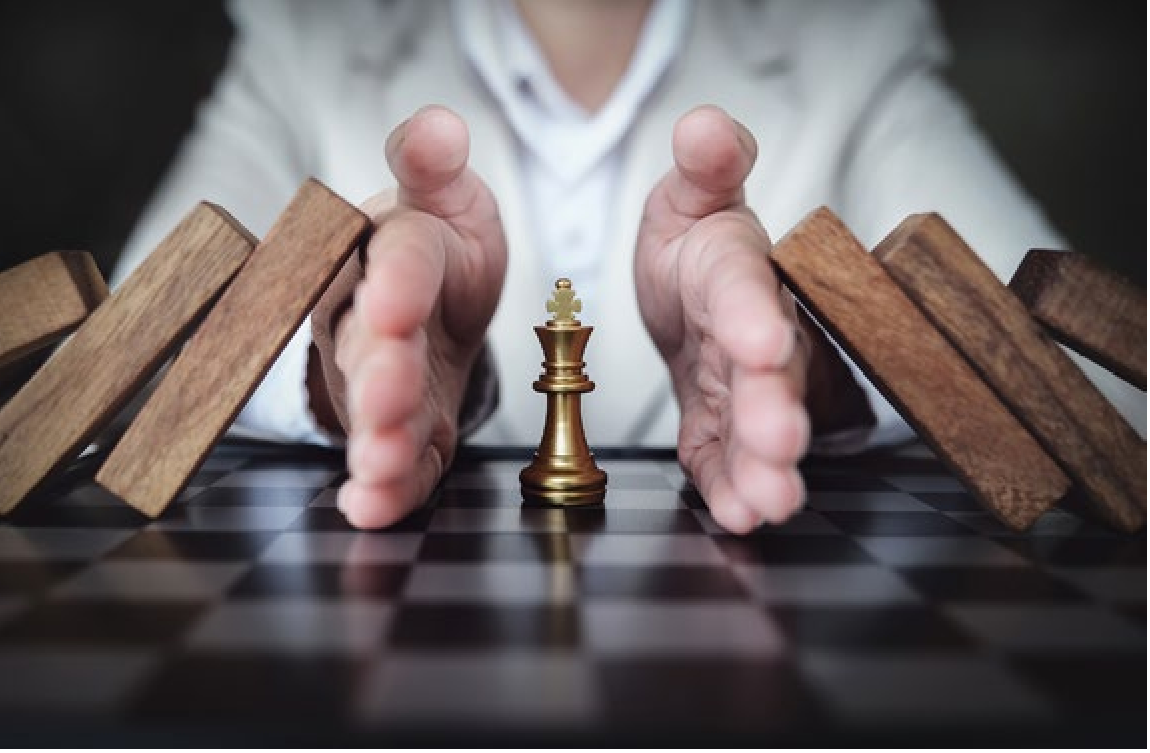

RISK MANAGEMENT IN THE TIME OF COVID-19

Written by Karrie Hyatt

Risk management for every type of company is changing more quickly than ever before due to the novel coronavirus pandemic. Companies are facing new risks that need to be covered by insurance as well as finding gaps in their existing coverage that is leaving them exposed in a way that was unthinkable at the beginning of the year.

Risk managers are having to work to keep up with the rapid changes that COVID-19 is creating. Right now, they are looking for ways to optimize their current risk while also looking ahead with what they have learned now to mitigate future disruptive events.

According to Karin Landry, managing partner for Spring Consulting Group, "COVID-19 has created some of the most difficult challenges the industry has seen in quite some time, so some of our most worrying 'ifs' have been become more real 'whens.' Companies who had never invested in risk management before will start to do so. Those that already had a program will look to make it more robust, and have it play more of a central role in overall organizational strategy. Enterprise risk management will see an uptick. Both employers and carriers will be looking for ways to add additional coverage like business interruption. Captives will be a big part of this shift, as they allow for more customizable coverage and cost savings opportunities."

“Risk management, to a large degree, is basic blocking and tackling,” said Harry Tipper, chief operating officer-insurance, CaptiveOne Advisors LLC. “It’s trying to anticipate the things that might disrupt your business and, then, trying to figure out how you might mitigate them or eliminate them. Most times the decision is how to mitigate them. In a few cases ‘bad things’ are going to happen no matter what you do; so, you look to see how you either might transfer the financial risk (that is, buy commercial insurance) or how to finance the financial risk (that is, self-insure or form a captive insurer).”

For Michael O’Malley, senior vice president and managing director with SRS, for his clients, which include many nursing homes, “The business model has evolved and there is even more focus on risk management now. A lot of businesses are being forced to change while dealing with a unique crisis.”

He offers the example of nursing home clients that finance both workers’ compensation and professional liability in their captive.

“They have been impacted, from a risk management prospective, by potential employee exposures while at work. In some states, there is an assumption that the employee was exposed while at work, so it is compensable under the workers compensation program. For employees exposed outside of work, there is the risk to patients from an asymptomatic spreader resulting in exposure under the professional liability coverage. Nursing homes must now develop additional testing, affectively testing employees upon arrival. From a risk management perspective, it’s been a dramatic change.”

RISK MANAGEMENT AND NEW EXPOSURES

"I can say that for most captive owners," said Tipper, "COVID-19 has made things very interesting."

The pandemic is revealing shortfalls and gaps in insurance coverage for many captive owners. Ranging from business interruption to workers' compensation to cyber security, even companies with detailed risk management plans are finding exposures where before the pandemic risk they seemed to be adequately covered. COVID-19 also revealing how crucial it is for risk managers to be on top of exclusionary language in policies.

Business interruption liability is at the top of everyone's exposure list. The risk is often well insured but, as many insureds found out when the "shelter-in-place" order went into effect, that business interruption due to pandemic was excluded from their policies.

"As a business owner, how do you deal with the fact that you have to shut down your business—not from a hurricane or something that damages your physical business but from a civil order that forces you to stop doing business?" asked Tipper. "As many are learning to their dismay, standard business interruption insurance doesn't handle that. On the other hand, and with some forethought, properly structured captives could provide a short term back stop."

Tipper continued, "Here is another aspect of risk management. How much will captive insurance take care of the essential things of the business, but at a level where you don't wipe the captive out financially with this one risk. Here we care talking about the risk management of captive's solvency."

Another exposure is potentially being liable for an employee or a customer's exposure to COVID-19 and the expenses involved for contact tracing. For risk managers, the question comes down to how much should a company spend on prevention and containment of exposures versus the cost of the risk.

"When you're a public facing business, such as a restaurant, managing risk from COVID-19 becomes harder. For example, you have little or no ability to find out who has been in contact with whom, to do contact tracing," said Tipper. "There's that whole issue of do you have legal liability because one of your customers has come down with COVID? That's yet to be seen if you do or how much since there is little judicial guidance in this regard."

According to Landry, medical stop-loss coverage is trending for captives as employers do not want to just give captured profits back to the carriers. The pandemic has seen new medical technology, such as telemedicine, come to the forefront, bringing with it its own set of risks. Health plan premiums are expected to rise as a response to the pandemic.

"A global health crisis like this gives new meaning to the phrase 'catastrophic claims,' and organizations want to make sure they can look out for their workforce and offer solid benefits that they can afford, while protecting themselves against future unprecedented events," said Landry.

With the rush to shutter business offices in March, many companies were forced to create ad hoc plans for cyber security for their employees working from home. Some companies had been operating from a policy where their employees could work from home a few days a week, and had appropriate security measures in place. However, most companies found that from a security standpoint they were not ready to make the transition.

"Larger companies can handle cyber risk better than the smaller 'Main Street' businesses. For example, before they sent employees home to work remote, some of the larger companies were able to give them laptops that had been vetted for security from their IT department, hence mitigating the risk of cybercrimes," said Tipper. "On the other hand, the average 'Main Street' businesses are hoping that a commercial cyber security product such as Norton and Lifelock will do the job; because, they don't have an IT department to provide the heavy stuff—cyber security."

"Because of some gaps in cyber security coverage from traditional insurance policies, insureds don't feel secure in terms of the insurance coverage being comprehensive. We've had clients move their cyber coverage into their captives so they could control the policy language and breadth of coverage while using the captive to access reinsurance," said O'Malley.

Employees working from home also revealed how little risk managers had thought about telecommuters and workers' compensation. "Workers' comp has seen a great shift in exposure and a gap in coverage. With many people working remotely, an injury that takes place in a home office could potentially yield a claim, but some organizations may not have appropriate coverage," said Landry.

"Companies are now looking at captives as the over-arching insurance instrument," continued Landry. "We have a client who got sick and said the employer did not take enough cautionary measures to keep him/her safe. If that person files a claim—is that a workers' compensation or a disability claim? It often is unclear who owns the claim. We are seeing companies turn to captives for this reason—a claim that doesn't fit anywhere else can fall to the captive."

INCREASING INTEREST IN CAPTIVES

Captive professionals are seeing a marked increase in interest in captives. This was expected at the beginning of the year as the market was hardening, but a lot of the current interest is due to new exposures created by the pandemic and risk managers scrambling to get adequate coverage.

When asked if he had seen an increase in captive interest, O'Malley answered, "Yes, and it's dramatic. The umbrella market has hardened significantly, so we are seeing lots of opportunity where our existing group captives are increasing their retentions to push the umbrella attachment higher while expanding the primary layer and financing the additional risk in their own captive. There is just an overall increase in captive interest with insureds wanting to consider a captive."

Landry has also seen an increase of interest in captives—both new captives and expanding established captives. "At the beginning of the year, captive owners had a different perspective—they were looking to maximize their capital for underwriting purposes and add lines of coverage. When COVID hit, and carriers were already starting to increase premiums, they began to look at it differently."

"Employers became concerned when they started seeing areas that their policies didn't cover—like business interruption for COVID exposures," Landry continued. "Then they began to ask about captives for different reasons. For those folks who didn't have captives, they were asking because they were realizing they had these uncovered exposures and were asking what they could do to minimize their costs. A captive can play a great role if the coverage is not available or unaffordable."

"It's a very robust time for captives, insureds are looking for alternatives to access capacity and finance their risk," said O'Malley. "Due to the impact of COVID on the overall economy, we were thinking that captives demand might lessen, but because of the hard market it's actually been the reverse. There's been a real demand and real interest in studying the benefits of a captive focused on increasing overall program control." ■

Karrie Hyatt is a freelance writer who has been involved in the captive industry for more than ten years. More information about her work can be found at: www.karriehyatt.com.