks are sure to feature highly. Yet people risk typically falls outside the remit of risk managers, while the concept of people risk management within HR is far less well defined.

Of the more than 50 top risks identified by risk decision-makers taking part in Aon's most recent *Global Risk Survey*, many included a human element. Failure to attract or retain top talent was the fifth highest people-related risk, while failure to innovate was sixth.

Other people risks identified in the report included cyber attacks (ranked ninth), political risk (15th), corporate governance (16th), directors' and officers' liability (20th), employee injury (23rd), employee fraud or dishonesty (24th), merger and acquisition restructuring (28th), inadequate succession planning (30th), workforce shortage (32nd), ageing workforce (39th), terrorism (41st), understaffing (43rd), pandemic (44th), social media (46th), absenteeism (47th), pension scheme funding (50th), kidnap and ransom (52nd) and discrimination (54th).

Most valued asset

People are increasingly seen as a critical asset in knowledge-intensive industries like technology and finance. But they are also being seen as a potential risk.

The value of human capital is increasing as the global economy becomes even more knowledge-intensive, according to Edward Houghton, research adviser for human capital and metrics at the Chartered Institute of Personnel and Development (CIPD), the professional body for HR and people development.

Research has shown that improved business performance is linked with high quality leadership, people management and engaged staff, according to the CIPD.

Similarly, a number of corporate failings have been linked to "toxic organisational culture" or poor people management—recent conduct scandals in the banking and automotive industries are cases in point.

A more recent, and more extreme, case would be the Germanwings airliner that crashed over the Alps in March 2015 with the loss of 144 passengers and crew. Investigators believed the plane's co-pilot, who had a history of depression, deliberately crashed the jet.

On the emerging risks front, incidents of cyber security breaches illustrate organisations' vulnerability to employee behaviour. Many data breaches have included a human element, such as an employee being duped into giving away passwords or transferring funds in response to phishing attacks.

Roads to ruin

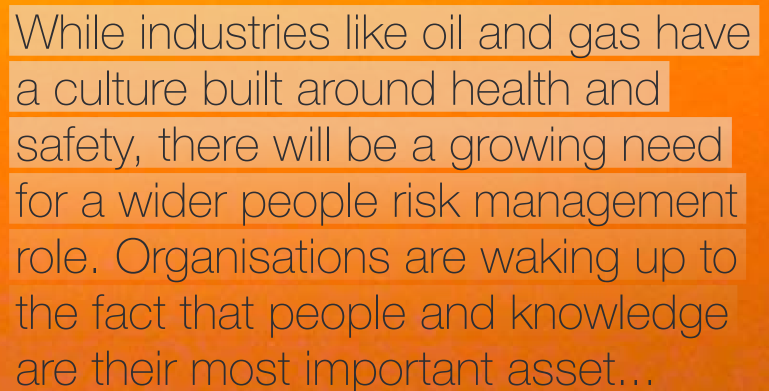
With increased reliance on technology, and the evolution of enterprise risk management, the risk management community is showing more interest in people risks, such as cultural and behavioural risks.

In a study of 12 major corporate failures, UK risk management association Airmic found seven key weaknesses. These seven weaknesses, which included poor leadership, ethos and culture, and defective communication, were all related to people.

The *Roads to Ruin* study concluded that that boards and specialist risk functions must work more closely together to avoid or mitigate the catastrophic consequences of events.

Measuring human capital

However, unlike property risk, people risk



is difficult to "pin down" and reporting on people risk is not up to the standards that investors need, according to Mr Houghton. Reporting of human capital management metrics could help investors value a company and better understand associated risks, he argues.

Information on health and safety is relatively advanced in sectors like energy and mining but investors have little information on human behavioural or cultural risk, or on governance issues like leadership capabilities.

"There is a need for a set of measures that show the value of people in an organisation and what steps are being taken to protect them, as well as how they will perform in today's often rapidly changing environment," says Mr Houghton.

People risk management

While there is a clear risk associated with people, this has not been a focus for HR in the past. In most companies there is not a HR risk manager, in the way that finance has a developed risk function to protect physical assets and liabilities. But experts do see a bigger role for risk management in HR in the future.

"People risk is fast rising up the agenda for HR professionals and directors, who want to ensure that they have the right culture and safeguards in place," says Mr Houghton.

"While industries like oil and gas have a culture built around health and safety, there will be a growing need for a wider people risk management role. Organisations are waking up to the fact that people and knowledge are their most important asset," believes Mr Houghton.

As a result, risk management will increasingly become an important part of the HR role moving forward, believes Mr Houghton.

A trend that may favour a greater focus on people risk management in the long term is the evolution in HR, according to Paul Devitt, global benefits consultant at Aon Hewitt.

While HR has historically been locally focused, increasingly companies are building a corporate HR function, which will be able to work more closely with risk managers and address relevant issues for business continuity or business strategy.

Corporate governance committees and the inclusion of HR on risk committees could also encourage a more coordinated approach, he adds.

Cooperation

The worlds of HR and risk management typically fall into separate corporate divisions and have developed in isolation.

As a result, cooperation between departments may be hampered by differences in culture and the lack of a common language around risk, and people risk in particular.

HR is concerned with people risk management—the risk that people and knowledge will leave a company—but it is not communicated and managed in the same way as property or liability risks.

"HR talks about the talent pipeline, performance and succession planning. But they do not talk about these issues in terms of risk. A common language needs to be found to articulate people risk," says Mr Houghton.

All of the experts interviewed for this report say they are seeing increased cooperation between risk managers and HR, and this trend is only likely to accelerate. Research from Willis Towers Watson found that risk managers at 35% of its large clients regularly engaged with HR.

Italian insurer Generali has seen a similar change in its client contact.

"Risk managers are becoming more and more key players around the tables where employee benefits are negotiated, and this does not only apply to clients running their employee benefits via a captive," says Vittorio Zaniboni, chief technical officer at Generali Employee Benefits Network. "Ten years ago, 95% of our counterparts were HR, while now this percentage lies around 70%, with the remainder from procurement and risk management," he adds.

With the cost of insured benefits rising, employee benefits are no longer just an issue for benefits managers, according to Mr Beech. "This is now an issue that requires a coordinated approach globally to contain costs and achieve efficiencies," he says.

CHANGING ROLES: Risk managers apply skills to benefits risk transfer and managing people risk

RISK MANAGERS ARE increasingly being asked to help place and transfer insured employee benefits, while their data and analytical skills can bring down the total cost of people risk.

Risk managers and insurance buyers are typically concerned with risks associated with physical assets and liabilities. And only a small number view people risk as part of their role.

People risk may be just as important for risk managers as property and liability risks, according to Julia Graham, technical director at Airmic and immediate past president of the Federation of European Risk Management Associations. However, she notes that progress in that direction has been slow, although inroads have been made around managing the costs of benefits and insurance.

"Whether it's reputation, physical or people, these are fundamental areas where risk managers can add value. Yet, to date, only a small number of risk managers have been getting involved with people risk and employee benefits. But the numbers are growing," says Ms Graham.

Purchasing skills

For most companies, people risk will be the responsibility of HR, rather than risk managers. Although risk managers can have a role, such as helping to report people risk, as well as developing a language around people risk, according to Mr Houghton.

"HR can advise on management behavioural risk and culture, but risk analytics, mitigation and risk reporting are the forte of the risk manager. There is an opportunity for HR to work with the risk community, which understands the nature and impact of risk," he says.

The area in which risk managers are having the most notable effect has been in the financing of employee benefits. In particular, as companies look at more efficient ways of funding insured employee benefits, risk managers have been called upon to rationalise purchasing and effect self-insurance strategies.

"Organisations are taking a more holistic view of employee benefits management and are involving risk managers together with HR managers in benefits decisions," according to Ms Liu.

"As the cost of employee benefits has been increasing, risk managers are helping HR purchase benefits more efficiently, while HR designs the appropriate benefits to attract talent," she says.

According to Mr Devitt, risk managers have the most value to add when it comes to the placement and funding of benefits, especially as companies look to consolidate insurance vendors and use financing structures such as pooling, bulk purchase or captives.

"Risk managers can bring their experience to promote a risk-financing approach to a benefits programme, including their design, delivery, funding and governance," explains Mr Devitt.

While the design of benefits is very much the role of HR and benefits managers, risk managers can "guide and influence" organisations as they expose themselves to benefit-related risks, he says.

Risk managers have skills and knowledge that can add immense value to HR and employee benefits, which require both risk analysis and risk transfer, explains Ms Graham.

"As well as being able to identify and assess risks, risk managers have knowledge of the insurance market and are skilled at account and portfolio management. They are also experienced in managing insurer and broker relationships, as well as running tenders," says Ms Graham.

For example, audits of employee benefits often reveal big overlaps or duplication of cover or excessive limits, she adds.

Risk managers can also add value in the area of compliance for employee benefits, according to Ms Graham. Multinational insurers, brokers and insurance buyers have accumulated knowledge and skills in creating compliant international programmes for property/casualty programmes over the years—and this experience can be applied to benefits, she says.

"Compliance is an area where risk managers can bring huge benefit to HR. Many of the tax and regulatory issues faced by insured benefits are similar, if not the same," says Ms Graham.

Enterprise-wide approach

Moving forward, risk managers are likely to take a much wider role in both employee benefits and the management of employee risk, going beyond risk transfer.

Risk managers are increasingly looking at employee-related risks well beyond the scope of employee benefits cover,

according to Paolo Marini, global head, customer management and marketing, corporate life and pensions, at Zurich Insurance Company.

For example, risk managers might be concerned with talent—and benefit tools can help in this regard—but they are also concerned with areas where benefits will be of little assistance, such as staff misuse of social media, or rogue trading, he adds.

"There are bridges between the two worlds of HR and risk management, and we do see more and more risk managers involved in what were previously considered HR issues. For example, risk managers in the UK are involved in dealing with deficits in employees' defined benefit pension funds, which can take up significant capital," says Mr Marini.

Wellness programmes are another potential bridge between risk management and HR, according to Mr Marini. "Treated in a certain manner, wellness programmes can improve the health of the workforce and therefore their productivity, as well as increase employee engagement, and we are seeing more interest in such systems," he says.

HR and risk managers will work ever-closer together in the future because employee risks will increasingly require risk engineering, one of the real strengths of risk managers, predicts Mr Marini.

For example, Zurich research conducted by the Oxford Smith School has shown that the majority of workplace disability cases are the result of either musculoskeletal injuries (such as back problems) or nervous health issues (like stress or anxiety-related conditions).

Such conditions will require data analysis to identify claims patterns and causes, as well as actions to mitigate or prevent future claims. Zurich has customers that are already going down this path, with HR and risk managers working together to reduce people risk (road safety for example).

"HR and finance also have common interests when people risks are funded in-house, self-insured or reinsured to a captive. And as data quality and accuracy improves, I would expect more companies will look at optimising risk management and minimise such risks," says Mr Marini.

Holistic approach to people risk

LARGE AND MORE SOPHISTICATED COMPANIES ARE STARTING TO TAKE A more holistic approach to employee risk, according to Tony Powis, chief executive officer—Willis Employee Benefits, part of Willis Towers Watson.

"Organisations realise that their employees are often their most valuable asset, and some risk managers are beginning to look at the risks around that human asset," he says.

Risks like the ageing workforce and talent are relevant to risk managers, who can look at such issues through a risk perspective. And while certain people risks fall into both risk management and human resources camps, there are overlaps between benefits and property/casualty insurance.

For example, if an employee is absent due to a workplace injury, it will have implications for both employers' liability and income protection coverages, according to Mr Powis.

There are "massive overlaps" between certain insurance and benefits, says Mr Powis. But most insurers, brokers and employee benefits consultants are not joined up across the spectrum of risk, including people risk, he says.

Adrian Humphreys, head of group risk and health at JLT Group, also sees big opportunities for a more holistic approach to employee risks.

"In the past, the company doctor, occupational health, employee assistance programmes, income protection and private medical insurance all operated separately. But it just isn't economic to run them in silos," he says.

By coordinating employee assistance, private medical insurance and occupational health, companies can get employees back to work much more quickly and cost-effectively, according to Mr Humphreys.

"Why on earth would you not join things up? It makes perfect sense to join the risk to the cost of financing that risk—and we are now seeing more joined-up thinking in employee benefits," he says.

According to Mr Humphreys, risk managers can bring "cohesion" as companies take a more holistic view. "Risk managers understand spend against mitigation—the idea that you can spend here to save money here. Risk managers can help HR get the most effective return on their investment," he says.

Taking a holistic view of people risks—both in terms of risk management and insurance or benefits products—can produce cost savings, explains Jayesh Patel, head of international risk management programmes at Allianz Global Benefits.

"There are synergies between products offered locally that can be thought of together—for example, disability insurance and medical benefits. It may be possible to reduce spend by looking at how to get an employee back to work before getting into expensive medical treatments," he says.

In the US and Australia, companies are using occupational health to manage workers' compensation spend, according to David Hully, key account manager at Allianz Global & Corporate Specialty.

"A slip or a fall, a repetitive strain injury or an occupational disease can result in a huge cost, but occupational health surveys and recommendations can reduce injuries, improve working conditions and reduce the cost of workers' compensation claims," he says.

Some insurers have moved to integrate employee benefits with property/casualty insurances, explains Ms Liu.

This is a notable trend in the US, where some insurers are working with their customers on integrated absence management, which has led some life and non-life coverages to be combined. For example, Zurich has developed combined solutions with disability and workers' compensation insurance in the US, as well as employers' liability in the UK, according to Ms Liu.

RISK FINANCING: Pools and captives bring increased oversight of benefit programmes

INSURERS AND NETWORKS offer a range of solutions to rationalise benefits programmes, from pooling arrangements to a new breed of international solutions.

At present, there are four main options for funding employee benefits.

The default position is full local autonomy, where country benefit managers are responsible for designing and placing benefits. But as the desire for central control has increased, the next logical step for many has been to enter multinational pooling agreements, administered by one of the main global employee benefits networks.

There are currently eight major network providers running thousands of employee benefit pools. The solutions are offered by recognised insurer names—Zurich, Generali, Allianz, AIG, Maxis (MetLife and Axa) and Swiss Life, as well as networks created from non-owned local carriers Insurope Network and life insurer network International Group Program.

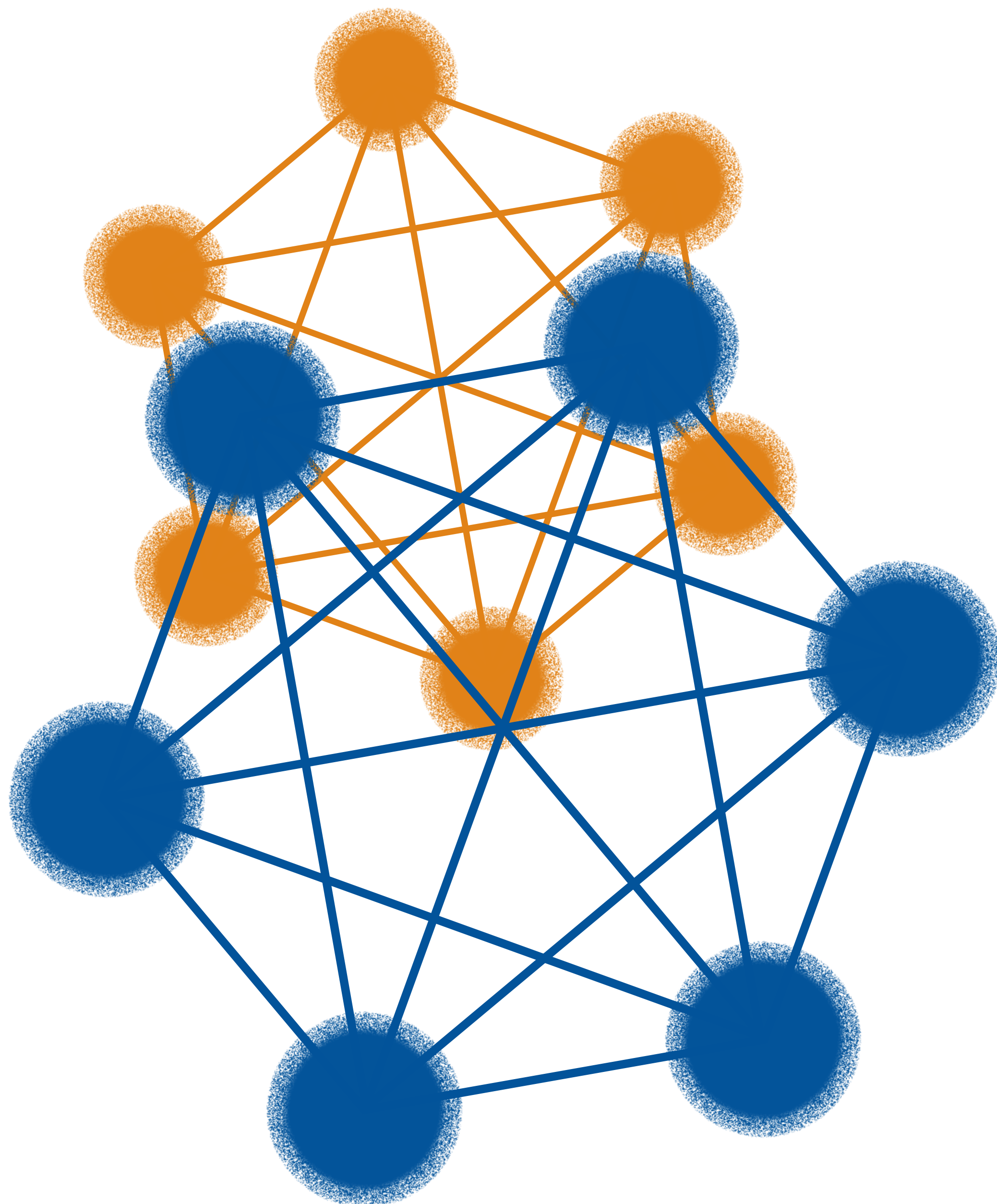
AIG recently entered the market in a deal with ING. In May 2015, AIG acquired a controlling stake in ING Employee Benefits Global Network, which was renamed AIG Global Benefits Network.

Pools enable companies to enjoy some efficiencies of scale and share in any underwriting profits—in the event of an aggregate profit, pools pay a dividend at the end of each year. Networks also provide some account management and centralised data reporting.

Employee benefits pools and networks are well established and in recent years a growing number of companies have taken them to the next level, using insurance captives to effectively self-insure employee benefits risks, explains Mr Devitt.

Under this model the network acts as a fronting insurer, issuing policies and paying claims locally. Captives offer additional savings and the potential to identify claims trends and take steps to proactively mitigate exposures.

A more recent trend has seen some companies bulk purchase portfolios of benefits. While similar to pooling, bulk purchasing sees benefits run on a portfolio basis with the insurer.

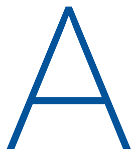


While the number of companies combining pooling, networks and captives has been increasing, insurers are keen to emphasise that different solutions will suit different clients.

“At Zurich we are taking a holistic view based on the needs of the customer. There is no one solution that fits all. Some customers will prefer a multinational benefits pool that utilises a more local approach, while others may wish to take a more global and centralised approach,” says Ms Liu.

“Our solutions are structured on a customer-by-customer basis. Different companies have different needs when managing their employee benefits—some companies will focus on cost while others on risk management,” she adds.

FUNDING BENEFITS: Captives offer big savings and risk management opportunities



N INCREASING number of companies are self-insuring employee benefits via their captives, creating significant savings and opening the door to using data to bring down the total cost of risk.

One of the most notable trends in benefits financing in recent years has been the increased role for captives.

Corporations have been using captive insurance companies to retain and manage their risks centrally for decades. For property/casualty exposures, the captive approach gives companies more control over their coverage, reduces frictional costs and provides a useful risk management tool.

Insured employee benefits, in contrast, have remained fragmented and largely local, and have not benefited from the same degree of central control and rationalisation.

"Historically there has been very poor visibility of benefits and benefits spend centrally, even though cumulatively the spend can often be larger than property/casualty premiums," according to Lorraine Stack, senior vice-president, Marsh Captive Solutions Practice, based in Dublin, Ireland.

But a growing number of companies are now using their captives to manage the cost of providing insured employee benefits, such as life, disability/income protection and medical insurance.

Small but growing

Out of an estimated 7,000 captive entities worldwide, around 100 are thought to manage sizeable employee benefits programmes. Opinions differ on the exact number, but everyone interviewed for this report believes the numbers are growing, and that interest has accelerated in recent years.

The number of captives writing employee benefits is expected to increase notably in the medium term, although total numbers will remain relatively small, according to Ms Stack.

"The journey from decentralised local benefits programmes to a captive can take several years and, given the huge interest we see from clients today, I expect we will see many more in the next five years or so," says Ms Stack.

While the idea of using a captive to fund benefits risks has been around for a number of years, interest has been growing as the concept has matured, and as insurers have improved their offering, according to Ciaran Healy, director of consulting for Willis Global Captive Practice.

"The growing trend is that companies are managing their benefits through a multinational pool, funding the risk through a captive, using multi-line stop-loss reinsurance to provide protection and reduce volatility. This approach can reduce benefits spend by 5%-10%—a big number for companies with a large workforce and a good story for risk managers and HR to tell," says Mr Healy.

Regulatory changes in Europe, with the implementation of Solvency II in January 2016, are also likely to boost interest in using captives to fund benefits, according to Mr Healy.

In recent years, European captives have been preoccupied with Solvency II's new capital and risk management rules. However, many are now turning their attention to how they can get the most out of their captives under the new regime, explains Mr Healy.

"During the past six months we have seen more interest and more focused conversations. I am confident that the growth in captives with employee benefits will accelerate as these projects are implemented," he says.

The development of the captive employee benefits programme concept could also help drive captive use into the mid-sized commercial sector.

For example, looking at employee and property/casualty holistically could strengthen the business case for medium-sized companies to establish a captive for the first time, believes Paul Woehrmann, head of captive services at Zurich Global Corporate, part of Zurich Insurance Company.

This could be a full captive (re)insurer, a rent-a-captive or virtual captive, such as a cell in a protected cell company, he adds.

Natural partners

Most insured employee benefits are straightforward to include in a captive and bring benefits to both the existing property/casualty portfolio, and to the management of benefits costs.

Employee benefits are high frequency, low severity risks that are relatively simple to forecast, according to Ms Stack. "Employee benefits are well suited to a captive. They mitigate the more volatile property/casualty risks and offer diversification," she says.

Diversification benefits are particularly attractive for captives domiciled in the European Union (EU), and subject to tougher solvency and risk management rules under Solvency II since January 2016.

Solvency II is increasing compliance and governance costs for captives based in the EU and companies have been looking at ways to reduce cost and get more from their captives, explains Mr Woehrmann.

One way in which captives can increase premiums and broaden their risk profile is to add employee benefits. Solvency II provides capital credit for non-correlated

Pension risk

A SMALL NUMBER OF ORGANISATIONS HAVE USED captives to manage pension risks, in particular as they look to deal with defined benefit plans.

Such schemes, which typically pay a guaranteed income on retirement, have proved uneconomic and many pension funds have large deficits, where liabilities far exceed assets. As a result, most companies have closed their defined benefit schemes in favour of defined contribution schemes, which shift the investment risk to employees.

This has seen companies look for solutions to legacy defined benefit schemes, including de-risking, longevity risk transfer/hedging, or bulk annuity deals. And this is where captives can be part of the solution.

Captives are being used by companies to transfer or hedge risk—mostly longevity exposures—with reinsurers and investment banks. The captive offers a cost-effective vehicle to front a longevity swap and pass longevity risk to counterparties, according to Marsh's Ms Stack.

Some organisations are also looking to take control of assets and the investment policies of defined benefit schemes from pension trustees. This has seen a small number of trustees purchase a bulk annuity from a fronting insurer, and reinsure the risk back to their captive, she adds.

Brian Quinn, managing director of Granite Management, also notes that some mature employee benefit captives are now looking to include pension-related risks, such as longevity and investment risks from closed defined benefit pension schemes.

"Companies need to have available cash to fully fund the pension liabilities and a risk appetite to bring pensions risk into a captive. Many companies are thinking about this, but only a few are doing it," he says.

risks, giving captives diversification benefits when adding life risks to a property/casualty portfolio, he says.

While many companies will not expect employee benefits to bring significant profits to their captive, they often use it as a risk management tool to improve governance and create more value, explains Generali's Mr Zaniboni.

"Among the main advantages, the impact risk diversification has on solvency capital has been recently very high on managers' agenda. Meanwhile, adding large amounts of premium to the captive books will also enlarge the top line of the profit and loss account and give the captive a larger capital base to insure other exposures," he says.

A number of captives that have included employee benefits in recent years have also taken a more holistic view of their reinsurance protection, taking advantage of cross-class cover offered by insurers.

"Once companies are comfortable ceding employee benefits to their captive, they may then look at cross-class protection for the captive, such as stop-loss or aggregate covers. This helps to further increase efficiency of risk transfer, in addition to the diversification benefits under Solvency II," says Mr Woehrmann.

Captive advantage

While there are a number of advantages of bringing insured employee benefits into a captive, the potential cost savings can be compelling. By using a captive to fund insured benefits, companies can make significant savings, such as broker commissions and insurer profits, according to Ms Stack. There are also advantages in improved cashflow and the ability to collect investment returns, she says.

"Financial efficiencies of moving from a decentralised structure to pooling are generally accepted to be in the region of 10%-15%, but there are also incremental savings to be made from using a captive. Companies tells us that the cumulative savings [of using a pool and a captive compared with buying locally] can reach 25%," says Ms Stack.

Willis Towers Watson research has shown that multinational pools produced a 6.1% return on investment, over three years. The top quartile produced dividends greater than 10%, although one in every three pools returned no money at all. The study, which included 14 benefits captive programmes, also showed that the use of a captive produced a median return of 11.3%.

Life and accident insurance contracts were the most consistently profitable, with returns of 23% for both pooling and captive business. However, standalone medical contracts generated average returns of -8% in multinational pools and -2% in captives.

Enhanced cover

Using a captive can also give risk managers and HR more control over employee benefits cover, as well as ensuring that cover is more consistent.

"The captive can be used to offer benefits cover that is not widely available in the market, such as nuclear, chemical, biological and radiological, passive war risks, or for medical conditions like Aids," according to Mr Healy.

Increased control of cover is particularly useful when looking to attract and retain talent. "You can improve the cover available locally using a captive, which could be a real advantage when looking to attract and retain talent," says Ms Stack.

"And organisations can provide the benefits cover they want, not what insurers want to provide," she adds.

Data mine

Organisations that use captives to finance insured employee benefits risk can also achieve better management and transparency of data.

According to Ms Stack, one of the biggest hurdles for the centralisation of benefits is transparency. "Information on employee benefits spend is shockingly sparse," she says.

"Even with pooling structures, networks typically only provide data six months after the end of the underwriting year. So there is no true actionable visibility on data," she adds.

However, captives need to pay claims quarterly or monthly, so data from fronting insurers flows faster to support the cashflow arrangement. "Quarterly reporting means more transparency of financial performance and the ability to improve claims and cost management," says Ms Stack.

The data and systems required by captives can also help improve governance and control over benefits, according to Mr Quinn of Granite Management, the Hamilton, Bermuda-based captive management and employee benefits consulting company.

Some companies are concerned with "benefit slip", where local HR managers increase employee benefits without the approval of the corporate centre, he adds.

Risk management boost

To date, the main focus of captive employee benefits programmes has been around the immediate cost savings but more sophisticated companies are now beginning to explore potential risk management and mitigation actions.

"Initially, captives focus on growing their benefits programmes but some sophisticated benefits and captive managers are now looking at the next stage, how to manage programmes and reduce the total cost of risk," says Mr Beech.

"There is a lot that can be done to understand claims—on analysis and intervention—and this is an area where risk managers can help," he says.

For example, benefits managers might respond to a large increase in premiums by cutting benefits or shifting more of the burden to the employee. In contrast, a risk manager might look to address issues and reduce the cost of claims, explains Mr Beech.

The area in which there is currently most interest is in medical benefits, where claims inflation and overall spend is high. Using a captive to manage medical benefits enables companies to take a proactive risk management approach to limit future claims, using wellness programmes to keep employees healthy and at work, explains Mr Beech.

Companies that started using their captives to fund employee benefits a decade ago are now beginning to focus on cost savings through data analytics and risk management actions, explains Mr Quinn.

"Our more mature clients—those that have funded benefits in their captives for five to 10 years—have achieved the main efficiencies. But now they have the data they need to work down medical claim costs and improve governance," he says.

As risk managers and HR professionals cooperate and manage the cost of benefits through the use of captives, it seems logical that this relationship could develop further in the future.

The inclusion of employee benefits in captives could "open the door" to more joined-up thinking on people risk, believes Mr Devitt. "At first, benefit funding in captives looks to unlock underwriting profit and diversification; now we see more talk of governance and cooperation," he says.

This view is shared by Mr Woehrmann. "Risk management actions can bring down the cost of risk, so the captive may act as positive pressure for HR to work with risk managers to improve the quality of risk," he says.

Data analytics is driving innovation and enables employee benefit networks to deliver huge value to HR and risk managers alike, according to Mr Zaniboni.

"If you are able to collect the right data and interpret it correctly, you can completely change your benefits policy. You can assess the impact of your investment, understand specific needs/criticalities and implement a targeted approach. This is all the more clear in the context of health and wellness programmes, where you can address specific disorders in a much more efficient way," he says.

As companies embrace ERM, insurers can help clients use their captives to manage their human risks, according to Marine Charbonnier, head of financing solutions at AXA Corporate Solutions.

"ERM identifies exposures, including human and employee-related risks, and we have identified the need for protection and can help bring these into the captive," she says.

For example, AXA CS offers additional 'human protection' cover, such as group personal accident, business travel and key man insurance. It has also helped companies use captives to cover pecuniary losses, including business interruption and exceptional costs, such as those related to terrorism exposures.

Cultural challenges

While there are many benefits to using a captive to finance employee benefits programmes, this solution will not suit every organisation and there are significant challenges to successful implementation.

Companies require a critical mass of employees (at least 5,000) with a good geographical spread if they are to use a captive to fund benefits risk via a multinational pooling arrangement, according to Ms Stack.

Employee spread is important because companies will not want to add high accumulations of risks, such as concentrations of employees in single high risk locations, such as a major city or catastrophe-exposed zones.

There are also important internal operational considerations, notably around the structure of HR and how it is connected to other parts of the business. In particular, there needs to be a degree of centralisation and cooperation between HR and the risk management function, which is not typical in most companies.

"One of the biggest challenges for customers wanting to bring employee benefits into their captive will be the need for effective communication between HR and risk management," according to Mr Woehrmann.

"Typically, risk management is a centralised function to drive non-life insurance programmes and HR is decentralised. So companies will likely need an additional layer to organise and centralise

benefits, which will take time to establish," he says.

While savings will be attractive to HR, employee benefits managers will be concerned with the quality of benefits. Moving to a captive-based approach could mean changes to carriers and HR will want to know that insurers are able to deliver the required benefits locally.

"HR will need to be confident that by using a captive, their objectives of providing rewards to an employee will not be diluted but in fact enhanced," says Mr Healy.

The importance of engaging with HR and understanding its needs cannot be underestimated, according to those interviewed for this report.

"Introducing a captive can be a big change programme for HR—particularly if there is no existing financing strategy—so any changes need to be aligned with their needs and requirements," says Mr Devitt.

"Organisations looking to take control of benefits and fund them through a captive will need to bring HR and the risk management function together. Each part comes with its own objectives, but when bringing employee benefits into a captive it is best to have everyone on board early," says Mr Devitt.

Implementing an employee benefits captive programme is challenging and sometimes it may fail. A key reason for this is often lack of coordination between HR and risk management, or insufficient management backing, explains Ms Charbonnier.

"It's not necessarily always a question of what insurers can offer or what international employee benefits networks can do, but how organisations are not always aligned in their thinking or not coordinated between HR and risk management, but also between local and global as well," she says.

Global vs local

A key challenge for risk managers looking to bring employee benefits into a captive will be the local nature of insured benefits, and the implications for programme structure.

Employee benefits have to be written "bottom up, policy by policy and country by country", according to Mr Beech. "Benefits are tailored to each country, individual welfare and tax environment, making it difficult to write a one-size-fits-all policy," he says.

The need to write benefits locally can be a big hurdle to overcome for risk managers, but it is part of the learning process, advises Mr Beech. "However, it is cost-effective to use insurer networks to centralise premium flow and manage claims. And much can be learnt from the principles on property/casualty global programmes," he says.

Risk managers are used to the concept of a global programme for property/casualty risks," says Ms Stack. "These are well established and efficient structures that risk managers are very familiar with, but comparable global programmes do not yet exist in the employee benefits space," she says.

"There may be a collection of group policies—for life, accident and health, disability and medical—that sit in the local markets, which share experience under a pooling arrangement. But there are no global master policies, although some insurers are working on this and it may happen over time," she adds.

Industry perspective

Another consideration for risk managers is the relative maturity of the employee benefits captive concept and the ability of insurers, brokers and the wider risk community to provide expertise, service and product.

There has been a notable increase in investment by insurers and networks in recent years, but capabilities may not yet be at the same level as property/casualty.

"The ability of insurers and networks to facilitate benefits funding by captives has improved. A number of networks have invested in developing employee benefits pooling systems that captives can access, and several now have good offerings," says Mr Healy.

Mr Zaniboni believes insurers are now in a good position to support captive clients with employee benefits.

"Interest in employee benefits captives started in the 1990s, and it has been a long learning curve. But we now have a comprehensive view of the pitfalls and complexities and can partner with our captive clients to help them navigate through this experience," says Mr Zaniboni.

However, while great strides have been made, captives have only been accepting employee benefits for around 20 years, and numbers have remained small.

"This has to be kept in perspective. While interest is undoubtedly growing, there are still no more than 100 captives funding employee benefits," according to Thierry Mestach, vice-president, head of markets and strategy at MAXIS, the global benefits network owned by AXA and MetLife.

"If we globally see 10-15 new global benefits projects/requests then it has been an extremely good year for our captives business. But we do not see hundreds of clients—it is a niche segment of the most sophisticated and largest clients that are requesting it," he says.

The extent of demand is relevant as insurers and the international employee benefits networks require a return on any investment in services and products to serve captive clients.

As the numbers of clients wanting to bring insured benefits into their captives have grown—and expectations of service delivery and sophistication have also increased—insurers and networks have had to invest in enhancements to their offering, according to Mr Mestach.

CLIENT NEEDS: Vendors develop joined-up solutions and enhanced captive services

AS THE NUMBER OF multinationals with captive benefits programmes increases, and as companies take a more holistic view of people risks, brokers and insurers are looking to respond with a more joined-up offering.

The insurance industry is often noted for its silo approach, where insurers structure their operations around specific lines business. This is particularly evident in the divergence of life and non-life business.

Many insurers have chosen to focus almost exclusively on one or the other. Only a handful of multinational insurers have capabilities in both property/casualty and group life and, up until recently, these were not well linked.

However, the trends of financing benefits in captives and a more holistic view of risk are challenging insurers to change. In recent years, leading multinational insurers, brokers and benefits consultants have made moves to offer corporate clients a more joined-up offering.

This is particularly evident among insurance brokers, the largest of which have combined with employee benefits consultants. For example, Marsh has owned Mercer since 2002, while Aon acquired Hewitt in 2010, and Willis recently merged with Towers Watson.

In recent years these organisations have looked to encourage greater cooperation between the benefits consulting and property/casualty broking arms, and many now field people from both sides of the business in client meetings.

A similar trend has taken hold among large multinational insurers. The integration of non-life and life corporate business among this group has accelerated in the current challenging market conditions, which have made some carriers look to leverage their positions, cross-selling products and finding ways of attracting more corporate business.

European insurers approached for this report, notably Zurich, Generali, AXA and Allianz, have all looked to link their corporate property/casualty, group life and assistance businesses. In some cases, all three are part of the same business group.

All these insurers say they have combined their group life and property/casualty expertise for large clients, at least in terms of relationship management.

For example, Zurich offers clients one point of contact for both life and non-life solutions. “A single relationship leader will manage all of a customer’s needs, and this is particularly important when using a captive to finance both employee benefits and property/casualty programmes,” says Ms Liu.

Growth of captive benefits programmes has made other insurers respond in a similar way.

“We have had to consider how we interact with captive clients in a more combined way,” says Mr Zaniboni of Generali. “While we do not yet manage employee benefits and property/casualty risks via a single contract, we do have a synchronised approach to all corporate solutions with the dedicated Generali Global Business Lines unit,” he says.

“We operate a joint client management platform, including a common credit risk management platform; we have aligned our methodologies on collaterals and on treaties and reports, which have the same look, feel and rationale across both lines of business; and we have strongly invested in improving our reporting capabilities, from the network infrastructure to the business intelligence development,” says Mr Zaniboni.

“The objective is to go beyond accounting and help companies take the most out of a coordinated risk management strategy,” he adds.

Service enhancements

But the growing use of captives to fund employee benefits has also required a response from insurers that goes beyond client relationships. Insurers and networks have had to improve their overall offering to captives, with a particular focus on data, reporting and network infrastructure.

“Where clients go, we have to able to offer a solution,” says Mr Mestach. MAXIS, for example, has made further investments in its offering, resources and systems in response to clients’ needs, he says.

“Medical costs, which are often around 60%-70% of the employee benefits budget (excluding pensions), are high and still continue to increase year upon year. So we have enhanced our medical reporting capability, including claims analysis, to help clients get a better picture overall and among other things also to enable us to help them start doing more in the area of risk prevention,” he says.

“But to provide that type of data on a regular basis over a number of countries is a challenge and has required a substantial investment,” continues Mr Mestach.

Work in progress

While investments have undoubtedly been made, captive servicing for employee benefits is not as advanced as it is for property/casualty.

Differences exist between insurers’ capabilities, but the two common areas where risk managers would like to see improvement are around data and communication across the network.

“Insurers have been investing, but it’s about the glue that holds the network together. Networks need to improve their coordination. They have the dots on the map, but they need to get a better idea of what their partners are doing,” explains Mr Beech.

Information on coverage and claims—the bread and butter of risk managers—exists among local insurers but it is often not readily available, or is not passed to the network or corporate head office, according to Mr Beech.

“Insurers need to do more on infrastructure and data, in terms of helping organisations to identify issues and helping employees through wellness programmes. The transfer of data is not there yet, but it will come,” he says.

GLOBAL PROGRAMMES: Insurers take the best from p/c and apply to benefits

ITH THE growing use of captives and a desire from some companies for more centralised employee benefits purchasing, insurers have been looking at ways to bring the advantages of property/casualty global programmes to the benefits arena.

There are a number of trends that support potential demand from multinational companies for global employee benefits programmes, including an ever more internationally mobile workforce and the trend towards more central control over employee benefits.

As discussed in the previous sections, companies are seeking to have more control over employee benefits, centralise their purchasing, seek economies of scale and reduce complexity. However, these aims can be difficult to achieve under fragmented traditional pooling arrangements, where clients have to deal with numerous carriers.

And with the increased use of risk managers and captives in the placing and financing of employee benefits, there is a natural desire to bring some of the benefits of property/casualty global programmes to employee benefits.

These trends look likely to drive demand for global employee benefits solutions that recognise the need for compliance and local cover, but at the same time the need to reduce complexity and increase central control.

Until recently there has not been a product that replicates a property/casualty global programme for employee benefits. However multinational insurers, to varying degrees, have shown an interest in developing such a concept.

International solution

In 2015, multinational insurer Zurich announced that it had developed an international benefits programme, combining local cover with cross-border policies in a single, simplified programme.

While not structured in the same way as a property/casualty global programme, the Zurich International Programs for Employees looks to bring the advantages of global programmes to benefits.

"Responding to the trends in corporates' need for central control, the involvement of risk management along with benefits management and the focus on insurance and tax regulation, Zurich is excited to announce a new solution, Zurich International Programs for Employees," says Ms Liu. "This can help corporates balance their local needs with an efficient global approach when managing their employee benefits needs," she says.

Zurich International Programs for Employees still requires local policies, each with their own terms and conditions and local tax and regulatory requirements but where possible it draws on the advantages of property/casualty global programmes by mirroring their structure as closely as possible, explains Mr Marini.

Zurich agrees overall terms and pricing centrally, explains Mr Marini. "Our solution seeks to issue as few local policies as possible, balancing the desire for simplification and central control with the alignment with local regulatory and tax requirements," he adds.

A global programme differs from pooling arrangements, which have been available for many years, explains Mr Marini.

"A pooling arrangement is a collection of local contracts, financially consolidated and offering retrospective profit share. An international programme, however, centralises contracts with the group's overall size in mind, and rather than paying a profit share, the margin is already included in the rates," says Mr Marini.

"Pooling is a diplomatic and non-invasive solution that offers significant benefits and is here to stay, but a new breed of programmes is emerging that will offer companies a more centralised approach," says Mr Marini.

Zurich's International Programs for Employees is said to have received positive feedback from customers.

"It is a central challenge for global corporations to manage purchase of employee benefits and non-life insurance products and services," says Tracey Skinner, director of insurance and risk financing at British Telecom Group.

"With a good relationship between risk managers and HR and the new approach presented by Zurich, we will be able to finance the best cover for employees and manage the risk more efficiently through our captive," she says. The company is one of the multinational companies that has shown an interest in becoming a pilot customer for the new solution.

This new generation of global benefits programmes will not be for everyone but it definitely suits centralised organisations with relatively small operations in multiple overseas locations, explains Mr Marini.

"Companies with smaller operations overseas are unlikely to enjoy significant buying power on price and terms and conditions but this can be solved by a global programme," he says.

Challenging concept

Zurich's global programme for employees is being rolled out in 2016, and is still a new concept for the market to digest. As a result, there remain differing views among insurers.

Mr Mestach of MAXIS believes that international programmes are more suited to some populations of employees than others. For example, MAXIS provides international cover for expats and mobile employees but is more sceptical when it comes to covering larger local employee populations.

"There have been initiatives to cover local populations in more than

one country—such as life risk in multiple locations under one plan—but this is challenging. Offerings that are available in the market will often be tailored or be suitable only for smaller sets of employees," says Mr Mestach.

"A global policy covering large pockets of employees will face challenges at a local level, for example it may [run into] issues around tax, social security and also local customs/culture," he says.

"For these reasons, at MAXIS we are not convinced by cross-border programmes. We have had some of these programmes in the past, but there are no actual plans to develop them further," says Mr Mestach.

According to Allianz's Mr Hully, organisations can already achieve many of the benefits of a global programme through pooling and captive arrangements.

"There is a well-tested and established method for emulating the benefits of a global programme. Organisations can maintain the local scope of cover and meet compliance requirements by using a pooling arrangement, and then centrally reinsuring into an insurance carrier or captive," he says.

"Regulations and language may differ from a property/casualty global programme but essentially the same functions are there for employee benefits—you can go to a single global insurance network and the information flow and reporting infrastructure is there," he adds.

The latest development by Zurich has also caught the attention of Generali.

"I can understand why some clients find the idea of an employee benefits global programme attractive and we look at this development with interest. But we have yet to see how far the industry can go with this concept and how the fiscal and legal obstacles can be effectively overcome," says Mr Zaniboni.

"Unless a global programme can solve the tax and fiscal issues, it would, in reality, remain an aggregation of different programmes. And traditional employee benefits solutions continue to offer value and advantages," he adds.

Lloyd's Register, London

CASE STUDY: Lloyd's Register

LLOYD'S REGISTER IS A MARITIME CLASSIFICATION SOCIETY AND RISK MANAGEMENT SERVICES PROVIDER with some 9,000 employees in 80-plus countries.

In 2013, the company looked to consolidate a number of non-life coverages and insured employee benefits under one arrangement, reinsured into the group captive.

Working with its broker Willis (now Willis Towers Watson), Lloyd's Register's captive reinsured eight property/casualty-life coverages, together with life and income protection, fronted and underwritten by a single insurer, Zurich. The captive also purchased a stop-loss reinsurance cover from Zurich to provide aggregate protection across non-life and life exposures.

Almost three years on, the cross-class cover and the inclusion of employee benefits within the captive have proved a great success, according to Clive Clarke, Lloyd's Register's group insurance manager.

The company has since added other employee benefits—notably a global difference in conditions/difference in limits global life and international private medical cover—and is open to including others in the future, he says.

"The claims experience suggested that employee benefits were a good risk for the captive and would help make the captive broader in terms of risk, yet not deeper in terms of exposure," explains Mr Clarke.

The decision to purchase a cross-class cover and bring employee benefit risk into the captive was threefold, explains Mr Clarke. Lloyd's Register was interested in broadening the spread of risks reinsured by the captive, as well as getting greater visibility of employee benefit data and increasing its leverage with insurers.

By bulk-buying non-life and employee benefits coverages with one insurer, Lloyd's Register now has more control over its insurance protection, according to Mr Clarke.

"Employee benefits premiums can be large and there are good savings to be made by looking at solutions. We were able to show that we can keep a significant percentage of premium for the group, but, by giving a small risk away to the insurer, we are also able to protect the P&L and business against unforeseen losses," he says.

Consolidating insurer and broker relationships has pros and cons, according to Mr Clarke. While it may not be possible to get the best rate for every line of business, a strong relationship with one insurer gives consistency of service and a partner that is willing to go the extra mile.

"We are able to go to one or two key people at our insurer, whether it's employee benefits in Germany, a property risk in Morocco or an environmental policy in the US, and we get a consistent approach," says Mr Clarke.

"There is also huge value in flexibility. We can get something from our insurer they would not normally be willing to give us. This means we get services that match our drive for business innovation," he adds.

Data is also an important consideration for Mr Clarke. By adding employee benefits to its captive and by using one insurer, Lloyd's Register is getting consistent information on premiums and claims for property, liability and employee benefit risks.

"I am now able to present all data to the risk committee, not just for property and casualty risk, but the whole gambit," he says.

When Mr Clarke joined Lloyd's Register in 2012 he was tasked with expanding the group captive in a controlled way, including the addition of employee benefits. "The ground work had been done, but I needed to prove that it could work and provide added value. I was pushing at an open door but needed to prove the concept," he says.

"There was willing, but we had to convince stakeholders of the benefits. We had to show HR and pensions that one insurer was able to meet their income protection and life cover needs and provide services to get people back into work," he says.

In Mr Clarke's experience, HR and pensions are open to working with risk and insurance managers. His organisation has been insuring employee benefits through its captive for almost three years and this has helped cement his relationship with the HR and pension functions.

"Increasingly I discuss risk and insurance solutions with HR and pensions, as well as the benefits insurance brokers can bring. They now value the link that I can bring between risk and employee benefit solutions, as well as the different solutions which self-insurance can bring," he says.

* Lloyd's Register Group Limited (LR) is a technical and business services organisation and a maritime classification society, wholly owned by the Lloyd's Register Foundation, a UK charity dedicated to research and education in science and engineering. The organisation dates back to 1760. Its stated aims are to enhance the safety of life, property and the environment, by helping its clients (including by validation, certification and accreditation) to ensure the quality construction and operation of critical infrastructure.

CASE STUDY: Deutsche Bank

DEUTSCHE BANK, WHICH EMPLOYS MORE THAN 98,000 PEOPLE WORLDWIDE, BEGAN USING ITS LUXEMBOURG-BASED CAPTIVE insurer to fund employee benefits in 2013.

The financial services group had used pooling arrangements for a number of years, before moving to the "next level", using its captive to fund insured employee benefits risk, explains Valerie Alexander, managing director of Deukona, the in-house broker of Deutsche Bank.

Benefit risks are insured by the local insurer belonging to the network, which pools the risk centrally before reinsuring it to Deutsche Bank's captive. The captive makes underwriting decisions centrally—setting premiums and terms and conditions—and these are fed back to local contracts via the network.

The captive is protected by individual stop-loss cover provided by the networks, although other options such as a single cross-class reinsurance solution to cover both non-life and benefits are available. Such a cover, which caps the captive's aggregate liability, may prove advantageous under Solvency II, Ms Alexander believes, so Deutsche will evaluate what is available.

The company uses three employee benefits networks to manage a wide range of locally placed employee benefits policies, including life, disability, personal accident and private medical.

However, it does not make sense to use the captive to fund all employee benefits in all countries, explains Ms Alexander. For example, group schemes are not common in Germany, while relatively high exposures and competitive market conditions in the UK mean that Deutsche has at present decided not to include UK benefits in the captive.

Ms Alexander notes that, while employee benefits have been placed in captives for some time, it is only recently that numbers have achieved a "critical mass" in the eyes of insurers. As a result, the services offered by large multinational insurers and networks around employee benefits funding and captives have yet to fully mature, she says.

For example, some networks have improved data and reporting capabilities, while others "need to up their game" in this regard, according to Ms Alexander. It is true to say that having a captive solution for employee benefits improves the information flow, but the standard of data reporting is not as high as it should be.

As a result, the potential risk management benefits of using a captive to fund employee benefit risk are currently not being realised, Ms Alexander warned.

CASE STUDY: Siemens AG

ENGINEERING AND ELECTRONICS FIRM SIEMENS AG BEGAN FUNDING EMPLOYEE BENEFITS THROUGH ITS GERMANY-BASED captive in 2013, following a joint project between finance and HR, looking at ways to optimise insured employee benefits.

Having been through the process, Holger Kraus, head of risk finance and strategy at Siemens Financial Services, Insurance has some practical advice for risk managers looking to follow suit.

Introducing a captive changes the roles and business models of brokers and insurers, as well as a corporation's internal functions, explains Mr Kraus.

Rather than placing business, the broker becomes a consultant, while the insurer moves from risk transfer partner to a fee-based provider of infrastructure and service. And while Siemens HR and risk management functions cooperated in the past, this has significantly intensified since the captive was used to finance benefits.

However, while there are many helpful people in the insurance industry, at times there is still a certain degree of rivalry between the traditional and the new approach in funding employee benefits.

"It is very important to manage and integrate the perspectives of the key stakeholders and it is key not to underestimate the cultural aspects," says Mr Kraus. For example, it is probably quicker to implement a captive benefits programme in a centrally managed organisation, compared with one where benefits are largely locally controlled, he explains.

Siemens' captive benefits programme is still in the "ramping up" stage but the company aims to use the captive to more actively manage employee benefits risks and costs, explains Mr Kraus.

"The intention is to use data, where privacy rules allow, to analyse trends and design risk management and preventative measures. Benefits are a significant cost and it will be worthwhile looking at ways to manage that cost," he says.

CASE STUDY: GM Motors

IN 2002, US-BASED AUTO MANUFACTURER GM MOTORS STARTED TO USE ITS BERMUDA-DOMICILED CAPTIVE INSURER, General International, to fund a wide range of employee benefits provided to its large non-US workforce.

At the time, the captive was self-managed by GM and the initiative was led by its then international benefits manager Walter Ralph and the chief underwriting officer of General International, Brian Quinn. Today, the captive is managed by Granite Management, the Hamilton, Bermuda-based captive management and employee benefits consulting company established by Mr Ralph and Mr Quinn.

Initially, progress was slow but as local benefits managers saw the advantages, the captive substantially grew its employee benefits premium, explains Mr Quinn. Today it provides benefits to around 85% of GM's non-US workforce, while employee benefits premium written in the captive has risen from $4m in 2002 to around $70m-plus today.

Economies of scale have enabled GM to dramatically reduce the cost of its healthcare, life insurance and other benefits, according to Mr Quinn.

The captive generates annual savings—without any loss in benefit or service quality—between 15%-30% when compared with the cost of purchasing employee benefits with local insurers.

The biggest savings initially were through the removal of frictional costs, most notably broker fees and commissions, as well as insurers' profits, explains Mr Quinn. However, GM is now looking at potential further savings through the use of medical trend analysis to manage medical costs.

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