MULTINATIONAL POOLING IN TODAY’S CLIMATE: Seven Steps to Keep You on Track

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The business climate has undergone dramatic change in the last six months, increasing pressure to cut costs across the board. This is an ideal time for companies to examine whether their existing multinational pooling arrangements are delivering the maximum savings, or whether a multinational pooling arrangement is now the best option.

Multinational pooling arrangements involve “pooling” multiple insurance contracts around the globe to minimize risk. They help companies save money and optimize cash flow. If a surplus remains from the premium from local insurance contracts, after deducting all claims, administrative expenses, insurer risk charges, etc, it is returned to your company via an international dividend payment.

A general rule of thumb is that multinational pooling arrangements can return 8% to 12% of premium via the international dividend. This can run as high as 11% to 19% with a captive pooling arrangement, described below. Of course, the experience of the insurance contracts factors into the dividend results and can vary from year to year. But companies can see significant results from concerted efforts to maximize the financial results of their multinational pools.

Given the current environment, companies need to be aware of what has changed relative to their multinational pools, including the financial stability of their network partner, as some insurers’ ratings will have changed.

Here are seven steps to make sure your multinational pool is in line with your business strategy and risk tolerance.

**STEP 1 — EVALUATE HOW YOUR BUSINESS HAS CHANGED IN THE LAST SIX MONTHS.**

What has changed in your approach to employee benefits? Have you made acquisitions, opened up new offices, closed offices, added new lines of coverage, or expanded coverage in some countries? Have you added any new pools, perhaps due to forming a natural pool of contracts in one of your networks?

Examine the experience of the local insurance contracts. Have they run deficits for more than a year? If so, they may be contributing negatively to the overall results. Perhaps you should consider moving them out of your pool.

You may have outgrown the financial vehicle for your pool. For example, you may have started out with a small number of countries and used the small group pooling arrangement of an international network. Now that your business has grown, the pool may be much larger, but the international dividend may still be limited to a percentage of the surplus. In this example, you would need to move from a small group pool to a Loss Carry Forward basis.

**STEP 2 — DETERMINE IF YOU CAN ASSUME MORE RISK.**

Are you capable of assuming more risk in your financial pool, or have you had negative results that might cause you to want to reduce your risk? By increasing the risk, you will reduce the risk charge, which is a reduction from the available surplus.
Conversely, when you reduce the risk, you increase the risk charge, so it is important to find the right pooling structure that fits with your corporate philosophy. You may want to examine Full Stop Loss or Loss Carry Forward, or a Loss Carry Forward with a write off within 3 years or 5 years. There are a number of alternatives that you can explore with the networks; ask them to give you quotations on several scenarios.

**STEP 3 — EVALUATE YOUR MULTINATIONAL POOL USING AVAILABLE RESOURCES.**

Look at the annual reports from your pooling networks for the past three years, which will provide a good source of data. If you have several multinational pools, would it be smart to consolidate the pools into one? Is the pooling network (or networks) still the right one for your business? Could you enhance your current financial arrangements in the pool, or have you outgrown it altogether?

Next steps include:

- Develop a global benefits inventory, listing all the employee benefits policies that you have around the world—those that have already been pooled and those that have not.
- Determine if additional contracts in the global benefits inventory may be incorporated into your pool by evaluating if the coverage is “poolable” (suitable for pooling) for the respective country. The insurance networks will be happy to provide a list of what coverages are poolable where.
- Evaluate the strength of the local carriers of the international networks. A number of insurers have had their financial ratings change recently due to the financial crisis. Taking a fresh look at these revised ratings is very important.
- Examine the pooling network’s carriers as a whole. This can be part of an overall carrier evaluation. One way to do this is to rank each of the local carriers according to financial stability, price competitiveness, and administrative capabilities. A common methodology is to assign a numerical rating to each of these three areas and develop a matrix showing the pooling networks, based on the aggregate results of the local carriers’ evaluations.

**STEP 4 — OPTIMIZE CASH FLOW.**

Although receiving a large dividend at year-end can be seen as good news, you are in fact lending money to the insurance company and getting it back 18 months later, together with a conservative interest rate. This is comparable to receiving a large tax refund; it is good news, but you could have kept this money invested in your company. There are various cash-flow techniques that can better match the timing of the premium payments with the claim payments and optimize cash flow: advanced dividend payment, premium drag, reserve reduction, terminal retro and hold harmless agreements. These are essential in today’s environment.

**STEP 5 — DEVELOP AN RFP AND SUBMIT IT TO THE APPROPRIATE POOLING NETWORKS.**

If you have decided that you’d like to review your existing pooling arrangements or establish new ones, the next step is to develop a Request for Proposal (RFP) and submit it to the appropriate pooling networks.

There are approximately nine multinational pooling networks in the world. You should select those that are most appropriate for the geographic spread of your company as well as those that provide the best local service. Sending an RFP to all pooling networks creates unnecessary work, so it is important to research the networks in advance.
You must provide the networks with the appropriate plan descriptions for the coverage that you want quoted on and your premium and claims information.

Next, outline the financial arrangements you want quoted, and specify the level of limits you want on individual claims and the overall aggregate loss.

Finally, develop a questionnaire on the networks’ experience, local insurers, financial arrangements, captive arrangements, etc.

Once the RFP responses come in, the real work begins. You must analyze the results, select finalists, conduct finalist interviews, chose the network, then begin the implementation process. Key to this step is moving contracts to the network’s insurers to add coverage to your pool, or to start a new pool.

**STEP 6 — CONSIDER THE PROS AND CONS OF A CAPTIVE POOLING ARRANGEMENT.**

If your company is large enough, has a minimum of 3,000 lives available to pool and $2 million in poolable premium, review the pros and cons of captives. Under a captive arrangement, the local policies’ risk in the pool is either partially or completely ceded to a captive, depending on pool agreements and local regulations. Therefore, risk fees associated with the pool are either reduced or eliminated.

Reinsuring a pool back to a captive can save 3% to 7% of premium in addition to the savings that pooling may already provide. But remember that with a captive, you are assuming the role of an insurance company. Ask yourself:

- Is the risk/reward ratio high enough?
- Do you have the internal expertise to manage a captive?
- Are you prepared to assume the administrative duties of running a captive?
- Will you be able to secure stop-loss coverage for the captive?

There are also several important related advantages to including benefit premiums in a captive. The use of employee benefit premiums can help the risk manager reduce and diversify the overall risk of the captive. There can be significant tax advantages (employee benefit premiums are considered third-party business under the US tax code) if the company has unclaimed tax deductions for general insurance premiums. Finally, the captive can be an important instrument to ensure the execution of your governance structure.

**STEP 7 — SEEK OUTSIDE HELP IF NEEDED.**

If you feel you don’t have the expertise to complete the steps above and need outside help, a global benefits consultant can assist you in several areas:

- Gathering the data on all your global employee benefit plans from a number of different sources, such as your local contracts, local brokerage operations, the pooling reports, and the pooling networks themselves.
- Developing the RFP and sending it to a number of networks that provide the pooling arrangements most appropriate for your global presence, maximum potential premium, number of contracts, and ideal financial arrangements.
- Helping you chose which networks to approach. He or she will know the global footprint of the networks, the financial strength and service abilities of the carriers, and overall experience in dealing with a company like yours.
• Assessing and negotiating the appropriate financial arrangements that the networks should provide quotes for—and the questions to ask about their services.

• Assisting in implementing optimal cash flow techniques.

• Evaluating the strength of the local carriers in the international network, ranking each according to financial stability, price competitiveness, and administrative capabilities. (A common methodology is to assign a numerical rating to each of these three areas and develop a matrix that evaluates the pooling networks based on the aggregate results.)

• Analyzing the RFP responses and selecting the finalists. He or she can help arrange the finalist interviews and assist you in determining which network best meets your overall needs.

• Determining whether you qualify for utilizing a captive to cede all, or part of, the risk associated with the local insured policies to a company-owned captive insurer, and whether the additional risk and administrative work is right for your company. Captives are not for every company—even those that have large numbers of employees and poolable premium. Utilizing a captive arrangement must fit with your company’s philosophy, risk tolerance, and internal expertise.

Contact

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Aon Consulting is among the top global human capital consulting firms, with 2008 revenues of $1.4 billion and 6,000 professionals in 117 offices worldwide. Aon Consulting is shaping the workplace of the future through benefits, talent management and rewards strategies and solutions. Aon Consulting was named the best employee benefit consulting firm by the readers of Business Insurance magazine in 2006, 2007 and 2008.