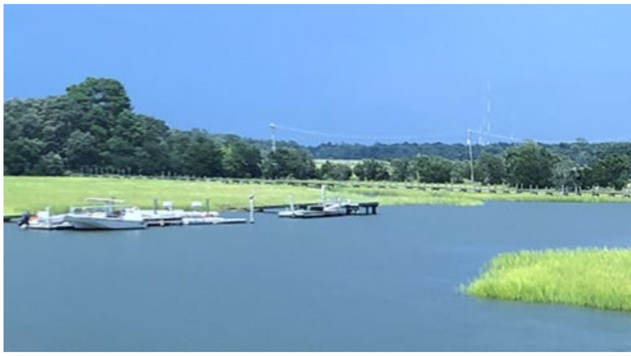
VIEW ON THE CREEK

August 18, 2021



Quarterly Newsletter from Energy Insurance Services, Inc., Volume 5, Issue 3

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Summer is passing by, and we continue to field new inquiries from EIM Members looking to explore the alternative advantages offered by a captive insurance facility for retaining or reinsuring risk in various lines of business. Individual members and groups of members are seeking means to create capacity at an affordable cost. The top risk issues include:

- Wildfire
- Conventional Property
- Renewable Generation Property
- Excess Liability

New MBP Welcomed by EIS

Please join us and welcome Sacramento Municipal Utility District (SMUD) as the latest EIS Participant. EIS was once again able to quickly respond to a renewal deadline and help get this latest program launched. Our initial conversations with Dan Delac, SMUD's Risk Manager, began several years ago. We are very pleased Dan and SMUD found EIS as a viable alternative to address wildfire risk. Our current number of open cells is now at 18.

PAC Conference Registration is Opening Soon

Please be on the lookout for our email with your invitation and link to register for the 2021 PAC Conference. Our conference is commencing Monday, October 25. The general session will be Tuesday morning. To schedule your specific MBP PAC meeting with EIS/ECM staff, please contact Taniyka Ragland at tragland@eimltd.com. We look forward to seeing you in Charleston. If you have any other questions please do not hesitate to reach out to your Account Manager or Randy Martin.

We will make appropriate arrangements for PAC members that are unable to travel by scheduling an online PAC meeting via Teams.

Captive Optima – *Can Big Data benefit the captive insurance industry?*

The simple answer – absolutely! In a recent newsletter, this section looked at how risk financing optimization studies and a SWOT analysis can identify those attributes of your risk and insurance department that lend themselves to risk strategies, including captives or other forms of alternative risk financing. This quarter we continue with a focus on the benefits of Big Data and predictive analytics in captive insurance programs and other potential risk financing options.

There has been tremendous press coverage of "Big Data" and its implications for insurance companies, including captive insurance companies. Big Data is especially promising and differentiating for insurance companies. With no physical products to manufacture and sell, data is arguably an insurance company's most important asset. Financial data, actuarial data, claims data and risk data form the basis for virtually every important decision an insurer makes for their program. Big Data can have a positive impact on all insurance processes from underwriting, pricing, and reinsurance to risk assessments and other strategic marketing decisions.

The 5 V's of Big Data

Volume – *The huge amount of data collected and reprocessed*
Variety – *The diversity of data types and data sources*
Velocity – *The speed data is collected and reprocessed*
Veracity – *The authenticity and credibility of data*
Value – *The ability to analyze, transform and utilize data*

New advanced tools enable Big Data to handle capabilities and techniques such as predictive analytics and increased utilization of data. Predictive scoring, pricing and risk selection tools are now top priorities for data and analytics investing. Other important areas include real-time underwriting performance monitoring and management, as well as spending on third-party data sources.

For captive insurance purposes, Big Data is most beneficial in the areas of Risk Assessment, Cost Reduction, and Claims Handling.

- **Risk Assessment** – Big Data technology can increase the efficiency of the whole process of risk assessment. Before arriving at a final decision, a company can utilize Big Data and use predictive modeling to unearth potential issues and, then based on historical and industry data, put them into a suitable risk class and use the data to assess additional potential options for the captive.
- **Cost Reduction** – Big Data technology can be leveraged to automate manual processes, making them more efficient and reducing the costs spent on handling claims and administration. This will allow the captive to write lower premiums and save the insured money.
- **Claims Handling** – Big Data technology can assist in both claims management and litigation expense management. Using past liability data and integrating data analytics into the claims process, the captive can help determine liability at an earlier stage in the process. Defense costs represent a significant proportion of the overall cost of claims, and Big Data technology can review and monitor legal firms, asses the degree of complexity based on prior claims, and potentially assist with settlement for certain claims.

Many insurance companies don't use a lot of data to price their products. They rely on demographic information that is 20 years old, and older. They often struggle to price policies correctly and may miss out on huge financial opportunities. This challenge is often present in the captive insurance industry when funding and capital requirements are evaluated. The most traditional and immediate ways that Big Data is impacting the captive insurance industry is by enabling new methods to price products and simplify underwriting.

Actuaries and data modeling can play a crucial role in the development of pricing new products and analyzing the minimum capital needed to sufficiently fund a captive. Actuaries are working with data analytics in the life, health care, and property and casualty sectors, as well as in risk management and investments. Insurance actuaries are adjusting to a shifting and complex landscape, with Big Data more accessible, relevant, and abundant than ever before. The American Academy of Actuaries continues to work with insurance companies and Regulators to review and refine regulatory frameworks in which Big Data work may be appropriately governed. Non-traditional data, such as demographic data, government data, and climate data can now be analyzed to determine the appropriate funding for a specific coverage. EIS has a distinct advantage with access to EIM's in-house actuary, Legare Gresham. Legare is a Fellow of the Casualty Actuarial Society located here in our Mt Pleasant, SC office. EIS is excited to be able to engage her help, as the need arises, with our current and prospective participants for feasibility and other special projects that will support credible analysis and decision making to achieve highly efficient alternative risk financing models.

As this new era of Big Data unfolds and commercial market prices continue to increase, now is the perfect time for companies to review their insurance programs and explore additional risk financing options. EIS and ECM are able to assist with feasibility studies and through current member experience to explore expanded uses of your current EIS cell or determine if a cell within EIS is a good option for your company. There can be significant cost savings available through exploration and discussions with EIS.

Focus on Benefits – *Excessive Medical & Other Benefit Aggregation Risk*

How is your organization addressing the rising cost of medical care? Is it on a holistic basis? Medical costs impact both the health insurance for employees and their dependents, as well as the medical side of a workers' compensation claim. Additional collateral costs are typically incurred with severe illness or injury, either arising from a non-occupational or occupational event due to benefits payable by the employer for lost time from sick leave, short-term or long-term disability benefit expense, or a partial/total; temporary/permanent disability award by workers' compensation.

Most companies are retaining greater amounts of the cost for health benefits, many funding 100% (although with employee contributions) and taking higher self-insured retentions on workers' compensation, up to and over $1 million. Additionally, the cost of sick leave, short-term and long-term disability may be additional retained costs. To manage better outcomes, some Member companies have embraced integrated management to drive efficiency on medical management and lost time issues whether occupational or non-occupational related. But financially, these costs are being managed in their own silos.

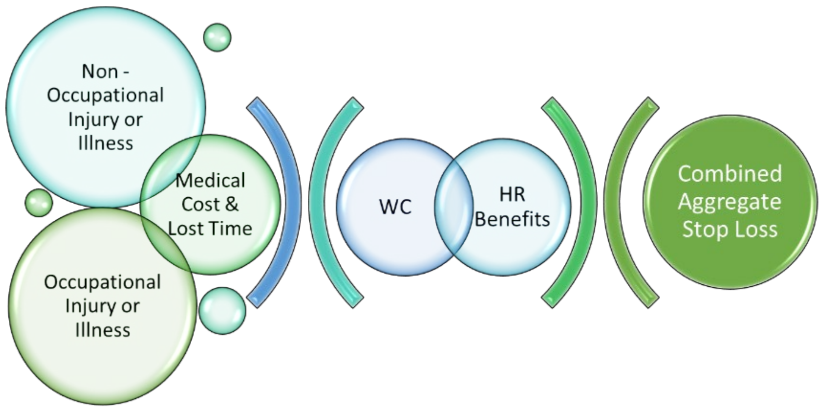
Why are we talking about this now? Now, more than ever, HR benefit specialists are being bombarded with several issues that are driving greater uncertainty in the budgeting of retained costs. To name a few:

- Health provider costs are continuing to rise 6.5% or more a year in most parts of the country
- Prescription drug costs are out of control
- Economic fallout from the pandemic is likely to have an impact on health care costs going forward yet to be calculated or imagined

- Employee transition to a work at home environment, and many will not return to a traditional office
- The opioid crisis is not over, just overshadowed by the pandemic and other social/political issues
- Social inflation on workers' compensation settlements may follow what is now happening in liability arena

Each of these issues would take a full article to review, so we are just putting these out there for now.

If there is ever a time for a benefits manager to embrace a form of stop-loss insurance or at least give it serious consideration, it is now! However, looking at traditional medical stop loss will not get you there to protect your company from the full aggregation of risk arising in all the areas in which you may be exposed. The most efficient and effective method to address these is bundling the aggregation of retained benefit coverage, modeling the loss probabilities on a portfolio basis, picking a level of cost that is unbearable and funding for a comprehensive solution in a *combined benefits aggregate stop loss* in a captive insurer.



There I said it. Yes, in a captive. Why? No market exists to provide a solution like this! Additionally, it may make incredible financial sense to your company. Similarly, your treasury likely supports the hedging of fuel and other commodities that your business is dearly dependent upon. Employees are more valuable than fuel and other commodities. Health care helps support employee satisfaction and engagement. As you know, providing an overall superior benefits package is necessary to support, attract and retain employees.

However, the company must be aware of the aggregation of retained risk and protect itself, financially, for that one year when all goes wrong and costs soar. Unfortunately, that one year is now recurring every three to five years.

Our suggested list of retained cost exposures for a combined benefits aggregate stop loss:

- Self-insured retention of workers' compensation
- Company funded employee & dependent health care benefits
- Company funded prescription drug costs
- Company funded short-term disability
- Company funded long-term disability
- Paid sick leave

Having had the privilege to view workers' compensation losses and medical costs from several EIM Members and to help model programs around workers compensation or medical stop loss, we know the aggregation of the retained costs can be staggering.

Hopefully, this will spark an idea or two. Consider putting all or some subset of these benefit risks in a captive that views these risks holistically and allow EIS to help you create a program to fund for that bad year that is coming.

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EIS Mission Statement – "To provide a facility to meet EIM Members' dynamic and specific business requirements for the placement and management of alternative risk solutions."

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