"Outstanding! David continues to break complex and often confusing subjects li ke business insurance and workers' comp down to an easy to understand level that the average business owner like myself can comprehend."
— David Striegel, President, Elizabeth Auto Care

THE 10 LAWS OF *Insurance Attraction*

How to dramatically slash your premiums while improving the performance and profitability of your company!

DAVID R. LENG, CPCU, CIC, CBWA, CWCA, CRM

The 10 Laws of Insurance Attraction

How to dramatically slash your premiums while improving the performance and profitability of your company!

by

David R. Leng, CPCU, CIC, CBWA, CWCA, CRM

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This book contains information about insurance and coverage, human resources, and safety. The information is not intended as a substitute for insurance, legal, or financial advice from an appropriately qualified professional and should not be treated as such. If you have any specific questions about any insurance matters, you should consult an appropriately qualified professional.

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For my mom, the teacher.
She continues to inspire me, and everyone who knows her,
to always try your best and never give up,
even when she faced the biggest challenge of her life –
beating cancer…

For my wife, my best friend,
you make my journey through life so much more enjoyable.

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Turning Premium Into Profits

Foreword

For many companies throughout the United States, 2008 and 2009 were bleak times. Businesses were reeling from an economic meltdown that was forcing massive layoffs, drops in productivity, and a bottom line that was barely keeping its head above water.

As the president of Duda Cable Construction, I was very much in the same leaky boat back then as most of my business friends and competitors, but with one very serious difference. On January 7, 2008, an unfortunate accident took the life of one of our workers, an event that rocked our company and me both emotionally and financially. As a result, our insurance costs surged at an alarming rate, to the point that we were paying upwards of $37,000 in insurance premiums *per month*, up from a little over $13,000 a month. After two years of increases in our costs, and despite work being readily available to us, my insurance premiums were strangling my company's competitiveness as well as my family's financial situation.

It felt like I was working just to pay my insurance premiums. Surviving as a business with these premiums was looking bleak. We needed help right away. However, the solution to my problem was not what I was expecting.

Like any other business owner, I turned to several friends to find out who they were insured with. I was also receiving quite a few calls from agents offering to save me money. Even my agent at that time, who worked for perhaps the largest insurance agency in the region, was trying to find as many options as he could. With so many agents promising they could save me money and deliver results, I thought we would be seeing a substantial reduction. I was wrong. Out of the four workers' compensation quotes I received, the second best was from the Pennsylvania State Workers' Insurance Fund. Yes, two insurance agents quoted companies higher than Pennsylvania's "insurance company of last resort." The best option was not even 10% lower than

the state fund. And all of the quotes were higher than my expiring policy.

I was about to take the "best" quote available when a business associate put in contact with David Leng. Almost immediately, he was at our location with several of his team members, evaluating our situation, looking through our books, reviewing our policies and procedures, and talking to us in a language we could fully understand. He took the time to deeply understand our company, telling us in so many words, "We're not leaving here until we get your rate down." And I could tell he meant what he said because within two months, we could see the light at the end of the tunnel.

Because of David's commitment to resolving our situation, we were able to quickly lower our insurance costs. First, he found and recovered $86,000 in errors that my old agent allowed to occur over two years, which no other agent saw. Second, David and his team overhauled our employee hiring, training, and management processes. In those two short months, David and his team were able to help us change how we operate and reposition us with the insurance companies. He made us more attractive to them *before* he went to obtain quotes on our behalf. His approach reduced our workers' compensation premium by 41%, in addition to correcting our premium errors! In those two short months, David's program put back over $200,000 in our pocket. Our situation has continued to improve, and our business is flourishing.

David and his team did a remarkable job. He literally kept us alive, and now it helps us to thrive!

What you will read in this book, combined with what you should have read in David's first book, is a road map to overcoming high insurance rates, a kind of GPS for lowering your premiums while raising both the productivity and profitability of your company. My situation serves as proof that just getting quotes is not enough to manage your insurance program's costs and that you can do better when you use a better way. I can tell you this from first-hand experience: if you are an employer and don't have David Leng's books in your office, you are putting your company at a serious competitive *dis*advantage.

Mark Duda, President
Duda Cable Construction
Vandergrift, Pennsylvania
August 20, 2016

Acknowledgments

I want to thank Linda Jovanovich, the Executive Vice President, and the members of the Hardwood Manufacturers Association, who inspired me and suggested that I write this book and whom I had the privilege of working with at their 2016 National Conference in Fort Worth, Texas.

Recently, the wood products manufacturing industry has been facing substantially increasing insurance premiums due to a combination of multiple large, catastrophic claims and a significant reduction in the number of insurance and reinsurance companies willing to provide insurance policies to them. Many of the members expressed to me that they had seen their premiums double or triple despite the fact they may have never had a claim. With insurance costs crushing the members, Linda asked for a straightforward way to help them reduce their premiums since obtaining insurance quotes was not really working for them.

The wood products manufacturing industry is facing just the beginning of a dramatic change in the overall insurance industry landscape (not just for wood product manufacturers). What they viewed as a reduction in competition between insurance companies was just the tip of the iceberg. What they failed to see was what was below the surface: **the coming massive transformative changes in how insurance companies underwrite, price, and even restrict the amount of coverage they can or will offer to a business.**

Linda expressed that the members wanted a plan to achieve better results and go beyond just trying to get quotes. After speaking with several members in preparation for the workshop, the members wanted more clarity on how insurance companies price their insurance policies and a better understanding of the overall insurance system and its impact on them. **Ultimately, they wanted to know how to lower their insurance costs. However, they came to express that they needed guidance on *how* to make their organization more *attractive* to the**

remaining few insurance companies so that they could earn better rates and slash their premiums.

The workshop inspired this book, an expanded compilation of everything touched on in that workshop and many ideas and concepts that there was not enough time to address. However, the concept of making your company more *attractive* to obtain lower premiums applies to every business, type of operation, for-profit or non-profit, etc. Therefore, the scope of this book expands beyond wood manufacturing to encompass pretty much any operation.

I would also like to thank my partner John M Duncan Jr, CIC, CWCA of Duncan Financial Group, and my colleagues Mike Lukart, CSP, CWCA of East Coast Risk Management; and Bob Seltzer, CIC, CBWA, CWCP, CWCA and Steve Stramara, CIC, CWCA of the Seltzer Group for their collaboration in building our joint *Risk Profile Improvement Process*, and our Behavior Based Safety and Employee Management Programs. These are the beginning steps in our *Employer Success Program*. These processes and programs are the basis of our ability to help companies not only slash their premiums but also increase productivity and profitability while reducing or eliminating their headaches in dealing with their insurance programs and problematic employees. ECRM is headquartered in North Huntingdon, Pennsylvania, and services clients nationwide from multiple state offices. The Seltzer Group is based in Orwigsburg, Pennsylvania.

I would not have been able to complete this book without the additional insights and suggestions of many insurance company personnel, including the underwriters, actuaries, and loss control team members of Eastern Alliance, W. R. Berkley, Cincinnati, Travelers, and Pennsylvania Lumbermens. Thank you!

Introduction

Would it be a safe bet that you have heard the following statement? *You never get a second chance to make a first impression*.

And while we are in a betting mood, would it also be a safe bet to say that you would agree with these two statements?

- *Nobody likes to pay insurance premiums.*
- *Everyone wants to pay less than they are right now.*

What do *first impressions* and *attractiveness* to the insurance companies have to do with reducing your insurance premiums? **Everything!**

Even if you have never had a claim, what you will learn throughout this book will be critical to understanding the evolving insurance industry, how it will cover your business, and how much you will have to pay for that insurance coverage.

As we continue to bet, the odds are also likely in favor of you agreeing with at least a few, or even all, of the following statements:

- *It takes a lot of time to shop your insurance, with underwhelming results.*
- *Transitioning between insurance agents is painful, and it is even more painful when changing insurance companies.*
- *There always seems to be something that gets missed. And that "something" will return to haunt you when you make a change.*
- *It seems insurance agents do not truly understand what your business does and what your needs are.*
- *You are frustrated by the ambiguous and confusing insurance underwriting and pricing system.*

Over my 25-plus years as a speaker and an Outsourced Chief Risk Officer for employers, I have interviewed hundreds of business owners, leaders, and executives. They have all expressed the frustrations I just

outlined and lamented the amount of time, energy, and/or money they have spent dealing with their insurance program.

So why do you, as a successful business owner, keep rolling the dice when it comes to managing your insurance program? Only you can answer that question, but you can take some comfort in knowing that you are not alone.

When you look at the amount of money you have wasted on your insurance program, the money you could have been better used to accomplish a specific goal elsewhere in your company, how can you not feel frustrated? You may also regret the time you have frittered away trying to obtain bids or quotes on your insurance program, only to fall short of your desired results. In doing so, you now realize that focusing on growing and running your company would have been a better use of your time and resources.

Why do you feel this way?

The answer is very simple: the insurance industry has taught employers how to purchase insurance. However, it has done so in a way that can best be described as clunky, confusing, and potentially dangerous. You experience it every year, particularly 90-120 days before your insurance renewal. This is when insurance agents seem to come out of the woodwork asking to quote your insurance, only to promise much and deliver little.

However, **business leaders are only at fault for two things:**

- Being led to believe that being attractive to all of these **insurance agents** (who simply want a commission from selling you insurance policies) is the same as being *truly attractive* to the **insurance companies**.
- Wanting, but not demanding, a better way!

But a better, more successful way to manage your insurance costs exists. Remember, insurance is your way of transferring your *risk of the unknown* to an insurance company in exchange for a known amount of money, commonly known as a *premium*.

So, the questions you need to ask yourself are as follows:

- Are insurance companies betting on or against my company's *risks*?
- What are the odds each insurance company is placing on my company's "success"?

The odds of betting on insurance are somewhat backward, as insurance companies are betting against payouts. They are trying to calculate the odds of paying out anything to you as a business (paying a claim).

So, does the insurance company view you as a longshot or a sure thing? Unlike traditional forms of betting, in the insurance world, a longshot is a good thing because the insurance company views the likelihood of something happening, where they have to pay out money to you (pay a claim), as highly unlikely. The better the longshot, the lower your premiums.

On the other hand, being a sure thing, where the insurance companies view the likelihood of paying out (paying claims) as highly likely, is *not* a good thing and will be very expensive for you.

It all comes down to how attractive you are to the insurance company (not to the agent), which influences your odds or premiums.

Whether you have 25 or 1,000 employees, *The 10 Laws of Insurance Attraction* outlined in this book will influence if insurance company underwriters view you as a better risk and, thus, deserving of lower premiums. Therefore, making an excellent first impression is critical.

However, it is imperative that your business continue to be attractive to insurance companies to maintain these lower premiums. How well you manage your company and its risks is what keeps insurance companies interested in the long term. If you do not remain attractive, insurance companies will quickly raise your premiums. Also, insurance companies have a long-term memory in the form of computer databases, which means every time they review you as a "risk," they remember everything they learn about you, good or bad. This embedded memory of your business will be in play the next time they are asked to quote your operation's insurance.

For those readers who jumped over the *Acknowledgements* in this book, you missed the reference to coming massive transformative changes in how insurance companies underwrite, price, and even restrict how much coverage they can or will offer to a business. This, too, will greatly impact how you are insured and how much it will cost you. You will learn more about this in this book.

As a fellow business owner, I am pleased to demonstrate here how insurance programs and their costs are actually controllable, much like other areas of your business. I have discovered that by addressing the areas that make you continually attractive to insurance companies, you can provide greater profits to your company and become more productive and more competitive in the marketplace.

As you become more attractive to insurance companies through better business management, you will not only receive more "competitive" insurance options, it is possible you may also no longer need to purchase costly traditional insurance.

In this book, you will learn about the world of alternative financing, such as group captives, which becomes available. And in doing so, you can take advantage of insurance programs that offer significantly lower cost structures. This is a world where you are able to take control of your insurance program just as you control your business. In other words, instead of focusing on your insurance costs as an expense, you can view it as investing in a profit center.

You may have noted that I have used a few references to odds and betting, although, truth be told, I am not much of a betting person. I am more comfortable calculating and hedging my bets. I usually enter a casino with a fixed amount of cash in my pocket and end up leaving after donating the contents of said amount to the house. Hopefully, these analogies will help you understand that actuarial calculations determine insurance rates—the odds set on your business—and will help guide you in what you can do to impact or influence those odds.

Full disclosure: this book cannot magically slash your insurance premiums in half overnight. But it *can* help you know more and accomplish more by giving you the tools you need and a better understanding of what can and should be achieved in reaching your goal

of lower insurance costs, increased employee productivity, and improved profitability. By doing so, you will be able to concentrate and focus more on successfully growing and running your company.

Know the Rules – Before You Play!

Stepping up to the table to place your chips for the first time, whether it is Blackjack, Craps, Baccarat, Roulette, or Poker, can be intimidating. Even if you believe you know all the rules, when you are playing for the first time, you probably have not had time to experience all the nuances that will help you become victorious.

As a business leader, you continually step up to the insurance table to play the insurance quotation game, letting the roll of the dice determine what you will pay. So, let us take a look at the insurance game.

Does this situation sound familiar? About 90-120 days before your insurance renewal, the phone starts ringing off the hook with insurance agents asking to quote your insurance. You invite a couple of agents in, and they say, “Oh, we’re an expert in your industry…” or “We specialize in your industry, and because of this, we understand you the best and can give you the right coverage.” They then stress, “We have great, sizeable relationships with the insurance companies so that we can get you the best rates in your industry.” Maybe they even go so far as to promise some “risk management,” “safety,” or “claims service” but do not clearly define what they will do. Face it, they are promising to offer you services to entice you to let them quote, and many business leaders later found out that these services are minimal or non-existent and are certainly not effective.

However, as most insurance agents represent a significant number of insurance companies, they all return to argue over who has the best relationship with a particular company and how they can use that relationship to help you the most. Agents will then argue that they can

best leverage in the marketplace and, therefore, can give you the best rates. Since insurance companies operate on the "first come, first serve" rule, they all argue over who will represent you to the same insurance companies by asking for an *agent/broker of record letter*.

This is how insurance has been bought for well over 30 years, and this is why I contend the system is broken. In fact, it can also be dangerous, considering the *Insurance Institute of Home and Business Safety*'s statistic that slightly over 50% of businesses that suffer an insured catastrophe cannot afford to reopen or close within three years of their reopening.[1] Consider that you could be out of business if you or your agent miss providing critical coverages – in other words, you could be paying for an insurance policy that will not pay out or enough when you need it the most. Unfortunately, this is such a complex subject that a separate book is required to explore, explain, and help you have a clear plan to avoid this.

I will repeat this in this book and explain it further a little later: **Law #1—Know the Rules—Before You Play**. The main rule you need to understand is that Underwriters do not get in trouble for not quoting insurance for a business. ***An underwriter will only get in trouble for issuing a policy for the wrong account.***

But back to the impact on your bottom line…

The Insurance Industry Is Rapidly & Dramatically Evolving

Do you do business the same way you did 30 years ago? Probably not. Chances are you may not even be doing business the same way you did five years ago. However, it is interesting to note that although insurance agents are still basically selling insurance the same way, possibly by offering a few "promises," the insurance companies are not offering or quoting insurance the same way.

This evolution of the insurance industry will affect everyone. I can hear someone saying, "I have not had any claims, so I am clearly

[1] https://ibhs.org/

attractive to insurance companies!" Unfortunately, with this evolution we will discuss, the answer is that you *may* or *may not* be attractive to insurance companies.

When I went through underwriting school as a college intern (yes, in the last century), all of the information that we went through was either provided by the agent or in a manual: loss runs, applications, drivers list, payrolls, sales, locations, property values, construction of the building, alarm systems, if buildings had sprinklers, number of employees, rating territory, class codes, etc. There were only 10-15 data points insurance companies looked at.

Today that has all changed! Now, there are hundreds of data points underwriters look at and analyze. Here are some examples:

- Experience modifier
- The ratio of claims to the number of employees
- Loss ratios by policy type
- Wages to medical claims ratio
- Number of claims with wages greater than 25,000 to number of employees ratio
- History of rulings by judges in your area
- Do you offer benefits? What percentage of employees that have benefits?
- Do you have disability insurance?
- The average age of your workforce
- Age, economic, and social aspects of your area
- The average wage of your employees (this is total wages divided by the number of employees)
- Proximity to quality healthcare
- Number of lost time claims to number of employees ratio
- The insurance companies' loss ratio and results in your area
- The insurance companies' loss ratio and results in your class of business
- Known industry trends in your class of business
- Is your area infrastructure in decline (your town's water supply, fire company)?
- The rankings/scoring of your local volunteer or paid fire company
- Can your fire company respond to the types of fires your industry might have in terms of men and equipment?
- Do you have the water supply needed to be able to fight that fire?
- Is there enough water pressure to support enough fire trucks that are needed to fight the fire?
- What does your website say about your operations and what you do versus what you "really" do?
- OSHA visitation history and findings
- Known public lawsuits against you
- Housekeeping
- How well do you screen your drivers?
- The overall score of your employees' motor vehicle reports
- Type of equipment used in delivery, distance, and duration of delivery
- Material handling issues, meaning if you have heavy products, do you have the mechanical lifting means
- Job rotation or repetitive job
- Loss controls opinion on the quality of your management and dedication towards safety and eliminating or reducing claims.
- How often have they seen a submission on your business in the last five years?
- How many times have you changed carriers in the last five years?
- New employee screening processes
- Drug testing
- The quality and dependability of the information provided by the agent
- Quality control program
- Do you have a dedicated safety professional on staff or use a safety organization that insurance companies recognize as being outstanding, or do you just have somebody wearing a safety hat or using a safety company that they recognize is only OSHA-focused and not safety-focused?
- Do you have a formal return to work? Is that evident in your loss runs/claims?
- Do you have formal quality control processes?

- Your Maximum Probable Loss
- How are your values segregated and protected?
- Fire load of your building
- Sources of combustion in your facility and your product
- Financial condition as displayed by Dunn & Bradstreet and other credit rating authorities
- Lag time in reporting claims/injuries
- Do you have formal safety programs?
- Do you have a progressive disciplinary program?
- Are pre-employment physicals conducted?
- Are pre-employment functional capacity testing done?
- Your turnover ratio
- Your Safer and Central Analysis Bureau (CAB) Report on your fleet

As you can see, what insurance companies look at goes well beyond what you may view as "insurance" issues; instead, they venture into your company's operations. They analyze your human resources, policies and procedures, environmental, regional issues, and industry-specific issues. Heck, insurance companies may now check to see if your local fire company can respond to the types of fire your business might have in terms of the number of firefighters and equipment. They even want to know if you have the water supply to fight that fire.

An example of a simple change: Let us pretend you have 40 employees, average 5 claims a year, and that you only average $2,000 in claim costs compared to your $40,000 premium. Usually, that would be considered an "excellent" *5% loss ratio* (claim costs to premium ratio).

Today, an underwriter will look at your ratio of injuries to employees and say, "You have a frequency problem – more than 10% of your employees are getting injured in a year, which is a significantly high-frequency injury rate." If this is the case, they perceive you as a higher risk than somebody with a lower frequency. The result is they will charge you more premium. However, this is just the tip of the iceberg.

They will go further. Insurance companies will examine the nature of the injuries and determine if they are a symptom of poor training or a poor safety culture. They will couple that data with turnover statistics, reviews on the web about your company, your financial score, and other data points from outside your company to create their underwriting score for your business.

The scary part is that you can check many positive boxes and feel you would score well. However, that is when you are shocked when the uncompetitive quote or “declination” comes back and frustrates you.

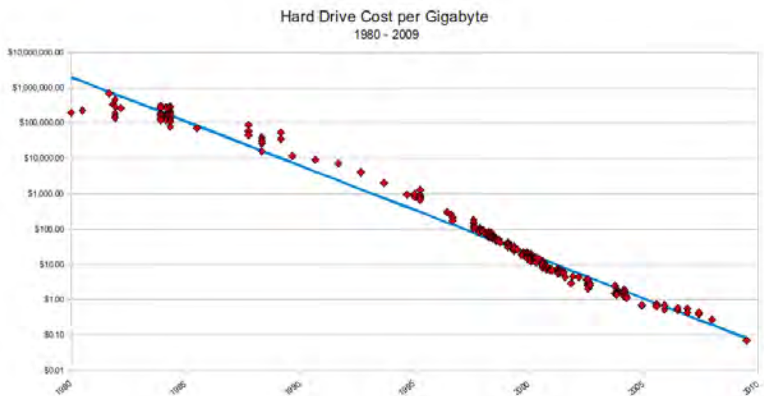
The issue is insurance companies also analyze their own experience in your industry as well as overall industry trends. If they are losing money overall in your industry, they will decline or want to charge you a significantly higher premium.

You may feel incredibly frustrated when they decline to quote or offer a ridiculous premium because your operations check one significant negative underwriting box because you do some minor thing their reinsurer does not like. It is probably something “incidental” or “less than 1% of your operations,” but still they decline or charge a massively higher premium.

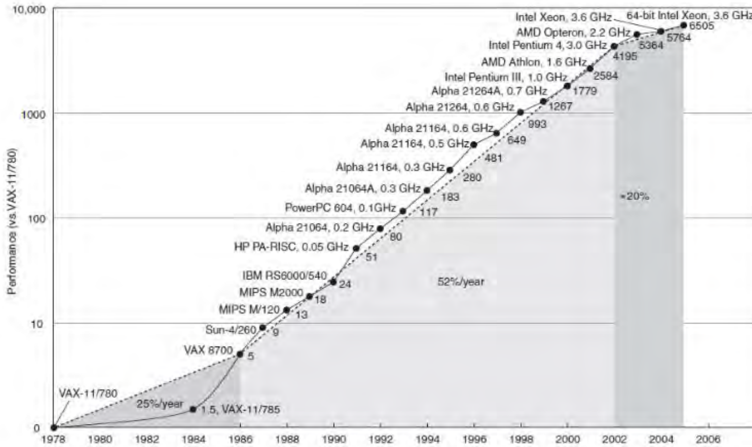
Why is the evolution occurring? <u>COMPUTERS!</u>

Let’s explore the impact computers, analytics, and actuaries have on insurance today.

1st – Storage space is dirt cheap now and getting cheaper.



2nd – Data processing speed continues to accelerate and gets faster all the time.



What does this mean? This combination of data storage and processing power enables insurance companies to gather and process vast amounts of data, which is where actuaries come into play. **It is called *Analytics*.**

Actuaries are mathematically and statistically oriented people. They love data. My alma mater, Penn State University, is cranking out 50 to 100 graduates annually in this field. These actuaries are slicing and dicing data to figure out how they can help insurance companies have a competitive advantage in the marketplace so they can grow and drive more profits to their shareholders. They are trying to figure out how to underwrite risks better so that they can become more predictable and, by doing so, become more profitable.

Actuaries are continually using this data to build a better mousetrap.

Suppose the actuaries see they have an industry, or even a narrow segment of an industry, where they can find significant profitability. In that case, they can help steer the insurance company to get more business in that industry. They will naturally become more competitive in that industry, but it ultimately comes down to them building that better mousetrap.

It is a lot like the movie *Moneyball*, which highlights how the Oakland A's built a better mousetrap for identifying baseball players. In the past, scouts would say, "Oh, that guy has a real smooth swing," or "He's really fast and makes great plays," or "He's built well and fields great." But the Oakland A's actually started slicing and dicing the data: i.e., what is their on-base percentage, their fielding error rate, how many times have they hit doubles, how often are they injured, and identified the best players from a statistical standpoint. They then weighed this information against their payroll and built very competitive playoff teams while staying among the lowest payrolls in Major League Baseball.

Sports commentators have referred to the NHL's Arizona Coyotes hiring of 26-year-old John Chayka as "Moneypuck." Gary Drummond, President of Hockey Operations for Phoenix, said, "John is among the best and brightest minds in hockey. He is knowledgeable and driven and has an incredible passion for the game. He brings an innovative approach to assessing talent and looking at player development, and combined with his strong analytics expertise, we feel that he's the right choice for the direction we want to go with our franchise." Notice the emphasis on *analytics*.

Just as the internet impacts almost every portion of our lives today, it also impacts premiums and underwriter perception. Underwriters can research and find large amounts of data and information about your business. They will rely upon it to make decisions, regardless of whether the information is accurate or not. I will tell you this: if you are not participating with Dunn & Bradstreet, you are in trouble as insurance companies financially score businesses via independent financial scoring companies. But more on that later.

When it comes to your website, bragging about certain things you do that you really do not do to make your company sound bigger and broader than it is may cause the insurance company to have a negative perception of you. This is particularly true if the insurance company underwriters do not like the risk in what they see.

The Insurance Services Office, the largest surveying organization in the country, sells its inspection reports to any insurance company

willing to buy them. They sell them for an amount that is less expensive than it would cost the insurance company to send their own employee to do the inspection.

The questions then are: what is the quality of the inspection, and when was the inspection last completed? It could be years old and very outdated and incorrect. Keep in mind computers have indefinite memory; something that you may have had as a negative risk years ago, such as a bad piece of machinery that did not have proper guarding, may still be out there, even though the machine has long been fixed or even replaced. That speaks to the quality of your submission, an underwriter's decision on quoting or not quoting, and the amount of premium they want to charge.

Underwriters gather and stick your business's data in the actuary's mousetrap model. Even with zero claims, they will not offer you insurance if your data does not fit their model. If your business somewhat fits their model but does not match their ideal risk, they will charge you significantly more premium.

Let us examine what affects an underwriter's decision to quote you and the pricing they may offer.

Maximum Probable Loss

An understanding of *Maximum Probable Loss* may provide some clarity on insurance company underwriting. *Maximum Probable Loss* can make a significant impact on your insurance. Most insurance companies use *Maximum Probable Loss* to determine if they can or cannot quote/write your insurance. They do this by adding your building and its contents, your business income, equipment coverage limits, and basically everything on your property policy that they will insure.

The insurance company is trying to determine the most amount of money they may have to pay out should you suffer a catastrophic loss/claim. Based on this amount,

Pretend you have three $10-million buildings, including what is inside (equipment, stock, materials, furniture, etc.), that are close

together. The insurance industry may view your *Maximum Probable Loss* as $30 million.

Suppose you have significant space between those buildings, with no materials stacked up between the buildings, which would help a fire to spread between the buildings. In that case, your *Maximum Probable Loss* may be viewed as $10 million.

Depending upon your scenario, including the construction of your buildings and/or the presence of a properly maintained and designed fire sprinkler system, an insurance company may or may not want or be able to write your insurance if your *Maximum Probable Loss* is too high.

This wider spacing of the buildings reduces *Maximum Probable Loss,* which increases the number of insurance companies that can quote your business insurance and leads to lower rates as well.

However, that scenario was for fire. What about another potential risk, like a tornado? That further spread of buildings would still be considered too close, and your *Maximum Probable Loss* would be back up to $30 million.

With changing weather becoming increasingly concerning for insurance companies, the age, construction, and maintenance of your building will become critical in determining the pricing of your insurance or even whether you can purchase insurance.

That's dealing with property insurance. However, the same issue of when an insurance company can or will accept as a liability insurance risk is also evolving. With the dollar amount in lawsuit demands growing and the ridiculous awards from juries climbing rapidly, insurance companies are starting to look at how much they can pay out in a single lawsuit in various industries or with certain exposures.

For example, you are a machine shop. Depending upon what and where your parts go, insurance companies may or may not offer liability insurance or limit how much they will offer. However, if you have vehicles that deliver, they may view you as a trucking risk and limit how much liability insurance they will offer.

That is unless you can *PROVE* to them that you are indeed "best in class." Having few or zero claims does not do it by itself. A "robust safety manual" you can show them is not enough. Talking a "great

game" falls short in the new underwriting world. All your data, the evidence they find, and the insurance company inspection must demonstrate that you are truly on top of your game.

Why is this so important? <u>REINSURANCE!</u>

Whether you are familiar with reinsurance or not, reinsurance drives the insurance marketplace.

Every insurance company is in business to make money. Every insurance company realizes that a significant or catastrophic claim, however rare or unpredictable, can quickly negatively affect its profitability. Therefore, to help more predictably make a profit, insurance companies realize they can only take on so much risk before they can no longer insure a particular business without help.

Once they determine the size of a large or catastrophic claim before it has too great a negative impact on their profitability, they must either draw a line in the sand and say, "We can only offer X amount of coverage," or they have to ask other insurance companies to help them insure their business.

Therefore, to work with larger businesses, insurance companies must buy insurance to spread their risk to other insurance companies. These other insurance companies are *Reinsurance Companies.*

However, the reinsurance insurance company(ies) your insurance company uses will have established rules of their own as to what types, sizes, and risks in terms of businesses they are willing to share in. Suppose your *Maximum Probable Loss* claim payout is X, and your insurance company cannot, or will not, write more than X. In that case, they will purchase reinsurance if the reinsurance company shares in the risk with your insurance company.

Suppose, based on what you do, or the makeup of your risk, causes your insurance company to need to buy reinsurance, and their reinsurer will not offer to share in your business's risk. In that case, the insurance company will decline to quote or provide insurance.

In some cases, an insurance company may offer to only participate in a layer of your insurance program up to a certain amount or

participate in a percentage of your total *Maximum Probable Loss,* with other insurance companies taking the balance of the coverage percentage.

Example #1:

- You are a fabrication shop with a Masonry Building with a Steel Roof but no sprinkler system.
- You need $10,000,000 of coverage, and the insurance company believes your *Maximum Probable Loss* is $10,000,000.
- An insurance company considering offering you insurance can only retain (or offer) $5,000,000 of coverage.
- Their reinsurance company will only offer an additional $5,000,000 in coverage but charges a higher rate due to the risk.
- Your insurance company can offer you insurance, but the premium may not be as competitive as you would like.
- However, using the same scenario, you require $15,000,000 of coverage. They could not offer you coverage as your building is not sprinklered. Or, they would have to buy very expensive reinsurance, and the premium they offer you goes up dramatically.

Example #2:

- You are a fabrication shop with a Masonry Building, Steel Roof, and a proper sprinkler system.
- You want $15,000,000 of coverage, and the insurance company believes your *Maximum Probable Loss* is $10,000,000 due to the sprinkler.
- Your insurance company can retain (or offer) $10,000,000 of coverage.
- Your insurance company may or may not purchase reinsurance for the additional $5,000,000 based on its internal underwriting rules.
- Your insurance company can offer you insurance and do so competitively.

Example #3:

- You are a fabrication shop with a Masonry Building with a Steel Roof and a sprinkler system, but the sprinkler system does not meet current requirements for what you do (either inadequate density or water flow issue).
- You want $15,000,000 of coverage, and the insurance company believes your *Maximum Probable Loss* is now $15,000,000 due to the deficient sprinkler system.
- Your insurance company can now only retain (or offer) $5,000,000 of coverage.
- The reinsurance company is willing to offer only an additional $5,000,000 in coverage at a higher rate due to the higher risk.
- Your insurance company will decline to offer you insurance, or they will have to find another reinsurance company to be able to offer a quote.
- Even if they do, adding an additional insurance company will make them even less competitive.

The same scenarios will play out in each of these examples, even if you have never had a claim before.

Simply put, **your past is not a 100% guarantee of your future when predicting catastrophic claims.** Using data analytics, underwriters are trying to determine the odds of your business's success in the future and bet that you will not hurt their bottom line. Yes, if you made money for insurance companies in the past, that is a plus. But if they see something within your operations they believe creates too much of a risk to take, they will not offer insurance or will have to purchase more expensive reinsurance to be able to accept the risk. This costly reinsurance will drive up your insurance premiums.

As you can see, by improving the quality of your risk by having a proper sprinkler system, insurance companies can insure businesses with higher values because a sprinkler system will dramatically reduce the likelihood of a total loss and, therefore, reduce the *Maximum Probable Loss*.

Reinsurance enables insurance companies to insure larger risks. However, if you cross their insurability line, you will need to find a different insurance company to insure you. The focus on data analytics is just beginning to create a problem where only a small number, or even worse, no standard insurance company, will insure certain risks.

The evolution of data analytical insurance underwriting is also playing out with reinsurers. Reinsurers are looking at the types of risk, be it size or industry, in which they do better or worse. Their choices will impact the traditional primary insurance companies will be able to offer.

As we are already seeing play out in the wood products manufacturing industry, which clearly can be a higher risk, other industries will eventually fall into “higher risks” as the reinsurers look at their data sources and change their underwriting models.

This evolution will become even more evident when reinsurers identify certain underwriting scenarios or industries as being too risky. At that point, traditional insurance companies will want nothing to do with certain types of businesses. At that point, you may have to pay significantly more for your insurance through non-traditional (a.k.a. surplus lines) insurance companies.

However, the reinsurers and analytics impact more than just property insurance. *Maximum Probable Loss* also affects the pricing of your liability policies (auto, general, umbrella, directors & officers, employment practices, cyber, etc.) If the underwriter views you as having a greater likelihood of a large claim. It impacts the underwriter’s decisions and pricing regarding workers’ compensation as the amount the insurance company has to pay on your behalf for medical and wage loss of injured employees is *unlimited*. The larger the amount the underwriter views as a potential payout (claim), the greater the premium they will want to charge or potentially not even offer insurance.

When negotiating with underwriters of various insurance companies, there are certain areas of a business that the underwriters want to assess or score. For example, when they look to quote property coverage for a business, underwriters will want to understand how well

a business controls what could lead to a potential fire or explosion, mechanical breakdown, or some other type of damage to a building, equipment, or inventory. The main areas that they will want to assess are:

- Company Culture & Management's Involvement
- Employee Management
- Hiring, Screening, Training, & Safety
- Housekeeping
- Policies & Procedures, Processes
- Facility & Equipment Maintenance
- Welding & Painting
- Sprinkler System, Fire Protection, Water Supply
- Your Company's Financial Stability/Outlook

What is interesting is that if you have the same conversation with insurance underwriters and loss control professionals when it comes to general liability, auto, workers' compensation, etc., they all focus on the same areas as the property coverage, except they add the following to the equation:

- Injury Management
- Fleet & Driver Safety
- Quality Control

If you really think about it, all three of these additional areas fall into Employee Management. When it comes to the various categories underwriters are assessing, they are not isolated areas or mutually exclusive areas. Each area is rather broad, and they continually overlap.

Examples:

If your manufacturing or process involves dust, housekeeping, policies and procedures/processes, sprinkler system/fire protection/water supply will all be heavily scrutinized. They will look at how well you manage the accumulation of dust, how often

and deep you clean, how well you maintain your dust collection system, how proactive you are in maintaining your equipment, and whether you have a properly sized and maintained sprinkler system.

Housekeeping, Policies and Procedures/Processes, Employee Hiring, Screening, Training, and safety will be examined in the healthcare industry, as employee and patient safety and well-being are priorities.

Management Involvement/Company Culture and Employee Hiring, Screening, Training, and Safety will affect how an underwriter prices your Directors and officers, Employment Practices, and Cyber policies.

As you will learn throughout this book, there is a correlation between how well you hire, train, and manage employees and what you will receive in terms of your insurance premiums based on those criteria. However, the number one thing all insurance underwriters have stressed to me from their standpoint in determining the quality of a business and rates that they would use to quote a business' insurance was *company culture*. Insurance companies want to know if ownership and management are involved and to what level. Is that involvement evident when they look inside the facility and observe its operations and its employees?

On upcoming pages, we will delve even deeper into these key areas and other essential issues that may impact your insurance premiums and your company's overall performance and profitability.

Stacking The Deck In Your Favor

You probably have heard the saying, "The house always wins." That is because the house knows and sets all the rules. Since they know the odds, they can then stack the odds in their favor.

Insurance odds are not as finite as Blackjack, as they are more subjective, like horse racing. However, the horse racing odds are still calculated, so the house wins more than it loses. That is true of the insurance industry as well. However, you *can* influence the insurance odds makers (underwriters), as you will learn throughout this book.

Ultimately, what business leaders I have had conversations with over the years wanted to know the most was how to reduce their insurance rates. When speaking with executives, I always ask, “Would you agree or disagree that your premium is based on the insurance company’s perception of your risk?” Without a doubt, they all agree.

Although underwriting has changed over time, the underwriter’s perception of your risks, or your *Risk Profile*, continues to dominate how an underwriter determines your premiums. What has changed are the sources of information that influence the underwriter’s perception.

While in college, I participated in a summer underwriting internship at an insurance company. I went through the insurance company’s commercial underwriting school and was fortunate enough to work with their most senior underwriter after the initial training. He was regarded by many of his peers as one of the best underwriters in the industry and became a mentor to me.

To this day, I remember my first account, which was submitted by one of his agents. It was a submission for a large construction company,

and I vividly remember poring through the details of the account. Included in the submission were the industry standard applications, the insurance company's supplemental, and a rather thick packet of loss runs.

The agent had called the underwriter (and me) to discuss the account. The discussion revolved around the type of work the contractor performed, how most of their claims were a "bit of bad luck," and the largest claim was a "shock loss." The agent mentioned that they were a very safe contractor. He then expressed that he had a "great in" at the prospective client and that we had a "great opportunity" to write the insurance as the employer was very upset with his current agent and wanted to switch companies.

After going through the loss runs, my first reaction was to question whether the insurance company should even provide a quote to this contractor based on all the claims. They had claims across the spectrum of policies: auto accidents, defective construction liability claims, damaged and stolen equipment, and injured employees. This account was not a very good risk. They had not only had a large number of claims but also had a number with substantial amounts paid out. When I pointed this out to the underwriter, he smiled and said, *"David, **there are no bad risks; there is just the wrong premium**. You can write any risk you want so long as you get enough premiums for the risk by pricing the risk correctly or structure the coverage to limit how much we have to pay out."*

He then instructed me to call the agent so we could ask questions to understand what his prospective client has been doing to address the claims and prevent them from reoccurring. Unfortunately, the agent did not provide enough solid details on what was being done to address the claims and risks. The underwriter informed the agent that we would not provide a quote unless we could get more information. The agent proceeded to press the underwriter. The agent believed he could still have this prospective business become his client if we just provided a quote.

I was surprised when the underwriter pulled the large electric calculator with a paper tape roll over from the corner of his desk, looked

over the loss runs, and punched some figures into the calculator. He then informed the agent that any quote offered would probably be in a certain premium range and asked if we should proceed to finalize a quote. The agent responded that the range was 25-30% higher than the prospective client's premium. The underwriter asked the agent to get him more details, and he would revisit the submission. In the end, we did not receive any more information, so my first account went down as a disappointing "declination."

You might find it interesting that the next time the agent spoke to us, he informed the prospect that he could not find a company willing to be competitive with their expiring premium and that the agent found out that the prospective client's premium increased 38% that year anyhow as everyone else also quoted higher premiums.

The two key takeaways from my experience during that summer underwriting accounts are as follows:

- If you really want to drive down your insurance rates, you must improve your *Risk Profile*. It is a straightforward concept, but it requires time, effort, and attention to detail.

- **Underwriters do not get in trouble for NOT quoting an account. An underwriter will only get in trouble for issuing a policy for the *wrong* account.** They could be "called to the mat" after a big claim or after loss control pointed out something serious that was previously unknown and asked, "Why did you write this account?" or "Why did you price this business so 'low'?" So, conveying the details and the quality of a risk is *critical*.

Many business leaders believe that an insurance quote is simply based on their payroll, sales, number of vehicles or property value, and the insurance company's rate. This is why most executives believe they need to get quotes from multiple companies to determine which has the best rate. On the surface, this may appear true, but when most

executives learn how the rate for their business is actually determined, they are rather surprised.

An insurance company typically has several subsidiary insurance companies in their 'family' of companies. Each of those subsidiary companies has its own rates. I can think of one insurance company group that has 14 different subsidiaries. Each of those 14 subsidiaries has different rates, ranging from the lowest filed rate in a state to the highest filed rate in that same state. This range of available rates is designed to give the underwriter the flexibility to choose which companies and rates to use. In addition, the underwriter can apply credits or surcharges to decrease or increase that rate further. As you see, the underwriter must go through a process to decide which rate they will finally use for a quote.

Maybe there is another way to understand how risks and insurance company pricing are calculated. Since this large company with 14 subsidiaries has the lowest filed rates, there is no reason they cannot be "competitive" enough to write and keep every business in operation today if quoting insurance was all about finding the insurance company with the lowest filed rates. However, this insurance company does not write for the majority of businesses.

Why is that? Because they match their rates to what they *perceive* to be the risks of that business. They will use a higher rate tier if they perceive your risks to be higher. Therefore, they do not always use that lowest tier. In fact, I have been told that they have more business in their highest rate tiers than their lowest.

In reality, you can see that the underwriter determines the premium they are looking for based on the risk of your operations. The underwriter then backs into the actual rate they will use. As you can now clearly see, your premium is derived from what the underwriter perceives to be your organization's risk, namely your *Risk Profile*. To help you visualize how an underwriter looks at your business to calculate your Risk Profile and to determine the premium they will charge to insure you as a risk, I created the following conceptual premium formula:

Your claim costs over 5 years	+	Perception of additional potential risks and claims	–	Perception of how much you improved your risk and addressed claims over the past year(s)	=	**Your Risk Profile and Premium**

So, what is your Risk Profile?

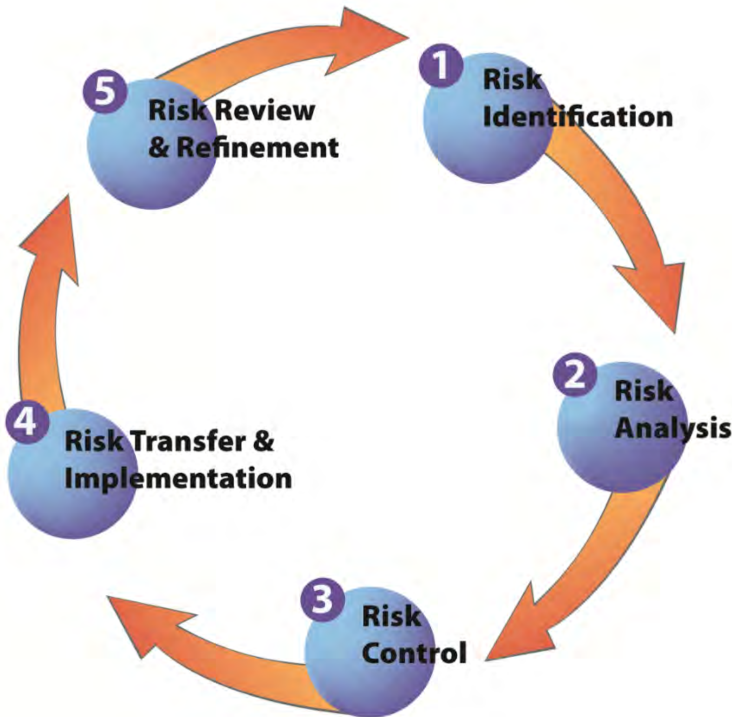
When you take time to improve your Risk Profile and reduce your risks, you will ultimately drive down your rates. When you reduce your risks, you improve the safety and quality of your operations, reducing the frequency and severity of injuries and accidents. When you reduce your risks, you improve quality control and your policies and procedures, which will reduce the number of incidents and lawsuits. Everything we are discussing revolves around your perception of your Risk Profile.

Going back to the previous chapter, where we discussed how insurance agents come in and focus on the financing of your risk or insurance by asking, "Can we quote you?" when what they really mean is, "Can we find holes and gaps to cover your risk and basically sell and up-sell you?" I believe you are beginning to see more clearly why I believe the traditional insurance shopping, or quoting process, is not truly beneficial to an employer.

It would be best if you got out of the quote and hope trap and the poor results it yields. It takes years to pass so that the claims that have already occurred and appear on your loss runs fall outside the *"Your claim costs over five years"* window most underwriters look at. Therefore, the quickest and best way to reduce your rates in both the short and long term is to focus on impacting the underwriter's *"Perception of how much you improved your risk and addressed claims over the past year(s),"* and you can only do so by focusing on the entire Risk Management Process.

The Risk Management Process is a five-step ongoing process that involves:

- Risk Identification
- Risk Analysis
- Risk Control
- Risk Transfer and Implementation
- Risk Review and Refinement



Many insurance agents jump directly into step four, risk transfer and implementation, by quoting your insurance and transferring that risk to an insurance company. Sadly, they do not spend the time in the risk identification phase. (We will discuss more on what the agent's role should be in Law #9)

Yes, agents may identify some exposures or potential claims, but their focus is to try to sell you coverage. If, ultimately, you are going to buy coverage, whether for primary coverage or to cover excess losses if you are self-insured, you will pay a premium based on your risk.

If you are bidding out your insurance and have not addressed your risks, you may have purchased coverage at the "best" quote that year. But you are still going to pay a higher premium based on the perception of a higher risk. In other words, you will pay a higher premium than if you had "proper" controls to minimize that risk.

If you control your risk well enough, the question becomes: Does it even make sense to purchase insurance coverage for that risk?

As we go through the steps of the Risk Management Process, it may be easiest to understand the complete process by providing you with a general overview of how my team goes through this entire process when working with our clients. There is no right or wrong way to go through the process, but do not skimp on the process. Make sure you go through each and every step thoroughly.

Step One: Risk Identification

During this step, you really need to dig in and identify all the risks inside your organization. Our initial Risk Management and HR Assessment is a lengthy process, but it is not overwhelming to our clients as we probably spend eight or nine times the number of hours that our clients spend in the process.

It is a critical initial step because if we do not identify the risks and gather good data, we cannot analyze them and figure out how to control them best. We can also not determine how best to deal with this risk through better controls, transferring the risk to a third party, or even buying insurance.

Let us jump ahead a little. If we decide to buy insurance for something, if we have not first identified the risks and understood them, how can we clearly explain to an underwriter how we improved this risk to get better rates?

When we work with our clients, we invest hours upon hours of our time gathering and analyzing data. Steps include a thorough loss analysis, looking at OSHA logs, and interviewing key employees to understand better the risks they see in the organization. We then review their current safety programs, compliance, claims reporting and management process, quality control procedures, and HR, including the

hiring and orientation process. We tour and analyze the facility or job sites. We do all this to understand a particular business and identify its associated risks thoroughly.

In this stage, it is important to be open and honest with yourself or an outsourced risk manager about your entire organization and its inner workings. If you do not identify the risks, you cannot address them. Trying to ignore or hide a risk is equivalent to sticking your head in the sand and hoping something bad does not happen.

I became friends with a business owner who loves to tell me sayings and stories he learned from his dad and granddad. One of the first sayings he conveyed to me when I met him was that his dad always told him to *"Keep his insurance agents like mushrooms – in the dark and feed him sh##!"* When we first met, his premiums were exploding. At that time, he realized that hiding things caught up to him as, eventually, insurance companies did see what he was not openly sharing about his company. Ultimately, insurance companies will see your risks through your loss runs, or they will see the risks during a loss control inspection of your business. Either way, underwriters will rate you according to those risks.

When we dig into your operation, we will conduct a five-year or more *Loss Analysis* of your incidents. This applies to your entire organization, including workers' compensation, general and auto liability, property, etc. We are looking for the totality of the risks that impact your business. For example, a poor fleet safety program or frequent fleet losses are important because vehicular accidents can injure your employees and damage products being delivered.

We will look at five years of OSHA logs (OSHA 300s and 300As), as well as your accident/incident and near-miss investigation reports. We are going to look through your employee handbook and review your safety manuals, fleet safety program, safety committee and training schedule notes, and policies and procedures. We will understand how you hire new employees by reviewing your employment application and employment packet, how you orient and train your new employees, how you conduct your safety programs, and how often.

Conducting a *Loss Analysis* will enable us to determine the origin of claims and injuries and the causes and types of claims. Eventually, this will allow us to know where to begin our focus on prevention. By understanding what changes or processes you implement following those claims, we can see the holes or problems in your policies, procedures, and programs. We will determine if you have problems with individual employees who are frequent claim repeaters, causes of claims, or a possible problem area of your operations. We may have them go through a program specifically directed at reducing the potential of a repeater becoming injured again.

We conduct an *Experience Modifier Analysis*, where we look at your experience modifier worksheets to understand how your experience modifier was calculated and verify if it is correct. We can then determine what is needed to improve your injury management and return-to-work processes so we can improve your future modifier calculations. What I find interesting is that occasionally, we even find claims reported on a business's modifier from another unrelated employer. If so, then you are being overcharged.

Even a thorough *Coverage Analysis*, such as a review of your insurance policies, is essential. Believe it or not, your insurance policies are a good place to understand some of your risks. Your insurance company has identified certain risks they list, schedule, or cover on your policy. For example, we would learn how many vehicles you have, what type and size (weight) they are, and their use through their classification codes. These are all on your policy. Based on the size and nature of your fleet, controlling the selection of drivers and conducting fleet safety will be critical to your overall risk profile.

Interestingly, in addition to identifying risks and adding endorsements to your policy to provide specific coverage for those risks, an insurance company may also have identified particular risks and added an exclusion to the policy because they do not want to cover them.

I cannot count how often we have conducted a *Coverage Analysis* and seen policy exclusion endorsements relating to something material in a business' operation. In these situations, the insurance company identified a risk, determined they were uncomfortable with how it was

addressed, and decided to exclude coverage. Remember, the underwriter I learned from said they could insure any business by charging enough premium *or controlling how much coverage they offer.*

A *Contract Analysis* of your contracts and leases is also necessary. It is essential to understand what risks you have contractually taken on and those you are attempting to transfer to others. This is especially true of those you have signed that may not be "insurable."

In addition, an analysis of your past insurance company's surveys and recommendations and your responses can shed some light on what risks you are facing.

Even a *Fleet Safety Analysis* of your DOT and audits, SAFER and CAB reports, driver screening and eligibility criteria, and driver training and monitoring (telematics) processes should be reviewed if you have employees driving on the roads.

We will conduct a *Facility and/or Job Site Analysis* for every busines*s*. When touring a facility or a job site, we can see everything you do in action: your housekeeping, safety, maintenance, quality controls, revenue production, and employee performance.

The goal is to help you better identify your risk and minimize or eliminate the issues to ultimately drive down your costs and increase your profitability over expenses. After gathering all this information through employee interviews, data, coverage loss assessment, and analysis, we conduct a risk analysis.

Appendix C lists the items that typically would be examined as part of a risk identification process. Online checklists are also available to help with this process.

Step Two: Risk Analysis

After developing a thorough understanding of your business, industry, corporate culture, operating procedures, and the risks your operation faces, you are starting to move beyond insurance and towards Risk Profile improvement. In the Risk Analysis stage, we determine the potential impact of those identified risks by measuring and prioritizing them so you can determine if it makes sense to address a certain risk

now or later and, eventually, how much time, money, and effort should be spent on dealing with a certain risk.

Risk Analysis & Prioritization Scale

Severity			
	High	III	IV
	Low	I	II
		Low	High
		Frequency	

When in color, this is a **Risk Heat Map**. You would shade your business's risks from dark green in the bottom left, becoming lighter and shifting to yellow before turning to light and then dark red in the upper right.

The vertical is the severity of the risk's impact; the horizontal is the likely frequency at which the risk may occur. By placing each risk in one of the above four category grids, you can better focus on where to begin your Risk Control or Mitigation.

The risks in Box IV have the biggest potential impact on the operation and deserve first priority. Next, focus on risks in Box III and II. Those risks in Box I are a low priority.

Step Three: Risk Control

During the risk control phase, we determine which programs and processes are most effective in reducing the frequency and/or severity of that risk and ultimately reduce the total cost of risk to the organization.

It would be best if you took the time to understand and analyze each risk you identified. When determining how best to control the risk, it is

cost versus benefit for an organization. The goal is to have controls in place for each risk, enabling you to move that risk from Box IV to a lower-risk category of either Box III or II. Eventually, you want to have programs and processes in place to move as many risks down in category from III to II, or II to I, and eventually as many of those risks to that of Box I as you can.

In a bit more detail, you would likely retain a small, infrequent risk that rarely occurs and has very little consequence to it. Why pay insurance premiums to cover this small probable risk? You would not need to spend much time addressing or controlling this risk. Whereas, if that small risk occurs frequently and consistently, you would focus on determining the best way to control the risk by preventing it from occurring or reducing the frequency of the occurrence. Eventually, you may want to retain that risk rather than pay an insurance company to insure it.

On the other hand, if you have a significant risk, it is obviously something you would not want to retain. You would purchase insurance or reinsurance for this risk. Please remember the insurance company is charging you a premium based on their perception of this risk. Therefore, by digging into the risk and figuring out how best to control it by reducing the potential severity and/or its likelihood of occurring will yield lower premiums.

Explore a spectrum of proven alternative strategies to minimize risk. Whether it is behavior-based safety, training education, physically changing a job, transferring (subcontracting) the risk contractually to another party, or even avoiding the risk altogether, the goal is to improve your Risk Profile and perception of risk and dramatically reduce your insurance costs.

Step Four: Risk Transfer and Implementation

Once you complete these steps, it is time to implement the risk control programs and processes geared at reducing the frequency and/or severity of losses and then conduct your risk transfer. The implementation consists of tailored programs and strategies designed to reduce those risks, ultimately reducing insurance costs. In fact, if you

reduce a particular risk enough, you may be in a position where buying insurance for that risk no longer makes financial sense. Retaining a specific risk may enable you to save money you would have paid to insure that risk.

Once you implement these programs and processes, it is time to implement your negotiating advantage in the insurance marketplace. You will now be able to leverage how you have improved your risk profile better. The minus in the equation is the perception of how much you have improved your risk over the past year or years. You need to clearly and precisely convey to the insurance companies the improvements you have undertaken that will ultimately drive down the rates insurance companies charge.

This is also the time to look at insurance programs. You want to look at alternative financing arrangements, which we will discuss in the last chapter, Law #10, with items such as captives, high deductibles, and other strategies.

You may not realize it, but this is where most insurance agents start the process and focus on selling you coverage to earn a commission. However, in comparison, we are in the fourth step of improving your Risk Profile, which will ultimately yield better results.

Step Five: Risk Review and Refinement

In step five, we evaluate the effectiveness of your risk management programs, practices, and resources under real-world conditions to ensure the programs and processes work correctly. Remember, risk management is an *ongoing* process. You must continue to determine if your programs are working. If not, then adjust them. You also want to identify new risks and analyze and control them by implementing new programs. If you do not control your risks, you are susceptible to the risks controlling you.

The idea behind Risk Profile Improvement is to go through the entire Risk Management process cycle and continue doing so. How do you know if your insurance program is adequate and meets your needs if you do not go through the entire Risk Profile Improvement process and the Risk Management cycle?

We will talk about agent selection in Law #9. If your agent is not looking and asking for this information, how can you make certain this agent will understand your company and be able to respond to your needs? Suppose they do not look at all this information. How can they truly help you improve your organization's Risk Profile and ultimately reduce your overall insurance premiums and total cost of risk? And, if they do not look at all this information, how do you know if they even designed the right retention or insurance program for you?

I mentioned in the previous chapter why the insurance purchasing process is broken. Agents jump in at step four of a five-step program, hoping to place a policy and get a commission by doing exactly what they asked you, i.e., "Do you want us to quote your insurance?" The problem is that "Quote and Hope" is not a sound risk management strategy.

Although they claim to get you the best rates, they do so solely based on the information you provide.

You will be greatly rewarded for taking the time to complete the entire Risk Management cycle. You will achieve outstanding results similar to our client's.

Another way to look at the Risk Profile Improvement Process, or the Risk Management Cycle, is to look at large companies. Large box stores, retail chains, multinational manufacturers, banks, and other nationwide companies have an individual who only wears the Risk Management hat. They have a Risk Manager or a CRO (Chief Risk Officer) on staff. They and their team focus 24/7/365 on identifying, managing, controlling, and implementing programs to address risk.

These large multinational companies have the same exposures as your business, just more of them. They also have to hire, manage, keep safe, and potentially fire employees. They have an entire department staffed and at their disposal to help with those processes. Still, most businesses do not have the resources to have a full-blown Risk Manager or Risk Officer on their payroll. This is why somebody must wear that Risk Management hat for your organization. It can be you or someone outside your firm, but they need to assist you through the process of identification, analysis, control, transfer, implementation, and risk

review and refinement. By ultimately focusing on your risks, you will be able to drive down your premiums.

A Word of Caution!

When you are going through this process, do not bite off more than you can chew. The whole idea is to have continual small improvement; the Japanese refer to continual small improvement as *Kiazen*. Strive to improve your risk by just half a percent or one percent each month. This may not sound like a large amount, but you will accomplish huge improvements and results over time. I have met with organizations that attempted to implement too many programs simultaneously. The long and overwhelming employee training of many new programs leads to confusion and frequently leads to an increase in the very injuries they were trying to prevent.

After you have conducted your risk assessment and measured and prioritized your risks, you want to start addressing them one at a time. You may be able to tackle some of these risks as a group, and you may have to address some individually. You just need to complete them one by one by working through the prioritized list of risks and putting your processes in place.

Example

I was referred to an organization by their CPA as he believed his client's costs were out of control when it came to their insurance. The CPA could see the impact the higher premiums had on the financials. However, he did not have a good reference to determine why the premiums were climbing faster than his client was growing. The CPA astutely saw that an analysis was necessary to determine the cause.

We met with the business owner about mid-year during their policy period. When we sat down with this business owner, we found that they would obtain quotes every year. They showed us all of the quotes they received for eight straight years. Despite receiving multiple quotes where the premiums were exponentially

increasing each year, the owner believed the insurance company they were insured by was "the best company for them." While reviewing the quotes, we quickly saw their experience modifier had been climbing the past four years, and the insurance company's rate was higher than average. Therefore, it was easy to see that their Risk Profile was deteriorating in the eyes of the insurance companies.

We conducted our Risk Management and HR Assessment to identify the risks and issues they were facing. We identified several problems during this assessment and started analyzing some of the larger ones. We were able to do this very quickly as several were related.

You may find it interesting that we were able to have conversations with several of the insurance companies that had quoted them in the past but were always higher in premiums. Based on their perception of risk, we asked these insurance companies what programs or processes they would like to see put in place before renewal so that they could give additional consideration when rating the insurance next year.

A few insurance companies had identified some of the same issues we had identified. With this business, they had a very large fleet of heavy delivery trucks with many motor vehicle accidents. When reviewing it, we saw that the company's driver selection eligibility program was not utilizing best practices. Struggling to hire and retain employees, the company did not qualify or screen their drivers, so many drivers had poor driving records because they pulled motor vehicle reports only to see if they physically had a valid license.

From a *"Perception of additional potential risks and claims,"* the number of poor driving records led the underwriters to believe that the company drivers would continue having accidents. Thus, the insurance companies wanted to charge them higher rates.

Working with the employer, we established a robust driver selection and eligibility program. We implemented and conducted employee training for a fleet safety program, including defensive

driving. The employer was even willing to install a relatively inexpensive vehicle monitoring system (telematics) by tracking the company-provided hands-free cell phones. This enabled the employer to know where their vehicles were, their traveling speed, and where and how long they were stopped. The program also identified if a vehicle was driving more than five miles per hour over the speed limit and alerted the operations manager.

We also instituted a defensive driving course with additional training in safe driving. Although some satisfactory programs were in place, they were not up to best practices.

We placed all the risks we identified, measured, and prioritized in an implementation schedule. Following conversations with the insurance companies, we reprioritized a couple of the risks to make the insurance companies more comfortable with the overall risk of the company.

By addressing the fleet issues first, we could make this company more attractive to the insurance companies and obtain quotes on their behalf to reduce their auto premium by almost $81,000. The quote they accepted was about $114,000 less than the same insurance company unsuccessfully provided the prior year.

Even though we are discussing vehicles here, looking at their workers' compensation loss runs, you could see that many of their workers' compensation claims also came from their drivers. Injuries from loading and unloading and motor vehicle accidents were a big concern to the insurance companies.

By addressing the vehicle issues, we also made this company more attractive to the workers' compensation insurance company. We enabled the underwriter to justify a 23% lower quote than the year before. This resulted in more than $93,000 in savings over the previous year's policy. This reduction was even more important to this employer as their experience modifier was actually increasing due to their past claims history.

After identifying these risks through risk management and HR assessment, we installed the Risk Profile Improvement Process and

reduced insurance costs by just over $174,000 in less than six months.

Summarizing this example to demonstrate my premium theorem:

Your claim costs over 5 years	+	Perception of additional potential risks and claims	–	Perception of how much you improved your risk and addressed claims over the past year(s)	=	**Your Risk Profile and Premium**

Claim Costs—The insurance companies paid (including reserves) $547,000 in wages and medical costs for workers' compensation injuries over five years and almost $228,000 in vehicle accidents.

Plus (+) Potential Injury Perception—Due to past claims history and prior poor motor vehicle reports of the drivers, the underwriters were concerned that there would be a catastrophic vehicle accident leading to a $1 million or even greater lawsuit. They were also concerned about the likelihood of an employee being injured in an accident or from a serious back or shoulder injury from loading or unloading that would end up lasting years or even go into litigation.

Minus (-) the Improvements—Underwriters believed the business implemented better driver screening, including removal of poor drivers, a fleet safety program, defensive driving training, enhanced training on loading and unloading, and improving their return-to-work controls.
Equaled = An Improved Risk Profile and a 24% reduction in premium. The underwriter believed that the improvements made more than compensated for any potential risks the underwriter perceived, enabling the underwriter to underwrite to a 35% loss ratio instead of a 25% loss ratio. The dollar amount of the losses did not

change; only the perception of the risk did, which led the underwriter to the comfort level, enabling a premium reduction.

You must be able to go beyond just saying you made these improvements; you need to be able to tangibly show and demonstrate that the changes were made and that they were meaningful. This example shows that small changes can have a considerable effect. Since then, we have installed additional programs based on the identified risks, resulting in an extra $78,000 premium savings the following year.

Focusing on all stages of the risk management cycle: identifying, prioritizing, and mitigating risks; created a feeding frenzy in the insurance marketplace for this insurance program. You, too, can achieve similar results by going through the entire Risk Management Process with your organization.

Still skeptical about *Risk Profile Improvement*?

Let us look at this from a different angle. It may be something you are probably familiar with when receiving quotes - **Schedule Credits.**

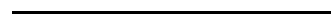
Most states allow insurance company underwriters to vary the premium they can charge you for your operations through Schedule Credits. These are subjective credits or debits (surcharges) an underwriter uses based on their perception of your *Risk Profile*. They are based on your risk control management experience, safety program, hiring practices, etc. Typically, the maximum credit or surcharge an underwriter can apply is 25%. To assist underwriters, the Pennsylvania Compensation Rating Bureau even goes so far as to offer a suggested Risk Characteristic Chart in Pennsylvania's state workers' compensation manual. They identified the following risk characteristics for the assignment of credits or debits subject to the maximum range of 25%:

Features of Workplace Maintenance or Operation	-10% to +10%
Risk Elements Not Addressed in Classification Plan	-10% to +10%
Availability of Medical Facilities in or Near Workplace	-5% to +5%
Safety Equipment/Devices Present in/Missing From Workplace	-5% to +5%
Extraordinary Safety Programs Applicable to Workplace	-5% to +5%
Qualifications of Employees	-10% to +10%
Accommodations/Cooperation with Carrier by Management	-5% to +5%
Considerations Related to Policy Expenses	-5% to +5%
Other Risk Characteristics Not Addressed Above (Specify)	-10% to +10

The Pennsylvania Manual goes on to state, "Schedule rating adjustments for any given risk shall be based on information contained in the carrier's files and records when the credit or debit is determined, and such supporting information must be retained in the carrier's files and records for such risk throughout the period of time in which the policy is subject to audit under provisions of the policy."

In other words, the underwriter must have documentation as to why they are applying credits or surcharges to your policy. This is where your *Risk Profile* can significantly impact your premium, good or bad. As the credit or surcharge is subjective, it is essential for you to provide documentation that the underwriter can clearly see and use to justify why and how much they are using as credits on your policy.

So I ask, again, what is your *Risk Profile*?



Do You Really Want To Gamble On Your Insurance?

As a successful business owner, why would you keep rolling the dice when it comes to managing your insurance program? Constantly frustrating yourself chasing quotes through the broken insurance industry bidding process? Leaving the determination of your premium up to the insurance industry with their "hard" and "soft" market cycles? Only you can answer these questions. But you can take some comfort in knowing that you are not alone.

Nearly 30 years of experience has shown that *the most successful* business owners do not allow their results to be left to chance. They have found that by better managing their organizations, they become more *attractive* to insurance companies and earn significantly lower premiums. Using these little known management secrets, they have made their companies more productive, profitable and enjoyable.

Inside these pages you will find out how to stop gambling as the way to reduce your insurance premiums, and learn how to put yourself *in a winning position where you ultimately control the game.*

ABOUT THE AUTHOR

"I've been working with David for over 10 years, his most recent book completely captures what every business owner needs to know to achieve ultimate success in the insurance world and improve their business operations at the same time!"

Steven A. Stramara, Sr. Vice President, The Seltzer Group

"David's first book, 'Frustrated & Overcharged,' was the best one I ever read about ways to control your Workers' Compensation costs. Even though the book was designed for employers, there was so much to learn from an agent's perspective. I am now looking forward to reading his latest book."

— Bruce C. Dolin, Dolin Insurance Associates, Inc.

"It was very informative and easy to understand for someone who isn't well educated on the complexities of workers comp. It made me realize the importance of managing claims, which nobody had ever explained. Needless to say, that's a major issue for an employer. It was an eye opener."

Amy Scarnati, Vice President, Double Nickel Delivery II Inc

"What a great book!! The entire book is easy to read and you gave quotes, stories and other real life examples. I especially liked the behavior based (employee management) program approach."

— Rosann Linza, Director, Human Resources, Bolttech Mannings Inc.

David R. Leng, CPCU, CIC, CBWA, CRM, CWCA

David Leng is the author of *Stop Being Frustrated & Overcharged,* and is Executive Vice President of the Duncan Financial Group in Irwin, PA. He is a 25-year veteran of the Risk Management and Insurance industry and is regarded as one of the brightest minds in the industry. Since 2004, David has saved his clients well over $60,000,000 in premiums and overcharges. David was named Advisor of the Year for 2008 by the Institute of WorkComp Professionals and is a frequent contributor to *Workers' Compensation, Dynamic Business,* and *Environmental Health & Safety* magazines, and many other publications and association newsletters. David has also been a presenter at multiple group and association conferences and workshops across the country.

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